Industrial Change in China

Economic restructuring and conflicting interests

Kate Hannan

Routledge Studies on China in Transition

ROUTLEDGE

Industrial Change in China

At the Fifteenth Party Congress held in October 1997, China's leaders confirmed their intention to effect state enterprise ownership reform. As a result many state enterprise workers now face the prospect of losing their jobs. This will test the tolerance of the urban work-force and may challenge the political authority of China's leaders.

This book analyses the industrial reform measures taken by the Chinese government during the decade 1985–95 and identifies the economic and political tensions and contradictions that state enterprise reform has presented to a leadership intent on maintaining its authoritative political position. Using government sources and interviews with economists and workers at one of China's largest state-owned enterprises (the Second Automobile/Dongfeng corporation), Kate Hannan concludes that the relationship between state policy and enterprise is a complex two-way process characterised by tensions resulting from conflicting priorities.

Kate Hannan is a Senior Lecturer in the Department of Politics, Macquarie University, Sydney.

Routledge Studies on China in Transition
Series Editor: David S. G. Goodman

1 **The Democratisation of China**
He Baogang

2 **Beyond Beijing**
Dali Yang

3 **China's Enterprise Reform**
Changing state/society relations after
Mao *You Ji*

4 **Industrial Change in China**
Economic restructuring and conflicting interests
Kate Hannan

5 **The Entrepreneurial State in China**
Real estate and commerce departments in reform era Tianjin
Jane Duckett

6 **Tourism and Modernity in China**
Tim Oakes

Industrial Change in China

Economic restructuring and conflicting interests

Kate Hannan

ROUTLEDGE

London and New York

First published 1998
by Routledge
11 New Fetter Lane, London EC4P 4EE

This edition published in the Taylor & Francis e-Library, 2002.

Simultaneously published in the USA and Canada
by Routledge
29 West 35th Street, New York, NY 10001

British Library Cataloguing in Publication Data
A catalogue record for this book is available from the British Library

Library of Congress Cataloguing in Publication Data
A catalogue record for this book has been requested

ISBN 0-415-16246-7 (Print Edition)
ISBN 0-203-02100-2 Master e-book ISBN
ISBN 0-203-20942-7 (Glassbook Format)

Contents

Series preface

In the late 1970s, as China's reform era opened, the Communist Party of China committed itself to first doubling and then redoubling the aggregate size of the economy of the People's Republic of China by the end of the millennium. At the time and into the early and mid 1980s it was a prospect greeted as a desirable aspiration by most academic observers of China, but as little more. Many economists in particular pointed out the difficulties in the project and the near-impossibility of its achievement. In the event the target was attained with almost five years to spare, sometime in 1995.

The rapid growth of China's economy is a useful starting point for this series, intellectually as well as chronologically. It is not only that China has developed so spectacularly so quickly, nor that in the process its experience has proved some economists to be too cautious. Rather its importance is to demonstrate the need for explanatory theories of social and economic change to themselves adapt and change as they encompass the processes underway in China, and not to assume that previous assumptions about either China or social change in general are immutable.

China in Transition aims to participate in these intellectual developments through its focus on social, political, economic and culture change in the China of the 1990s and beyond. Its aim is to draw on new, often cross-disciplinary research from scholars in East Asia, Australasia, North America and Europe, as well as that based in the more traditional disciplines. In the process the series will not only interpret the consequences of reform in China, but also monitor and reflect the changes of the future.

The 15th National Congress of the Chinese Communist Party held in September 1997 once again highlighted the importance of China's state sector enterprises to the whole transformation project through its announcement of further reform. State sector enterprises are obviously economically important. Many are woefully inefficient and technically bankrupt. At the same time many – quite deliberately – are strategically significant enterprises particularly in the heavy industrial sector and in primary industry. As was intended through the new policies announced at the National Party Congress the state sector enterprises have to be commercialised and made more subject to the market if they are to fit into and be a complementary part of the evolving economy. However, state sector enterprises are also politically important. They employ a considerable proportion of the most articulate urban workforce and have in the past performed a significant range of welfare functions. Drastic 'down-sizing' in the fashion of early Thatcherite Britain is not an option for the leadership of any individual state sector enterprise, let alone of the Chinese Communist Party.

Kate Hannan's study of the reform process at the Second Automobile Corporation is remarkable for its access to the dynamics of change in one state sector enterprise. It highlights the dangers and uncertainties – for both workers and managers – in the drive for enterprise reform without adequate macro-economic controls; it is cautious rather than pessimistic about the possible outcomes but mainly for political and not economic reasons. Hannan acknowledges the economic pressures – particularly as they impact on enterprise managers – that will create greater urban unemployment as state sector enterprises are restructured. The pressure – particularly on the workforce – to reach newly defined corporatist solutions will be high – as in the Second Automobile Corporation. Yet at the same time there is a calculation that increased consumerism and sustained economic growth will offset the more obvious yet localised discomforts that will also occur.

David S. G. Goodman

Institute for International Studies, UTS

November 1997

Preface

My research for this book is based on two complementary but discrete primary sources. The first consists of policy initiatives and economic concerns outlined and publicly debated in officially recognised economic journals and newspapers. The second is a study of the effects of reform policy on the decisions made by the managers of one of China's large, economically advantaged state-owned industrial enterprise groups – the Second Automobile/Donfeng corporation. My first source has provided information for the macro-level dimension to my analysis and my second grass roots source has illustrated the manner in which macro-level industrial policy has been implemented. It throws light on the way that the managers of China's large advantaged state-owned industrial enterprises sought to satisfy their own interests and those of 'their' enterprise while being party to a process that has seen an ever-growing opposition of interests not only between themselves and Party policy-makers and administrators, but also between themselves and 'their' industrial workers.

My first source includes respected Chinese economic journals (for example, *Zhongguo gaige* [*China Reform*], *Jingji guanli* [*Economic Management*], *Jingji yanjiu* [*Economic Research*] and *Caimao jingji* [*Finance and Trade Economics*]) and other responsible, Party approved, sectors of China's print media, particularly the Party's official mouthpieces, *Xinhua* (*New China*) and *Renmin ribao* (*Peoples' Daily*). The information that I gleaned from these sources was deepened by information given to me in interviews that I conducted in 1988, 1989 and 1994 with economists from the Industrial Economics Institute of the Chinese Academy of Social Sciences. A brief October 1989 interview and lunch with Ma Hong, the then president of the Academy of Social Sciences, also served to increase my understanding of the Chinese government's macro-economic policy.

My second line of enquiry and source of research information began with a 1985 stint living and working at the headquarters of China's large and very successful state-owned enterprise – the Second Automobile/Dongfeng corporation. I made a number of valued friends among the members of the management and developed *guanxi* (personal connections). Since 1985 I have returned at regular intervals and managers and economists from the corporation have generously and willingly given their time for interviews. This means that I have been in the privileged position of having had a rare glimpse into the grass roots processes and effects of China's industrial reforms.

The Second Automobile/Dongfeng corporation is typical of many of China's largest, most economically advantaged state-owned enterprises. These enterprises have been and still are at the cutting edge of reform. They are used as reform 'laboratories'. China's leaders have consistently chosen enterprise groups such as the Second Automobile/ Dongfeng corporation to trial specific industrial reform policies such as the earliest mode of wage reform, labour, housing, welfare and taxation reforms, joint production arrangements and the privatisation programmes that are currently underway. The managers of the Second Automobile/Dongfeng corporation have already implemented policies that will soon divest the corporation of all its housing and worker welfare responsibilities. Privatising social and welfare provisions, like the practice of labour contracting, is well advanced. However, the managers of China's advantaged state-owned enterprises have not only been the conduits for central government reform initiatives, they have also used the process of reform. As I will argue, they have taken advantage of the process of reform in order to husband resources for 'their' enterprises and for 'their' workers. Indeed, their own success and status have been predicated on their ability to promote the interests of their 'kingdom'.

As China's industrial reforms took hold, the Second Automobile/ Dongfeng corporation developed quickly until its total labour-force consistently numbered between 250,000 and almost 300,000 workers. The conglomerate now has factories or owns shares in factories and corporations that are scattered all over China, but when it began its vehicle manufacture it was located only in the mountainous north-eastern sector of Hubei province. The corporation's headquarters is still located in this same remote area. It is in the town of Shi-yan (see following map). Those who have worked at the corporation since it began production are fond of telling visitors that until the vehicle manufacturing plant was located in what had once been this small market-town, the area around was not only very poor, but so isolated that the people in the valleys that the town serviced had only two family names.

In the last years of China's Cultural Revolution manufacturing plants, including the factories and administration that were to become the Second Automobile/Dongfeng corporation began to be established in this unlikely poor and remote region. The idea was that military hardware could be produced in an area that was deemed to be safely 'away from the [Soviet] enemy'. As a consequence, the region included a number of munitions factories and other so-called 'third front' military industries. This meant that even as late as 1985 it continued to be subject to restricted entry. When I wanted to walk in the surrounding mountains while working at the Second Automobile/ Dongfeng corporation I was told that the restrictions governing the area would not allow this and one person even went as far as pointing out that if I was silly enough to ignore this warning, then, the tigers lurking in the mountains would surely cause me some terrible damage.

The forerunner of the Second Automobile/Dongfeng corporation (simply known as the *Erchi*, or number two factory and then as the Second Automobile works in contrast to the First Automobile works situated in the north-eastern city of Changchun – Jilin Province) derived considerable benefit from the 1978 adoption of Deng Xiaoping's programme for economic reform. This programme quickly ensured that China's state-owned industrial units had much greater discretionary money available for the acquisition of plant and equipment, including motor vehicles. The Dongfeng (East Wind) trucks manufactured by the Second Automobile works became particularly popular among these 'purchasers'. There were long waiting lists for the trucks produced by the works. The trucks were seen to be much more modern in terms of their design than those manufactured by China's older First Automobile works. Soon it was a combination of state-owned industrial enterprises and increasingly wealthy peasant households, rather than the Chinese army, that were the Second Automobile's largest 'customers'. Today, the Second Automobile/ Dongfeng group manufactures a wide variety of Dongfeng trucks, buses, vans, engines and a range of other automotive parts and light vehicles, including a small Citroën sedan. The latter is produced under the auspices of a Sino-French joint venture referred to as the AeolusCitroën Automobile Company and now the Dongfeng-Citroën Automobile Company. The partnership that supports this car manufacturing project was initially facilitated by the enticement of soft French government loans. It took some time (more than six years), but the French interest in the group's car manufacturing projects now appears to be paying off. The French company now has immediate access to China's domestic automobile market.

In contrast to the mature European and American markets where buyers only replace motor vehicles, the Chinese market is predicated on a population whose rising affluence spells rapid market growth and expansion. It presents a 'brave new world' for both European and American car manufacturers, though their investment caution should not be completely abandoned. Today, the promise of household ownership of a car has become a part of the vision of modernity that in turn supports the Chinese leader's political authority. However, sales of sedans for individual use are slower than expected. The income of China's industrial workers and the private vehicle ownership dream presented by their leaders have not operated in concert. Nevertheless, the industrial priority status that China's leaders give the Second Automobile/Dongfeng group is a vital component of the group's continuing position as an advantaged and very successful corporation.

Recently the Chinese leadership has allowed the corporation's managers to list Second Automobile/Dongfeng group shares on the Hong Kong stock exchange. This is a privilege that the élite afford to their most prestigious state-owned enterprises. The shares of these enterprises are bought by so-called 'international' investors, primarily, indeed almost exclusively, on the basis of faith. At the same time as the Second Automobile/Dongfeng group had been allowed to list shares on the Hong Kong stock exchange and there had been some talk of listing group shares on the New York exchange, the group's books, however, were not showing a profit. Indeed, the corporation was 'running in the red'. In other words, it was showing a loss. The economic value of the group is not encoded in its bottom line, it lies in its potential and in the context of the Chinese élite's concern to promote private motor vehicle ownership as a part of the dream of modernity offered to their constituent workers.

Acknowledgements

There are a number of people I would like to thank for their support while I have been researching and writing this book. I would particularly like to thank Ji Jun and 'Mrs Ji' for their on-going kindness. They have been very welcoming whenever I have turned up on their doorstep. I would also like to thank 'Professor Li' and other Chinese friends, including those who were members of my 1985 'cadre's class'. Over the years a number of economists from the Second Automobile/Dongfeng corporation have willingly given me their time. They have patiently answered my endless questions.

In the early stages of my research for this book the Australian Research Council supported several of my visits to the Second Automobile/Dongfeng corporation and a number of later research trips were funded by the Macquarie University Research Fund. I thank both these bodies for their support and I would like to thank members of the Industrial Economics Institute of the Chinese Academy of Sciences for interviews that I conducted with them.

I would especially like to thank Professor David Goodman who supported this project at the time when I had written only the first sketchy outlines of the chapters. I am also grateful to my students at Macquarie University for their enthusiasm and ideas and I am particularly grateful to my family for their support and help. While I have been writing this book my partner Stewart Firth has taken on a good deal of the jobs that I would usually attend to and has even kept a telephone watch when I was stuck on a train in the snow in provincial China. I did not turn up at the expected time or even in the expected place. When I have returned home from visits to China I have talked endlessly about my experiences. My family have been willing to listen and Stewart and Michelle have even been willing to come with me. My daughters, Michelle, Kirstie and Nicole Hannan and Michelle's husband Dominic Moon and their little daughter Esther

Hannan-Moon, have put up with visits to their homes and telephone calls that have been much too short. Of course, none of these people are at all responsible for anything that I have said, the views that I have expressed or the errors that I have made. These are my own doing.

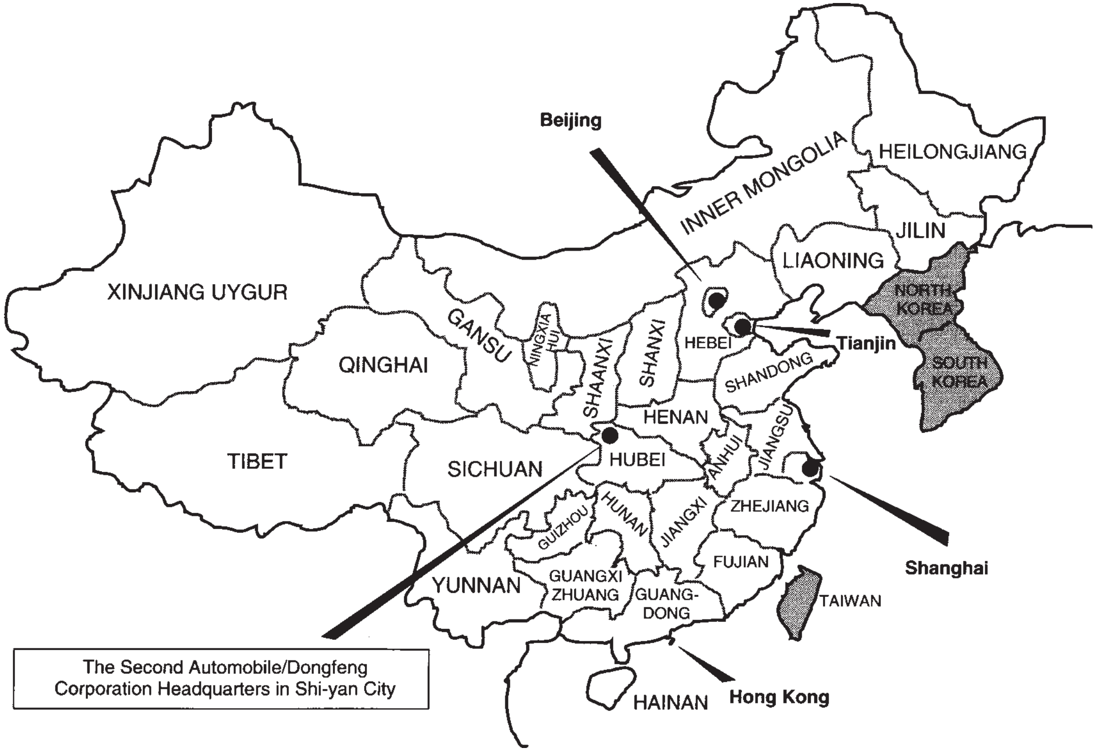

Figure 1 The People's Republic of China

Introduction

> The kind of socialism we are talking about is socialism with Chinese characteristics, and building socialism with Chinese characteristics is impossible without the Communist Party's leadership.[1]

This book surveys the economic change and social tensions that the recent process of restructuring China's state-owned enterprises has presented to a Party/state élite intent on maintaining their rule. While reform initiatives have changed and matured and economic and political interests and concerns promoted by the process of reform have been manifest in different ways, China's leaders have consistently sought to preserve their authoritative political position.

In 1985 when I began my research for this book I thought that I would limit my focus to the tension between the reform initiatives promoted by Party leaders and central government economists and planners on one hand and the concerns and interests of local government administrators on the other. Previous discussions that I had had with these parties alerted me to a mounting conflict in their relationship. I began by interviewing managers and economists from the Second Automobile/Dongfeng corporation because they were the leaders and decision-makers for a large centrally administered state-owned enterprise located within the geographic ambit of an administration (the Hubei provincial government) that had long been known for its proud independence from Beijing. I thought that my approach would leave me in a position to identify and discuss inter-governmental tension and conflict. It did. However, as soon as I began interviewing managers and economists from the Second Automobile/Dongfeng corporation I realised that the issues and contradictions thrown up by the process of industrial reform extended well beyond the growing tension between the central and provincial tiers of government. Moreover, these issues and contradictions were changing over time. They presented a moving feast. Faced with this situation, I elected to organise my research and later wrote this book surveying first one aspect of industrial reform policy and then another. In Chapter 1 I discuss the post-reform relationship between China's Party/state élite and local agents. The former consist of Party leaders, their policy advisers and the central government administrators who implement their policy and the latter consist of local government officials and the managers of large state-owned enterprises. In Chapter 2 I track the changing face of labour relations, the introduction of labour contracting and the erosion of manager/labour cooperation. In Chapter 3 I have concentrated on the reform choices open to China's leaders and the vexed questions associated with reforming the central government's financial levers – the banking, pricing and taxation systems. In the last chapter I have discussed the ownership reform recently sanctioned by the leadership's Fifteenth Party Congress.[2] This latest reform initiative is presented both as proof of the leadership's ongoing reform credentials and as a solution to the economic problems faced by China's state-owned enterprises. However, it must be implemented with considerable care.

During the latter half of the 1980s an opposition of interests between the managers of China's state-owned enterprises and their workers developed quickly, parallel to the already established opposition of interests between members of China's centralised Party/state élite and local agents. While I outline the development of this manager/worker opposition of interests and include a brief discussion of the dilemmas presented to China's Party/state élite by the prospect of an ever-growing number of urban unemployed in Chapter 2, it is not until the last chapter of this book (Chapter 4) that I discuss the issues that now flow from this tension.

Before turning to the social consequences of ownership reform, I found I must explain that while China's Party/state élite have now agreed that the goal of their reform is to promote a market-integrated economy, in practice they have had to continue to rely on administrative levers as a means of disciplining local level decision-making. This situation has left them with both a need for ongoing and clearly articulated reform credentials and a solution to the considerable economic problems exhibited by the state enterprises that, to date, have been the backbone of China's industrial production. It is in this context that they have turned to reforming the ownership profile of the state enterprises while recognising the wisdom of ameliorating the social costs extracted by reform, knowing the potential consequences of their decision and heeding those within their ranks who counsel caution. And at the same time, they have assumed that this reform initiative can be accommodated within the scope of their rule.

OPPOSING INTERESTS: BARGAINING, SOFT BUDGETS AND CHANGING INDUSTRIAL RELATIONS

The Hungarian economist Janos Kornai's 'soft budget' concept and his 'investment hunger' thesis have provided the theoretical starting point for my argument. Kornai offered useful explanations not only for the performance and economic decision-making taking place in centrally planned economies, but also for decision-making during the process of reforming these administrations.[3] My survey of macro-economic policy decisions and the interviews I conducted with economists and managers from the Second Automobile/Donfeng corporation revealed the steadily escalating process of bargaining and policy manipulation between those representing the Party/state on one hand and those representing local interests (both local government administrators and, I think even more importantly, state enterprise managers) on the other. I have concluded that this process derived from an existing opposition of interest within the Chinese polity that has been further nurtured by the process of industrial reform and fuelled by the soft budget constraint that had persisted throughout the reform process. The latter has been used by local agents whose economic decision-making has been driven by the nexus between success, status, growth and investment. What is more, as China's leaders promoted the process of restructuring the state-owned enterprise sector of the economy, the ever-growing opposition of interests between those acting on behalf of the Party/state and those promoting local agendas developed to the point where the élite's previous ability to maintain the appearance of a community of interests was undermined. And, there was more. A second line of conflict developed between state enterprise managers and their workers, even as managers continued to reward workers with large bonus payments, services and gifts.

When I have discussed the relations between managers and workers within the walls of China's state-owned industrial enterprises, I have begun from premises that couple Kornai's insights with those of the American Sinologist Andrew Walder. This combined theory has provided both a starting point and a contrast for my discussion of the changes in China's labour relations. In 1987 Walder published what was to become his much quoted article outlining industrial relations in

China's state-owned enterprises. He recognised that in the period immediately after the introduction of economic reform 'a tacit alliance [had] emerged between managers and workers, both of whom have an interest in retaining the highest amount of incentive [bonus and welfare] fund while distributing it relatively equally'. He reported on a collusive 'web of interests' that he found flourishing within China's state-owned enterprises. Walder's thesis was based on work that he had done at the Universities Service Centre in Hong Kong from June to August 1984 and at the Chinese Academy of Social Science's Institute of Industrial Economics from May to August 1986. In other words, it was based on research that he had undertaken immediately before the introduction of labour contracting into China's state-owned enterprises. Walder was disappointed with his findings. He argued that the cooperation and collusion he identified between managers and workers was confining the development potential of China's state-owned enterprises. Indeed, he presented his thesis as 'a problem for which no solution is currently in sight'. However, a 'solution' was in sight. Today, with the benefit of hindsight we can recognise first that the soft budget constraint that Kornai identified had operated at a particular point in China's programme for industrial reform and had facilitated the web of interests bemoaned by Walder, and second that the August 1986 introduction of labour contracting initiated a division of interests between factory managers and workers that was to flourish.[4]

TIANANMEN, RECTIFICATION AND THE QUESTION OF THE END GOAL OF REFORM

By the second half of the 1980s two lines of opposing interests were already evident within Chinese Society, one between Party/state administrators and local agents and the other between state enterprise managers and workers. Yet only one of these – the opposition of interests between those representing the Party/state and local agents – fuelled the urban unrest that culminated in the 1989 Tiananmen Incident. In other words, while the two lines of opposition coexisted, the older more established line (between central and local interests) was the one that promoted the events of 1989.

In the latter years of the 1980s the inability of China's leadership élite to press the interests of the Party/state in the face of the demands made by local agents did much to promote popular grievances. It was obviously in the interests of Party/state leaders to discipline the evermore strident investment demands made by local administrators and state enterprise managers, but they had been pressed to do this at a time when they were divided and disunited over the question of the end goal of reform. They failed to stand firm and their inability to manage the opposition of interest between themselves and local agents promoted both negotiation and manipulation of policy initiatives that often bordered on corrupt practices. And, probably even more importantly, led to an ever-rising rate of inflation. This situation in turn contributed to the grass roots concern and popular discontent of the period.

The Chinese leadership's response to the demands made by urban demonstrators is well known. People in the streets, both students and workers, 'requested' political reform and showed their disgust with both corruption and the rampant rate of inflation. First China's leaders used the army to repress any further expression of social dissatisfaction and then they sought to isolate the demonstrators by portraying them as irresponsible hooligans who would bring social and political chaos to China. They were now united by their need to make it clear no further overt challenge to the authoritative basis of their rule would be tolerated. Then, together with a campaign against corruption, they implemented a programme of economic contraction that would squash inflation. The programme gloried in the title of 'economic rectification'.

Under the auspices of rectification policy, China's centralised banking system was used to effect an abrupt and harsh reduction in available credit. The credit tap was firmly turned off. This is a very blunt economic tool. It does not recognise the economic viability of enterprise management decisions in terms of investment to profit ratio. It only recognises the negotiating ability and greater political sensitivity over closing or merging large advantaged state-owned enterprises with their large work-forces rather than the smaller, less influential state-owned enterprises, collectively owned and rural household enterprises. In the end and in spite of the heavy economic price China's smaller state- and cooperatively owned enterprises were made to pay, almost three years of rectification did slow the rate of expansion of productive capacity. However, it did this by merely squashing investment hunger and the ever-rising rate of inflation experienced in the second half of the 1980s. It did nothing to solve or even manage the underlying problem of lack of local government and state enterprise discipline in economic decision-making. What it had done was to reinforce the need for the Party/state leadership to continue to control China's banking system. A centralised credit tap is certainly a very blunt economic instrument, but it is at the same time a very useful political tool. It ensures that a socially damaging rate of inflation can be immediately addressed.

By the beginning of 1992 the sluggish state of production in many of China's large state-owned enterprises had combined with what a number of scholars now see as Deng Xiaoping's quest to be remembered as the architect of economic reform rather than 'the butcher of Beijing'. I think that on economic grounds alone, China's Party/state élite had little option other than to sanction the return to progressive economic policy. Apart from the closure of smaller enterprises, the economic problems exacerbated and generated by the three years of economic rectification had led to enterprise losses, debt-chains and a significant drop in both central and local government taxation receipts. Nevertheless, it was not until a great deal of politicking had taken place in the lead-up to the Fourteenth Party Congress held in October 1992 that there was formal agreement among the leadership élite over the end goal of reform. Now that goal was to be the development of 'a socialist market economy'. The final hurdle to the promotion of a market integrated economy had then apparently been overcome. Squeamish public comment from conservative members of the leadership over trampling on the Marxist holy ground of public ownership and exploitative, rather than cooperative, labour relations had finally been silenced.[5] The way was now clear for the adoption of the new 'socialist' goal. However, while at a theoretical level China's leaders, economists and planners had agreed that the development of a market integrated economy was their goal, their policy choices were limited.

COMPENSATING FOR THE PRICE OF REFORM

In the latter half of this book I argue that concern for their ongoing authoritative rule in the face of existing interests, tensions and contradictions meant that in spite of their Fourteenth Party Congress agreement to develop a market integrated economy, China's Party/state élite were quick to decide that the process of reform must be ameliorated by institutionalised arrangements and policy initiatives that go some way to compensating for its social and political costs. The result is that, to date, the opportunity to develop a market for capital facilitated by the banking system has been foregone. However, the question of how the machinery of the Chinese Party/state might effectively discipline the economic interests of local agents has remained. The answer to this puzzle was first found in tightening the centralised People's Bank control over client bank credit quotas. It was an attempt by the Party/state élite to impose their preference for what Kornai calls a hard budget constraint on local level economic decision-making. This was to be done using administrative fiat, but when this approach was seen to be flawed, another answer to the puzzle of how best to discipline the demands of local agents was needed. The 'solution' was the programme for ownership restructuring that is currently underway. After suitable auditing, China's state-owned enterprises are to become shareholding limited liability companies or joint stock corporations. Enterprise managers will be responsible to the shareholders who will appoint them. In theory they will be held responsible for enterprise profits and enterprise losses and so they are to be subject to hard budget constraint. However, there are still problems. There is the question of whether, in the presence of a well-developed and firmly entrenched opposition of interests between those representing the Party/state and local agents and in the absence of a capital market for bank funds, state enterprise ownership reform will be sufficient to ensure hard budget constraint is imposed on enterprise managers. In other words – will it ensure the necessary non-negotiable adherence to standardised economic rules and regulations by both representatives of the Party/state and local agents? And there are the increasingly sensitive issues of employment insecurity and the growing number of urban unemployed. The number of unemployed workers has already been considerably boosted by both the ongoing development of a labour market and the shedding of workers from state-owned enterprises already selected to take part in the present push for enterprise ownership reform.

By the mid 1990s, the Party/state élite had resorted to legislation that provides a shield for workers in the face of the ever-growing opposition of interests between themselves and the managers of state-owned enterprises who employ them. However, this approach to buttressing their claim to represent the interests of the workers not only promotes the concept of individual rights and interests and so harbours the potential to undermine the all-knowing authoritative basis of the leadership's rule, it also fails to address the present situation where many more of China's urban industrial workers have joined or will soon join the ranks of the officially unemployed. Once outside the gates of their factories urban workers will cease to enjoy the consumerism that reform has brought and the legislation that the Party/state leaders have promoted as a means of protecting their wages and working conditions will be irrelevant. There is no doubt that state enterprise workers have reason to be concerned over the security of their employment. The prospects are grim for those who lose their jobs. At best they will be pushed from the core into the peripheral urban work-force and at worst they may find subsistence difficult. This disaffection of the urban workers and the urban unrest that may well accompany it, is the reason that in spite of the Fifteenth Party Congress decision to further promote state enterprise ownership reform, a cautious approach has been advised by many within the ranks of China's Party/state élite. They are aware of the political damage done by the social unrest of 1989 and are concerned to avoid any potential damage to China's 'political stability and unity'. Their stance implicitly recognises my argument that while the opposition of interests between Party/state leaders and the inability of the élite to discipline the demands of local agents were major contributors to the social disaffection that culminated in the 1989 Tiananmen Incident, today it is the opposition of manager and worker interests exacerbated by employment insecurity and increased urban unemployment that has the potential to promote social unrest.

1 The national interest versus particular interests

Decentralisation, negotiation and manipulation

> [Under economic reform] there was an intention to put state-enterprise financial relations on a more regularised, depersonalised, 'hands-off' basis since the old [command] system of financial relations involved a constant process of bargaining between state officials and enterprise managers over the levels of financial resources flowing into and out of the enterprise.[1]

Even today, almost two decades after the Deng Xiaoping leadership began to implement their programme for economic reform, advancing one's interests through the negotiation and manipulation of policy has not yet been replaced by the financial dealings based on the standardised and impersonal relations central to the functioning of market economies. In the post-reform era negotiation and bargaining has both increased and become more complex and the process of reform has promoted opportunity for the articulation of particular interests even when they fly in the face of the general or national interest. This situation has in turn created a climate where the appearance of a community of interest between the state and local agents can no longer be sustained.[2]

In this chapter, I canvas policy issues and consequences promoted by the process of restructuring China's state-owned enterprises. I do this against the background of the increasingly transparent opposition of interest between those representing the Party/state on one hand and those promoting local interests on the other.

REFORM IN THE 1980s: INVESTMENT HUNGER AND INFLATION

Extended kingdoms

One of the first questions to be asked about China's industrial reform is – why did the Chinese economy stumble into such a severe and ever-rising rate of inflation in the latter half of the 1980s? The answer to this question can be found by considering the consequences of China's local administrators and the managers of large, economically advantaged state-owned enterprises pushing their own interests at the expense of the national interest. As the process of reforming a centrally planned economy progresses, planning must be ceded to enterprise level before market discipline is possible and in post-reform China there has been the added complication of central planning power being increasingly ceded to both local government bodies and the managers of state-owned enterprises and in some instances, to government corporations directly attached to central government ministries. The latter choose to act sometimes in the interests of the state and at other times in their own particular interest.

It is not too strong a statement to say that in China, in the 1980s, the decentralisation of decision-making promoted by reform resulted in a period when neither central planning nor market forces were in a position to discipline their financial demands adequately. As in the case of other reforming centralised economies, a 'catch-22' situation occurred. In order to implement the reform that will result in the development of a mature market integrated economy, decision-making must be decentralised, but without direct central administrative control over investment decisions and without a market capable of exerting uncompromised discipline, the reform process that leads to a market integrated economy is threatened. An increasing acceleration in the development of productive capacity occurs. In China in the latter half of the 1980s this situation had transpired and was then considerably exacerbated by the tension within the Party leadership over the end goal of reform. At this time the economic behaviour of local agents had created a situation where the primary cause of China's ever-rising rate of inflation was not end consumer demand, but an ever-increasing level of investment funds used for capital construction and fierce competition for production inputs and services required for the resulting extended productive capacity. Local agents were sating their ever increasing appetite for investment by using the greater autonomy that had been afforded them to invest in fixed asset construction outside the plan. In other words, they were instrumental in over-extending China's productive capacity. They did this in response to the still prevailing ethos that decrees that the increased size of their enterprise 'kingdom' that asset growth delivers reflects their success and increases their status.[3]

In what is now a widely accepted argument in relation to the former Soviet and East European experiences of the centralised command form of economic and administrative organisation, and now in relation to China during both the period of centralised administration and under reform policy, Kornai has pointed out that the investment hunger exhibited by local agents has two essential causes. These are first the lack of any restraint and second, a positively motivating factor.[4]

In China, the lack of any restraint on local interests is best understood using the explanation outlined above and by stressing that the lack of either direct administrative or mature market restraint that resulted in the over-expansion of China's productive capacity is mediated via the operation of a soft budget constraint. The negotiation, connections, bargaining and flexibility which are a feature of economic agreements and transactions existing under a soft budget constraint operate in tandem with a widespread and persistent belief among enterprise managers that cost overruns can be recouped from central government sources. Rather than enterprise management being responsible for profit and loss in the manner dictated by a market integrated economy, management demonstrates rampant cost insensitivity. In post-reform China, the cost overruns resulting from this situation have largely been recouped from the national budget via the banking system.

The positively motivating factor leading to the investment hunger that Kornai has identified, is aptly summarised by the observation that in both a command economy and a reforming centralised economy, 'expanding your budget means expanding your scope of power'. The larger an enterprise or even an administrative department is, the more powerful and the more prestigious that enterprise or department and its managers are perceived to be. Asset growth is the major yardstick of both local government and enterprise management's status and success, but unbridled, or at least undisciplined, asset growth in the context of soft budget constraint sucks funding out from the banking system and coupled with the ever-growing demand for production inputs, increases inflationary pressure. Obviously, this is not in the national interest.[5]

Separate kitchens, contracting and loans

By the latter half of the 1980s the decentralisation associated with reform had promoted rampant cost insensitivity. This situation was then made worse by the promotion of an economic contracting system based on 'separate [accounting] kitchens'. It did much to foster the self-interest and inflationary behaviour of both local government administrators and state-owned enterprise managers. The policy afforded these local agents unprecedented autonomy of decision-making. It offered them the prospect of a much more clearly delineated sphere of economic influence, responsibility and status. However, while the increased clarity in relation to their spheres of economic influence and responsibility was an intended consequence of reform policy, their economic behaviour was not. Local agents sought to maximise the good that they could bring to their area of economic responsibility, their behaviour serving to clearly demonstrate the observation that the more they could gain for their administration or enterprise through 'vertical bargaining with the paternal state, the softer the budget constraint tended to be'. In short, the economic decentralisation associated with the economic contracting that was the core of the separate accounting kitchens initiative, further encouraged the financial demands of local agents on the state. The managers of state-owned enterprises pushed their claims for production inputs while provincial government administrators often chose to ignore the priorities set out by Party/state administrators. This meant that while local administrators declared that they were very satisfied with economic contracting (some China scholars going as far as to point out 'the eating in separate kitchens reform was a set of particularistic deals for provincial officials designed to win their support for individual party leaders as well as for the reform drive'), their satisfaction did not translate into keen support for the centre's priorities.[6] And, there was another problem that remained unsolved. There continued to be numerous cases of direct local government interference in enterprise management decision-making, as for example, when local government labour bureaux have foisted unwanted workers on to state-owned enterprise payrolls. The separate kitchens policy was not successful in demanding a complete separation between central and provincial government budgets nor was it successful in separating enterprise management responsibility from local government interference.

As the discussion above indicates, local government administrators have supported, or at the very least have not obstructed, state enterprise managers' quest for resources, but at the same time, if the occasion called for it they would satisfy their own interests at the expense of those articulated by enterprise managers. Nevertheless, in the post-reform period the interests of these two most economically and politically influential local groups have usually coincided. This is borne out by figures that show that in the years 1981 to 1989, local government administrators and state enterprise managers, with the help of local household and foreign investors, invested at an average rate of around 24 per cent, compared with 'only 2.3 per cent growth in investments financed through the state budget'.[7] And, at the same time, the decline of the role of the enterprise Party committee helped to free enterprise managers from the often conservative economic views of resident Party administrators. The managers were much freer to push for their own economic interests. Without the need to consider political correctness as decreed by the enterprise Party committee, managers could undertake the manoeuvring necessary to ensure that the particular interests of their enterprise were well served. They did this in the knowledge that, since the introduction of economic reform, promoting the development of the productive forces was both their economic and their political duty. The introduction of the Factory Director Responsibility System in 1986 (replacing the Unified Party Committee Leadership System that had functioned between 1978 and 1981 and then the System of Factory Director Responsibility Under Party Committee Leadership) served this cause particularly well. It re-enforced the collapse of the political role of state enterprise managers into their quest for the economic development of their enterprise kingdoms.[8] The 1988 introduction of the Enterprise Law then served to further re-enforce both the demise of the decision-making power of enterprise Party committees and the central government's quest to separate government administration from enterprise management. It also played its part in re-enforcing the point that enterprise managers had a political responsibility to promote economic growth.[9]

It was in the context of both their economic responsibility for a given economic area and their political duty to promote economic growth that the managers of state-owned enterprises sought bank loans with the eager support of local government administrators and in some instances with the support of those acting on behalf of a particular central government ministry. The local government or state ministry officials do not have to find these funds, nor are they responsible for them. In bureaucratic terms, it will ultimately be the Ministry of Finance that will be forced to take responsibility for these loans and even then, ministry administrators have been able to off-load this responsibility. It was as a consequence of this last situation that in 1987 the State Council of the Chinese Communist Party passed regulations stipulating that the Ministry of Finance must stop financing central government deficits via direct borrowing or using overdrafts. The Ministry of Finance then continued to borrow from the banking system by issuing fiscal notes to specialised banks. Local bureaucrats and again, in some instances, the administrators of particular state government ministries have been selective in their enforcement of regulations. Not only has the Ministry of Finance been deaf to regulations stipulating that it must stop financing central government deficits in dubious ways, ministry officials have often ignored pricing irregularities and they have encouraged a climate in which the illicit transaction of administratively allocated goods and services has been finessed, often in response to petition from and negotiation with local government administrators and the managers of state-owned enterprises.[10]

Another area where local government administrators and enterprise managers were often complicit is when loan monies drawn through the banking system are granted on the basis of political consideration. This has included both the leadership's concern to maintain 'political stability and unity' and monies advanced on the basis of patronage relations between local government administrators and central government leaders. After all, it is the case that 'keeping the provinces satisfied and on board the reform drive has been an important consideration for reformist party leaders' and listening to their petitions in relation to a particular project is one way of pleasing local administrators while also generating obligation from them.[11] This situation has often contributed to even large and important state-owned enterprises failing to service their existing loan obligations in an adequate manner. Sometimes they have opted to offer no repayment of principal at all, while further monies have been advanced. The amount to be loaned has been negotiated in much the same manner as the percentage of profit to be retained by the state-owned enterprises has been negotiated with government administrators or the type and amount of taxation to be paid has been agreed upon. Throughout the 1980s and today too, a relatively large number of state-owned enterprises are said to have 'no intention of making [and were in effect not obliged to make] repayment of their bank loans' and this has meant that funds from retained profit and other sundry sources that would have been used for the purpose of loan repayment have been freed for the purpose of further fixed asset investment.[12]

While the practice of not routinely servicing bank loans has been endemic among all China's state-owned enterprises, it has been the large economically advantaged state enterprises that have been most able to press their interests in the context of the increasingly competitive bid to access investment funds. When denied resources enterprise managers have both intensified and varied their bargaining procedures. Moreover, the competition for resources has by no means been confined to funding. China's largest enterprises have used their advantaged negotiating positions to modify and inform government reform initiatives and particularly as a means of satisfying their need for raw materials (including skilled labour time). In short, enterprise managers have sought to satisfy both their funding and their immediate material needs via direct canvassing and negotiation combined with *guanxi* (personal connections). This has included pressing their case with local government bodies and even central government ministries who have been known to act in a manner consistent with the behaviour of local agents anxious to ensure that 'their' enterprises are successful. This situation has, in turn, meant that the competition which the process of reform has generated has not primarily been the market competition that China's Party leadership and state planners had expected. It has not been a competition based on increased profit to investment ratio, but competition based on petitioning and acquisitioning for, and access to, scarce expansion and production resources. In short, it has been competition for investment funds and access to circulating funds, scarce raw materials and skilled labour resources and it has been competition for services such as transport and communication links. It has not been competition among enterprises for the sale of product.[13]

Resource constraints, obligation and innovative funding

In China, the chronic shortage of raw and semi-finished materials that has been a feature of centralised economies, continued well after the introduction of reform policy and by the late 1980s this shortage had become critical. It was in this context that the managers of the most advantaged of China's industrial enterprises found yet another avenue for best serving their interests. They were in a position to pay over and above centrally-set ceiling prices for scarce raw and semi-finished products and for skilled labour time. This practice was then often inextricably entwined, or at least garnished, with what has been called 'relational contracting'. The latter are 'contracts of a recurring and non-standardised kind' that are particularly flexible and are based on relationships borne of 'doing business' over a period of time. They are often based on personal connections (*guanxi*), or business dealings become personal connections and these, in turn, are based on relations of personal obligation and reciprocity, the latter including the expectation of future help.[14]

Throughout the 1980s both local administrators and the managers of China's state-owned enterprises continued their former practice of perceiving enterprise profit in quantitative terms. When asked, they offered the view that profit was the most important facet of enterprise production, but it was profit that was calculated in absolute terms and not in light of the ratio between capital invested and profit earned. In spite of government interference in the day-to-day decision-making of enterprise management, in some respects enterprises did come to 'eat in separate kitchens', but what they consumed was predicated on the size of the enterprise and, above all, on the negotiating influence and ability of its management. As I have argued, the larger the enterprise, the more management were able to press their case for resources. They were more able to demand service from government administrators and from their raw material and semi-finished product suppliers. Moreover, the managers of state-owned industrial enterprises found that reform had provided other 'opportunities'. For example, they were quick to recognise that they could fund fixed asset construction by using a large proportion of their retained profit in tandem with monies drawn on an informal basis, some of these latter funds having been drawn from enterprise circulation funds. It seems that at times enterprise managers even resorted to drawing on the depreciation and worker welfare funds held in their custody. At the same time, enterprise managers had been active in raising monies from outside government channels. Again, the funds were often sought in order to expand production capacity and with increasing shortage of production inputs experienced in the latter 1980s, they were also used to pay above the officially designated price for scarce production materials and services (including scarce labour skills remunerated through high bonus payments, relatively good living conditions, gifts and services). And, even these practices were not the end of the matter. Enterprise managers also hoarded and bartered scarce goods. They could then either use these products, or they could barter them for goods and services that they did require.[15]

A large proportion of the funds that the managers of state-owned enterprises raised outside government channels consisted of funds made available through both contract arrangements negotiated between state-owned enterprises and smaller client enterprises and funds raised through enterprise share issues. In the case of contract agreements negotiated with smaller client enterprises (in the late 1980s these were usually small state-owned and collectively owned enterprises) the managers of larger advantaged state-owned enterprises found that they were in a position to promote lateral economic ties by offering the managers of their client enterprises administrative expertise, access to technical training and even machinery and, above all, the use of their bargaining power in order to acquire the scarce raw and/or semi-finished materials they required in order to manufacture the product that they would sell to their patron, the large state-owned enterprise. The smaller contracted enterprises were in effect piggy-backing on the competitive muscle of the large economically advantaged state-owned enterprises and they were required to pay for the access to funding, expertise, technology and raw materials that they received. At times these payments were facilitated by Agricultural Bank loans and so appeared as though this was direct investment in rural China. It was not. It was investment in client manufacture for urban based state-owned enterprises. The funds provided in this fashion were particularly valued by the management of the state-owned enterprise because they were away from the direct view of government administrators. They were again available to be used for fixed asset investment and they were be used for matters such as paying over and above the fixed or guidance price required for particularly scarce products. In this context they were a central component of the oil that has kept Chinese manufacture functioning, particularly during the latter half of the 1980s when the ever-worsening shortage of raw materials, semi-finished production inputs and services became a significant impediment to the state enterprises' ability to feed and so utilise their extended productive capacity.

Share issues

By 1987 the managers of many large state-owned enterprises were allowed to issue shares. The potential for ownership reform inherent in this policy is obvious and so too are the political pitfalls in its promotion. But during the 1980s, only the political price of promoting ownership reform was realised. Conservative members of the Chinese leadership élite found that they could not sanction ownership reform in a socialist society or they used this trampling on the Marxist holy ground of communal ownership in order to promote their own positions. The potential for ownership reform was not realised. Share issues were used only as a revenue raising measure. By 1988, the then president of the People's Bank of China, Li Guixian, was optimistically noting that 'we can sell a number of enterprises, or stocks of some large, state enterprises to reduce state investment and loans and lessen the burdens of the state'. He believed that monies raised by enterprises via share issues would relieve the stress on government finances and the demands made on government by enterprise managers for funding and that this was the primary function of enterprise share issues.[16]

In central government circles, where it was (I think quite wrongly) believed that excess end consumer demand was the primary cause of inflation, it was agreed that not only would shares augment state and enterprise funding, the sale of shares to workers and individual consumers would be useful in terms of soaking up excess household spending capacity.[17] But shares, like bonds, were not sold only to workers. They were sold to other institutions, including other state-owned enterprises and state and local government entities. When they were sold to workers the shares were then either a part of the booty available to them or, more often, they amounted to forced allocations that taxed workers' earnings in order to fill enterprise coffers. In 1989 the purchase of shares by workers amounted to around 2.7 per cent of individual wages, but then this avenue of revenue raising became 'less and less viable'. This was due to worker opposition. When enterprise workers had been required (all but forced) to purchase shares, there was an increasing and understandable resentment.[18] All this was a long way from the vision presented by members of the progressive faction within the Chinese leadership and the state economists who supported them. They argued that ownership reform would buttress the process of eating in separate kitchens. In other words they believed that it would boost the process of implementing non-negotiable contracts between government administrators and the managers of state-owned enterprises. They therefore argued that share issues would 'provide the necessary conditions for enterprises to truly operate independently, to assume sole responsibility for their profit and losses and to exercise self-control'.[19] But the shares issued were 'socialist shares'. The purchasers of shares in China's state-owned enterprises were not obliged to take any risk. Interest dividends were calculated as part of enterprise production costs, not on the basis of profit earned and even then the conditions surrounding these shares were corrupted. For example, the claim of central government administrators that those purchasing shares (in this case usually other state-owned enterprises or government administrations) would be in a position to influence policy decisions by the enterprise board, was usually, though not always, hollow. Often, influence was denied and/or a government administrators would simply delegate their supposed influence to the managers of the enterprise.[20]

Securities, savings and enterprise financing

Between 1988 and 1991, the price of all securities available on China's secondary market rose. The secondary market had replaced a former black market in bonds that had lasted from mid 1981 until April 1988. Obviously, the secondary market provided an avenue of liquidity and often profit for bond holders and both liquidity and profit for share issue holders. (Though this was not the case in relation to the treasury notes that had also circulated in the secondary market between 1988 and 1991. These had at first declined in value and then slowly their value had risen.)

The substantial rise in the price that enterprise shares and other securities had enjoyed while circulating in the secondary securities market had obviously been very welcome. It was said that the secondary market had 'played a beneficial role in increasing the price of government securities'. Obviously, it had 'made it easier for the government to issue debt'.[21]

In the secondary market the rising price at which enterprise shares transacted was uninformed by the buyer's understanding of profit predicated on the productive efficiency of the enterprise. In the latter 1980s the price of the shares had produced a 'thin' market that in its initial form had always risen and perceptions of share value were also informed by the status of the enterprise. This was again a concept based on the success of the managers of the enterprise in providing for and developing their kingdom and therefore on the likely future value of the shares when re-sale was sought. Ironically, at the same time as China's state enterprise workers were often resenting forced purchase of shares issued by their enterprise (as I have argued, they viewed this pressured sale of shares as merely another form of taxation), there was general public demand for the purchase of shares on the secondary market. In August 1992 there were even riots among the brash population of the Mainland/Hong Kong border city of Shenzhen when the public demand for shares was not met. At this point state administrators were forced to concede that 'a lack of experience in arranging new share issues and a lack of transparency in management' combined with 'malpractice for selfish ends [had] aroused public indignation'.[22]

Increasingly, a large segment of the secondary share market activity in government and enterprise securities was predicated on the unprecedented growth of household income taking place in urban China, particularly in south-eastern and eastern sea-board cities. In spite of the predominance of institutional purchases of enterprise shares, this growth in individual savings was explicitly recognised by central government sources as a resource that could be mobilised to help meet funding pressure. It was in this context that the state's promoting of share issues amounted to 'soliciting investment' from the Chinese people.

By 1992, central government sources were estimating that the outstanding balance of savings deposits at China's banks was more than one trillion yuan. It was this fund of savings deposits, coupled with the government's continued and expanding need to use securities as a means of issuing and so covering debt, that fuelled the continued growth in China's securities markets (both in terms of bonds and share issues). It is then not surprising that by 1992, government sources were matching the funds deposited with the banking system with the argument that noted 'if national economic development is to have a certain speed, capital input is needed'. Under the auspices of the economic rectification that had begun in 1988 and was cemented into place by the 1989 Tiananmen Incident, there had been a steady worsening in the economic position of the state-owned enterprises accompanied by a continued substantial drop in both central and local government tax receipts. The latter was predicated on declining enterprise profit. The solution to the problem of financing the enterprises was then again to be 'to turn the money that is in the hands of the masses into construction funds by various methods' and a principal method was to be through the issuance of 'a greater number of state-owned enterprise shares'. After all, it was argued, there had been too much emphasis to date on financing through banks and the 'excess reliance on banks' had increased inflationary pressure. The use of enterprise share issue was an obvious and tempting alternative that enterprise management had been only too pleased to use. Though more strictly controlled than contracting arrangements between state enterprises and smaller client enterprises, it too was funding that from the point of view of enterprise managers, was removed from the immediate purview of government administrators.[23]

Apart from worker reward and the raising of funds to meet asset acquisition and production expenses, the other use of enterprise shares was to ensure supply of scarce enterprise production inputs. Suppliers downstream in the production chain were provided with bonds or shares that they were then free to trade in the rising secondary securities market. The downstream enterprise would then feel obliged to meet the supply requests made by the share-issuing enterprise and if sufficient shares could be purchased (amounting to a sum representing more than 50 per cent of the worth of the enterprise) then, at least in theory, the influence that your shareholdings had bought you could be used to alter significantly the production run of the supplying enterprise.[24]

Output, profit and workers' bonuses

While state enterprise managers were garnering resources for their enterprises, the size of the enterprise kingdom and so the quantity of profit generated by enterprise production, was, as I have argued, serving to promote the status of both enterprise managers and enterprise workers. Quantity of profit reflected on management's ability to amass assets and to take care of its family of workers who, in turn, had the status of working for a big and successful state-owned enterprise. Bonus payments were drawn from quantitatively assessed enterprise profit and so too were the monies made available for the provision of enterprise welfare services. The level and quality of worker housing, education, healthcare and recreation facilities provided by the enterprise welfare fund directly reflected the profitability of the enterprise, but not the efficiency of the productive process. As both Chinese and Western economists have now pointed out, this meant that since the size of bonus and the provision of welfare services depended on the profit that in turn depended on the quantitative output of factories, how to increase the trio of output, profit and worker bonus payments 'weighed heavily in managerial decisions'.[25]

It now seems that the provision of worker bonus payments, housing and welfare services actually served to weaken the link between individual labour productivity and individual worker compensation that Party/state administrators were attempting to promote. Like Walder's study of labour relations within China's state-owned enterprises during the first half of the 1980s, studies of this situation talk of the so-called manager/labour 'collusion' that led to 'overcompensation' of state enterprise workers during the late

1980s phase of China's reform: a situation attended by rising state worker expectations that were, in spite of the ever-growing and maturing opposition of interests between managers and workers in the period after the 1986 introduction of worker contracting, very often met, but which have not been met during the 1990s. Indeed, it is now clear that during the 1980s state-owned enterprise managers had the 'difficult task of separating the image of their factories' resourcefulness from people's expectations'.[26] This was obviously an important and further 'positively motivating factor' in the managers' persistent bid to expand and then provision their productive capacity by any means available to them.

Effective management obviously had little, if anything, to do with the ratio of investment to profit that a predominantly market integrated economy would require and everything to do with the enterprise shopping list that management sought to satisfy in order to maximise output. Moreover, both worker and management incomes depended on protecting and advancing the enterprise's interests by management. This meant that once the payment of bonus-rates was devolved to enterprise management, workers' take-home pay doubled. This situation resulted in an attempt by the state to discipline enterprise management through the use of laws curbing (but not removing) their financial autonomy. Though the central government had retained control over the national wage bill and over the base and supplementary wages paid to workers, it found it necessary to decree that an annual bonus payment could be no more than three months of a worker's annual base wage. If this amount was breached, then enterprise management was required to pay a substantial taxation penalty. The result was that enterprise management ducked the state's attempt to limit monies flowing to enterprise workers (without the benefit of productivity and efficiency gains) by investing in worker housing and welfare services at an unprecedented rate. While state enterprise workers' take-home pay is estimated to have doubled between 1979 and 1984, in the second half of the 1980s enterprise-provided housing space, standard and availability increased substantially as did other welfare provisions. Gifts (non-cash privileges, goods and services) to workers from enterprise management were also forthcoming during this period. All these services, including the gifts, functioned to reenforce the order of seniority, favour and personal ties operating within the enterprise community (family) and underscored both the common interest between managers and workers in maximising enterprise production output and profit and the paternalistic role played by enterprise managers toward their workers.[27]

REFORM AT THE SECOND AUTOMOBILE/DONGFENG CORPORATION

Policies that have paid off

During interviews with managers and economists from the Second Automobile/Dongfeng conglomerate held in 1985, 1986 and again in 1987, I was struck by the extent of the premium that the management of this large economically advantaged state-owned enterprise were placing on extending their productive capacity, seeking out scarce productive inputs and taking care of their work-force. The policies adopted by the management of the enterprise group paid off handsomely. Their decision-making had ensured that productive capacity had expanded and that productive output measured in terms of quantity had increased and that the enterprise group had a work-force that considered themselves very well cared for. By 1986, the Second Automobile/Dongfeng group's fixed asset holdings had tripled in relation to its beginnings just half a decade earlier and the enterprise had won the right to be considered as a discrete entity under the central government's national plan. The enterprise group's labour-force had increased substantially in number and contained a highly skilled and well-educated core of much sought after workers. In other words, the enterprise management had been, on its own assessment, successful.

Small shoes and the saga of the central government's Automotive Corporation

The managers of the Second Automobile/Dongfeng corporation had done very well in terms of taking care of both their province of economic responsibility and their constituency. Nevertheless, the management of the Second Automobile/Dongfeng group did not have matters entirely their own way.[28] As I have argued above, local government administrators often worked in concert with enterprise managers and this was also the case with respect to administrators representing the Ministry of Machine-Building and the Second Automobile/ Dongfeng corporation and with the Hubei provincial government and the managers of the Second Automobile/Dongfeng group. Local government administrators and enterprise managers were often in opposition to Party/state policy initiatives, or at least both the local administrators and the managers demonstrated a will to manipulate such policy to their advantage. But they also harboured interests that may well be in conflict with one another.[29] For example, even though the Second Automobile/Dongfeng group had been under central government management since 1981 when it was placed under the Motor Vehicles General Bureau of the Ministry of Machine Building (the Second Automobile works amalgamated with eight other enterprises in April 1981 to become 'the path-breaking' Dongfeng Joint Automobile Industrial Company or in today's nomenclature, the Second Automobile/Dongfeng corporation), members of the Hubei provincial government administration had been a constant source of providing 'small shoes' for management's initiatives and interests. Moreover, with the creation of the China Automobile Industry General Corporation in May 1982 (often referred to as either simply the Automotive Corporation or the Automotive Ministry, composed of a part of the responsibilities of the Ministry of Machine Building), the Second Automobile/Dongfeng group had an immediate and clearly delineated central government supervisor. This situation may well have been considered to be an administrative advance that went at least some way toward protecting the group from the bureaucratic interests of local administrators at times when these interests did not coincide with their own. However, Automotive Corporation officials were not acting in accord with the interests of the state, nor were they acting in the interest of the enterprises under their jurisdiction. They were keen to use their supervisory authority to their own advantage. They sought to erode the decision-making autonomy already gained by the Second Automobile/Dongfeng group's management. The administrators derived financial benefit for themselves and 'their' Corporation from the Second Automobile/Dongfeng enterprise group.[30]

Profit distribution between the government in Beijing and the Second Automobile/Dongfeng group had been negotiated directly with the central government without reference to the Automotive Corporation, but the administrators from the Automotive Corporation had nevertheless seen fit to avail themselves of up to 5 per cent of the enterprise's retained share of profit, 10 per cent of the enterprise depreciation fund and a small management fee derived from sales income. The latter had been earnt by the enterprise group after all the demands of the mandatory plan had been met. These levies were resented. They were a source of considerable grievance. They were therefore probably the primary reason why the enterprise group's managers had struggled hard to free themselves from the central government's Automotive Corporation.

The Automotive Corporation had been charged with responsibility for determining the Second Automobile/Dongfeng group's mandatory plan output and the corresponding input allocations that would be provided for by the central government. This calculation was to be based on planning targets handed down directly by the State Planning Commission. The Automotive Corporation also appointed enterprise managers and Party secretaries to the group's enterprises, though final approval for top leadership positions had to be ratified by the highest levels of the Party and there was considerable resistance from the Second Automobile/Dongfeng group's managers when the Corporation attempted to go as far as appointing functional department heads. What is more, this was not the only resistance that the Corporation provoked. By 1987 the motor vehicle producers subject to its administration, particularly the First Automobile corporation and the Second Automobile/Dongfeng corporation, had rebelled. They successfully petitioned for the Automotive Corporation's demise and in the end, they won.[31]

The First and Second Automobile corporations compete and small shoes persist

Unfortunately from management's point of view, the Second Automobile/Dongfeng conglomerate's role in joining managers from the First Automobile group in successfully petitioning for the demise of the Automotive Corporation did not mean the end of competition between the two vehicle producing conglomerates and it did not mean the end to the 'small shoes' approach that government administrators were taking to the group. There had been understandable tension in terms of what was distributed by the Automotive Corporation to the older more established First Automobile group *vis-à-vis* the Second Automobile/Dongfeng group. This tension continued on, and so too, the bureaucratic chaffing caused by the right of first the Automotive Corporation and then other central government bodies to appoint senior management to both the First Automobile group and the Second Automobile/Dongfeng corporation. There was also the ongoing issue of labour allocation outside the ranks of management that, in spite of far-reaching and fundamental changes in enterprise labour policy, even today, continues to be a matter of considerable angst. During its reign the central government's Automotive Corporation had outlined the Second Automobile/Dongfeng wage and labour plans. Subsequently, it was the Hubei provincial government labour bureau that was charged with implementing the labour plan. The Second Automobile/Dongfeng group's relationship with the Hubei government labour bureau continues to provide a source of numerous conflicts and consumes a great deal of negotiating time. The provincial labour department has never wavered from its focus on ensuring that the automobile group take the workers that it assigns to it. As recently as February 1996, the labour bureau was assigning demobbed army engineers to the Second Automobile/Dongfeng conglomerate. When I asked about this, managers shrugged their shoulders in resignation and asked what they could do about this situation. It was, they said, 'their political duty'. After all, the managers of their corporation could only go so far in opposing the wishes of a provincial government administration that on other occasions would support and facilitate the corporation's production needs.[32]

A main player

Today, China's state bureaucrats are boasting that the Second Automobile/Dongfeng corporation is well advanced in terms of developing the capacity to become 'among China's largest producers of automobiles'. They estimate that 'it will take [only] 15 years for the [Second Automobile/Dongfeng] conglomerate to build itself into a large auto producer . . . with a capacity reaching one million automobiles a year'. It is product primarily destined for China's domestic market. But throughout the 1980s and indeed for the present, the Second Automobile/Dongfeng group's production is not based on the manufacture of automobiles. The focus is on producing middle and heavy-duty trucks and vans and on the manufacture of truck engines. While a small volume of export has been involved, the group's trucks and engines have also been sold primarily into China's domestic market. (In 1991 the group was producing 130,000 trucks per annum and by 1995 their annual production of trucks had risen to 180,000 units. These volumes have represented around 80 per cent of the group's production capacity.)[33]

Prior to their boost as a main player in China's current domestic car manufacture, the Second Automobile/Dongfeng group (under its Dongfeng Automotive Company title) had used its diesel engine plant built at its Xiangfan base as its medal of successful cutting-edge manufacture. This plant was a 328 million yuan investment. It was built using 'a complete set of advanced technology on diesel engines B from the Cum[m]ins Company of the United States'. The agreement for this proposal was signed in 1987. Plant construction began in 1988 and trial production was underway by 1989. The 1995 output figure for this arm of the Second Automobile/Dongfeng grouping was 60,000 sets of diesel engines which were to be used in light, middle and heavy trucks and as engineering and generating units and as ships' engines. This was the second arrangement that the Second Automobile/ Dongfeng group had with the Cummins Company during the 1980s. In line with the central government's open-door policy, this Cummins engine project included the transfer of American technology, personnel and personnel training. The Second Automobile/Dongfeng group's saving in terms of research and development is obvious and, at the same time, foreign contracted production has been an aspect of the group's manufacture that management has not been hesitant to use as a stick to beat their own suppliers. They insist that the quality of semi-finished products supplied to the group must be up to the standards expected by foreign investors. Foreign invested projects have also been useful in the bid to exert pressure on both government administrations and the banking system for the advancement of further development funds. In short, foreign investment, contracted production and technology transfers have served to promote the Second Automobile/ Dongfeng's growth and status and so the power exercised by management and the size of the kingdom that they administer.[34]

Citroën, Cummins, Thomson and others

By 1988 the negotiations that had been taking place between the management of the Second Automobile/Dongfeng corporation and representatives from the French company Citroën for the development and manufacture of small sedans for the Chinese domestic market, were well advanced. Throughout the 1980s the Second Automobile/ Dongfeng group had honed and developed its international connections. The joint investment arrangements that the group established with representatives from Citroën and with the American Cummins corporation for the licensed production of diesel engines, were by no means the only arrangements made with overseas companies. For example, early in the 1980s the group had upgraded its production of automotive thermostats by entering into a technical partnership with the American company Thomson International. By 1988 this arrangement had become the Dongfeng/Thomson joint venture and by the beginning of the 1990s a number of other looser arrangements had been made involving overseas companies. The Second Automobile/Dongfeng group had an interest in the Hubei

Asbestos Production Mill's equity investment agreement with an Italian company to produce car disc-brake pads. This enterprise is situated at the same Xiangfan City-Hubei Province location as other Second Automobile/Dongfeng group plants, including those producing Cummins engines. In addition, the Second Automobile/Dongfeng group entered into an agreement to import axles from Nissan Diesel for its assembly of trucks and buses. Technology for truck cabs, transmissions and chassis was also provided by Japan's Nissan company. By 1994 the Second Automobile/Dongfeng group had joined with a Taiwan based firm to invest $US50 million in a plant that will produce 100,000 light-duty trucks each year. This plant, like the Second Automobile/DongfengCitroën enterprises will be situated in Wuhan city's newly established special economic zone. The Second Automobile/Dongfeng group has also obtained a 35 per cent stake in the Zhengzhou Light Truck Plant often referred to as the Zhengzhou-Nissan company. The latter is a recent venture in which the Nissan Motor company has a 5 per cent interest.[35]

Two of the three bigs

Today, the three conglomerates that the Chinese leadership is intending to entrust with the bulk of automobile production are to be known as the 'three bigs' of China's foreign invested automobile production. They are the Second Automobile/Dongfeng-Citroën project, the First Automobile works-Volkswagen project and the Shanghai-Volkswagen project. (What have been called the 'three smalls' – Beijing Jeep, Tianjin-Daihatsu and Guangzhou-Peugeot – and the military backed Changan Automotive corporation-Suzuki projects are also expected to be favoured.) The tension and rivalry between two of the 'bigs' (the First and Second Automobile corporations) was probably inevitable. Not only was the Second Automobile works opened in opposition to the First Automobile works, but the management of the newer player went about successfully gleaning the majority of its already skilled workers from the older First Automobile works. Then they fostered connections with both the Qinghua University and the Jilin University of Technology. Both universities were considered to produce the best automotive engineering graduates in China. The Jilin University had formerly been the Changchun Motor Vehicle College. It had produced engineers that were employed almost exclusively by First Automotive corporation. Later the Second Automobile/Dongfeng group established its own in-house education system. The group has run very well-provisioned and reviewed middle-schools (I first viewed Halley's comet through a high-powered telescope belonging to one of these schools. While teaching conversational English to Second Automobile/Dongfeng corporation managers/cadres I had been persuaded to teach conversational English to the corporation's middle-school language teachers). Even more importantly, in terms of technological training of highly skilled automotive engineers and production workers, the group established a workers' university. Here workers and the children of workers were taught a very wide range of tertiary level subjects. Engineering skills, of course, but also computer, language and an impressive range of general knowledge education have been undertaken by the institution that has recently been re-named. It is now called the Hubei College of Automotive Engineering.[36]

The rivalry between China's First Automobile corporation and the Second Automobile/Dongfeng corporation has now become a race for the position of China's primary vehicle producer. The First Automobile corporation has established a joint arrangement with Germany's Volkswagen producers and now produces Volkswagen Audi, Jetta and Golf sedans. This older corporation had already had experience in both truck and car manufacture. Previously it had produced the Liberation (Jiefang) truck and the Red Flag (Hongqi) limousine. Faced with this situation, the management of the Second Automobile/Dongfeng group decided that their best chance lay in producing superior vehicles at a competitive cost. In common with the management of other state-owned enterprises the management of the group did not base this competition on the general category of profit return on funds invested, but on ability to sell quantity of product without concern over profit to investment ratio. Soon (by 1986) there were not only waiting lists, but long waiting lists for Dongfeng trucks. This was because the trucks were the preferred vehicle of the purchaser. There was a two-year delay in delivery. Indeed, it was these waiting lists, combined with government pressure placed on the Second Automobile/Dongfeng group's management to increase the volume of foreign exports, that led to the phenomenon of 'internal export'.

Internal export

By 1982 the Second Automobile/Dongfeng group had gained the right to export its products directly. It was allowed to by-pass the foreign trade bureaucracy. Soon, the group was allowed to retain 40 per cent of the foreign exchange earnt through export and gained the right to borrow foreign exchange from the China International Trust and Investment Corporation (CITIC). This could be repaid in domestic currency. By the second half of the

1980s, the Second Automobile/ Dongfeng group already had well-established contacts with foreign suppliers and markets and by 1991 the group's economists were boasting that by the mid 1990s the group would be earning as much as $US50 million in foreign exchange: a situation that added substantially to the prestige of the enterprise, its managers and workers. Foreign exchange earnings were 'a symbol of the financial ability of the enterprise group' and it was argued that foreign earnings are necessary for further economic development. Dealing with foreign companies was recognised as providing 'a window for improved enterprise information and for improving the labour force'. The group had been consistently purchasing engineering skills and production machinery from as far afield as Germany and Italy and by the latter half of the 1980s it had reliable, though relatively small, export markets for its trucks in developing countries such as the Philippines and Egypt. During this period innovative categorising within the group ensured an internal export market for the trucks that the group produced. By 1988 the Second Automobile/ Dongfeng corporation was obliged to sell only 30 per cent of its product directly to the central government. This percentage prevailed for some time to come. In 1991 prices the state's fixed price for purchasing a Second Automobile/Dongfeng vehicle was $US6,500. The group then sold the other 70 per cent of its product on the market at a price (under central government guide-lines) of $US7,000 to $US7,800 per unit. But there was yet another formally recognised sales channel for domestic product. This was private sale where the price of a vehicle could be as much as double the state's fixed price. Product manufactured after the government's estimated planned production capacity of the Second Automobile/ Dongfeng corporation had been completed, could be sold at this free (market determined) private price. In other words, it was only vehicles produced over and above the negotiated and bargained government estimated productive capacity of the group, that could be made available for private sale at a price that was without any government imposed ceiling. It was very important that the group's managers were successful in keeping the government estimated productive capacity of their enterprises as low as possible. This would ensure an adequate capacity for manufacture for the lucrative private market. When negotiation and bargaining arrived at a relatively low figure for the government estimate of productive capacity it was considered to be a *coup* on behalf of the Second Automobile/Dongfeng managers.

The majority of fixed priced vehicles sold directly to the state were being bought for the army. Other prospective buyers of Second Automobile/Dongfeng produced vehicles would have to add their names to a long waiting list for either a retail guidance priced vehicle or for the highly priced retail private sale vehicles. (The difference between the lists depended on the amount of *guanxi* required to ensure a place on the cheaper guidance price list. The management of another large advantaged state enterprise may well have sufficient connections to ensure a place in the guidance price list while a transport/farming household from south-eastern China would have no such useful connections and so would be obliged to put their name on the list for private sale.) In order to solve the waiting problem a buyer from either list (usually another large economically advantaged state-owned enterprise) would be encouraged to use foreign exchange to buy a unit from the Second Automobile/Dongfeng group. The unit purchased would be available immediately, however it would have to be paid for in a foreign currency and at foreign currency price. In 1991 it was set at $US7,800 – at the top end of the state set guidance price for a Second Automobile/Dongfeng produced truck. The truck then sold would appear as an exported vehicle for which the Second Automobile/ Dongfeng corporation had earned foreign currency. There was no quota dictating that export production be either that part of the group's government set manufacturing capacity available after the demands of the mandatory plan had been satisfied or that it be attended to only after all the dictates of the government set capacity had been met. In other words, there was no quota covering the production of vehicles for export. This is why there was no waiting list for these vehicles. As paradoxical as the name seems, the sale was called an internal export. It was in the interest of enterprise fund-raising, but it was a phenomenon that must have distorted the state's export figures and so on a very large scale would be likely to distort state policy initiatives.[37]

Unhappy engineers

It was because Second Automobile/Dongfeng group's engineers had had direct contact with overseas engineering expertise (from their experiences with both joint-ventures and the corporation's 'real' exports) that, when the Second Automobile/Dongfeng joint-venture agreement with Citroën was struck, there was some discontent among the engineers. They believed that German engineering expertise was better than the French expertise and so were critical of the management's agreement with the French government to accept a soft $US4.5 billion loan, 55 per cent of which consisted of credits for the purchase of French engineering expertise and technology. The balance of this loan was to be repaid over the next thirty years. The engineers' misgivings about French engineering expertise and technology had fallen on deaf ears.[38]

Design, price, status and supply

As I have noted, the initial advantage that the Second Automobile Dongfeng corporation had over the First Automobile corporation was that the design of their Dongfeng truck was considered to be much more modern. Before its recent design re-vamp, the Liberation truck produced by the First Automobile works resembled a 1930s vintage Dodge truck while the Dongfeng truck appeared to have been designed in accord with parameters common in Western countries in the 1960s. From the outset, the management of the Second Automobile/Dongfeng corporation pursued an aggressive growth strategy. When, by the latter 1980s, farming households that earnt off-farm income by undertaking contracted transport jobs found that they had sufficient accumulated funds to purchase a truck, or might be in a position to access rural financing through either formal or informal channels, managers of the corporation were quick to recognise this situation as a source of both market private sales and untied funds. By the second half of the 1980s the corporation was selling units at three (or more correctly, four) prices. As I have noted above, there was the fixed price that central government instrumentalities, particularly the military, paid for vehicles that continued to be constructed under mandatory planning guide-lines. Central government sources guaranteed production inputs for this section of the Second Automobile/Dongfeng group's production. There was then the guidance (or ceiling) price that other government instrumentalities, particularly other state enterprises and some collective enterprises paid for vehicles. Then, there was the private price paid for vehicles. Without the connections available to other state-owned enterprises and some collective enterprises who were producing semi-finished product or even other products required by the Second Automobile/Dongfeng group, rural transport/ farming households not only found that they had no option other than to purchase their vehicles at the much dearer private price, they also found that like guidance price buyers, they must pay a deposit merely to be listed for purchase of a Dongfeng vehicle. The balance of the purchase price was then due on receipt. Both payments were to be made in cash. The fourth price was the export price.

During the latter half of the 1980s the Second Automobile/ Dongfeng conglomerate's ability to earn export dollars and so import foreign expertise was central to its successful rivalry with the First Automobile corporation and so to its continued status as one of China's most advantaged state-owned enterprises, but this was by no means the only ploy used by management to ensure that the Second Automobile/Dongfeng conglomerate continued to be rated as a main player in China's industrial programme. As I have argued, like all other state-owned enterprise managers, the managers of the Second Automobile/Dongfeng group sought a quantitative expansion in their productive capacity. Management took whatever opportunity that came their way, including using the state administrators' enthusiasm for the development of 'lateral economic ties'. These ties are an integral part of any reform policy. After all, if vertical controls and means of supply are decentralised, then lateral economic ties must take their place. These ties are intended to overcome lateral blockages in supply and demand.

Using lateral economic ties

China's central policy-makers intended that lateral economic ties would break down provincialism and encourage local agents, particularly state enterprise managers to search far and wide for both their production resources and above-plan sales. The latter is all product manufactured after the requirements of the mandatory state plan have been met. The managers of the Second Automobile/Dongfeng group promoted lateral economic ties in a number of ways. For example, in 1988 having been faced with a shortage of both aluminium and rolled steel, they sold trucks manufactured by the corporation in exchange for aluminium and in the case of the rolled steel, they invested a substantial sum in purchasing shares in a steel mill in the southern province of Guangdong. Their intention was to purchase sufficient shares to 'buy' the right to influence the production undertaken by the mill, or at the very least to 'buy' obligation from the steel manufacturer. (When production quantity was still a mark of profitability rolled steel was not an attractive proposition for the mill.) Also by 1988, the Second Automobile/Dongfeng group was boasting approximately 300 factories or more correctly production entities or enterprises that under the auspices of promoting lateral economic ties, were counted as a part of the group. These included enterprises that were tied to the group under a joint venture agreement based on a 'unity of investment' whereby the factory or economic unit had thrown in its lot with the Second Automobile/Dongfeng corporation to the point where it had become either completely merged and so had become a part of the conglomerate, or to the point where it used contract agreements to effect close cooperation. There were also arrangements described as a loose cooperation. During the second half of the 1980s these categories of associated factories or enterprises benefited a great deal from their association with the Second Automobile/Dongfeng conglomerate and the self-interested decision-making of the group's management. However, those who had chosen to use contract agreements to effect either a close or loose cooperation with the Second Automobile/Dongfeng group were later required to pay for their association.[39]

By the latter months of 1988 and certainly by 1989, it had become very difficult indeed for smaller enterprises to have reliable access to production resources. The considerable advantage exercised by the large state-owned enterprises in terms of accessing production resources to feed their expanded productive capacity had closed out smaller less economically able enterprises. By becoming either a party to a large enterprise group, or even a contracted client enterprise of these large corporations the smaller enterprises' search for production inputs was all but solved. In return for an agreed sum of investment funds technical expertise was afforded to the connected smaller enterprise and raw materials to be used in the contracted production process were found. In many ways the role taken by the Second Automobile/Dongfeng group at this point mimicked the paternalistic role taken by the state or local government administrations. The smaller integrated or client enterprise had effectively bought themselves the right to belong to the group and had become a part of the province and the responsibility of the group's management. Indeed, management counted the capacity of the connected enterprise as a part of the group's overall productive capacity and the employees of these enterprises as a part of the group's work-force. The connected enterprises enlarged the Second Automobile/Dongfeng kingdom and so increased the status of the group and the success of the group's management.

From untied funds and enterprise paternalism to mergers and closures

The monies paid by smaller connected enterprises for their membership in the Second Automobile/Dongfeng group had, as I have noted, also provided funds for the conglomerate's management that were outside the purview and so the direct control of government administrations. These funds were able to be used without tedious explanation and manipulation of government rules and regulations. They were used for further expansion of productive capacity, for extra compensation for workers in the metropolitan enterprise group and for paying over and above state-set price limits for scarce resources, services and favours. However, in the period of severe economic contraction that followed the 1989 Tiananmen Incident's cementing of the contractive economic policies and tighter control of enterprise affairs preferred by the conservative members of China's Party/state élite, the smaller contracted enterprises (those who had not been invited to become an integral part of the Dongfeng conglomerate, but had elected to be either closely or loosely contracted to the Second Automobile/Dongfeng group) proved to be occupying a vulnerable economic position. In many cases, once the 1988–9 contraction of the economy began to hobble management decision-making, their contracts with the Second Automobile/Dongfeng group were no longer honoured. In other words, in common with the managers of other large advantaged state-owned enterprise conglomerates, the managers of the Second Automobile/Dongfeng group chose to reduce their productive capacity by not honouring the contracts that supported production undertaken by the client enterprises. This happened at a time when the contractual policies of the leadership resulted in the smaller enterprises being denied access to bank credit and when government sources, particularly local government administrations, were making an energetic bid to collect taxes due to them. The enterprises contracted to the Dongfeng group, like a large number of small state enterprises contracted to other large state-owned enterprise groups, were faced with either merger or closure. In either case a number of the workers in these enterprises were often deemed to be 'surplus' leading to more workers being added to what was already becoming a serious number of unemployed among China's wage-workers.[40]

While many of the state-owned enterprise groups had mimicked the paternalistic role of the state in relation to their contracted client enterprises, unlike the state they found that they were free to ignore the arrangements that they had made when they were pressured to reduce their production capacity. Indeed, the client relationships that the management of economically advantaged state-owned enterprises such as the Second Automobile/Dongfeng group had entered into had provided them with an opportunity to reduce capacity without reducing production in their core metropolitan enterprises and without dismissing members of their core work-force. It was this situation that prompted me to look back across China's first decade of reform and attempt an understanding of the role of the smaller state-owned, collective and now privately run enterprises in the Chinese economy. I have concluded that small state-owned and collectively owned enterprises (and now privately owned enterprises) provide an elastic band within the Chinese economy. When the economy is growing the smaller enterprises are able to extend their production capacity and increase in number, but when the Chinese leadership élite has deemed it necessary to discipline the growth in productive capacity, the dire consequences of the corresponding restriction of bank credit has fallen disproportionately on the smaller enterprises. The leadership finds that the power of the local administrative and enterprise negotiating lobby combined with dictates of political stability and unity require that the larger advantaged state-owned enterprises be shielded from the worst consequences of centrally induced periods of economic contraction. The smaller enterprises are left to take the full effect of restricted economic growth and, in the case of the 1989–92 period of economic rectification, they were left to take a great deal of the force of a particularly harsh period of economic contraction. At the same time as large state-owned enterprises cut their client enterprises adrift and the central government cut these enterprises off from bank financing (and while local government agencies harassed them for taxation payments), these smaller and less politically important enterprises were subject to an even stricter rationing of raw materials and energy supply than had been imposed on them in the past.[41]

In the face of the steadily increasing number of forced enterprise mergers and closures, central government economists had sanctioned the action taken by managers of large state-owned enterprises in relation to their smaller client enterprises by arguing that 'too many enterprises have emerged because of the [previous] over-heated economy and excessive capital investment'. They noted that all enterprises, including those which had emerged during the previous expansionist period, 'want to live' but that 'limited resources have to be divided to feed all enterprises, both good and bad'. However, it was not the end consumer demand of a market integrated economy that informed the decision over whether an enterprise was either good or bad. It was the political concerns of those who govern: the Chinese Party élite and the central government *apparatchiks* who administer in their name.[42]

Understandably, during the 1989–92 period of economic rectification, the managers of the Second Automobile/Dongfeng group were as willing as any other managers of China's large advantaged enterprises to promote the argument that small enterprises did not have a sufficient level of technological investment and therefore were unable to ensure the rational use of scarce raw materials. It was an argument that left the question of the type of enterprise which was to be subject to merger or closure dependent on whether or not the producer made what was deemed to be good use of producer consumption needs. For their part, the far less powerful client enterprises could only point out that the larger advantaged enterprises were enjoying 'double protection'. The advantaged state-owned enterprises had been in receipt of government subsidies and financial rescue packages administered in the form of bank loans that were to be used to provide enterprise circulating funds and to clear away long standing debts.[43]

No more sunshine

In spite of recognising that during reform competition between enterprises had been unfair and that they had benefited disproportionately from government policy and financial negotiations, by 1990 the Second Automobile/Dongfeng managers started to complain that they were not being treated as well as they would like. They complained of the increase in direct state regulation saying that 'again the monkey rides the tiger' and they felt the loss of their previous giddy bid to expand constantly the productive capacity of the group. They said that they 'could not see the sunshine anymore'. One of their leading economists described the period as 'unpredictable and unbearable': a period when the central leadership had its foot firmly on the economic brake, rather than the accelerator.[44]

By 1990 the majority of the large state-owned enterprises had been obliged to petition the central government (either through local government administrations, or directly) for funds or loans to be used to clear the debt-chains that they had developed. The Second Automobile/Dongfeng group was not an exception. The period of economic rectification had considerably exacerbated what had become known as the debt-chain problem (sometimes referred to as the debttriangle problem). It had come about when the management of state-owned enterprises found themselves very short of circulating funds. They failed to pay their suppliers and the suppliers in turn were then unable to meet their financial commitments.[45] Moreover, the economic problems promoted and generated by the 1989–92 period of economic contraction were not confined to the problem of enterprise debt-chains. They also included a persistently slack market; state enterprises stock-piling unsold products; increased local protectionism; the significant increase in unemployment resulting from the merger and closure of the smaller state-owned and collective enterprises; a growing financial crisis in government funding at both central and provincial levels and a substantial increase in the real national deficit. Many of these economic problems were not new. What was new was the extent of the problems. They were in no small part a product of state-enterprise behaviour during China's first decade of reform, particularly during the latter half of the 1980s, followed by a drastic and prolonged period of central government induced contraction of productive capacity.

China's period of economic rectification demonstrated that having established an over-extended production capacity and having exhausted usually available funding channels, enterprises will resort to increased use of inter-enterprise credit as a means of meeting their production requirements. Moreover, in the face of delays and a significant reduction in enterprise taxation receipts, the Chinese government (at both central and provincial level) delayed, only partially paid, or did not pay, government subsidies to state-owned enterprises. This meant that the debt-chains between enterprises were then extended to include central and provincial government administrations and that the practice of using the banking system and government bonds to plug government financial responsibilities was exacerbated.[46]

By the beginning of 1992, the problems of enterprise and government financing and increased unemployment were in urgent need of address. At this time the crisis in enterprise and government financing resulted in a domestic deficit consisting of three parts. One part was 'the 20.2 billion yuan deficit shown in China's financial books'; the second was the national deficit consisting of 'government debts to banks and enterprises' potential losses'; and the third comprised enterprise and local government debts to banks and higher level government administrations.[47] Debt was also 'hidden' within the accounting systems used by banks, government and state-owned enterprises. During this period the Second Automobile/Dongfeng conglomerate did not find that it had to stock-pile unsold product, but it did find that enterprises that had purchased vehicles from its plants were either unable to meet their financial obligation or were very, very slow to pay. This was why, at this time, the management especially favoured the sale of the vehicles it had produced to individual households, particularly those located in the richer southern and eastern sectors of rural China. During this same period, enterprise management found that they were short of circulating funds and so like many other state enterprises in the same position they were keen to use barter in order to access supplies.

The non-payment of government and enterprise financial obligations and non-performing inter-bank loans drawn down by the large state-owned enterprises was not new either. Again, what was different was the extent of the hidden debt. Budget deficits have been a part of China's monetary expansion and corresponding growth in productive capacity and so too, has the increased use of credits by the banks. Even during the period of relatively prolonged and aggressive economic contraction that followed the 1989 Tiananmen Incident, the situation continued to be one where the banks were 'eating out of the big rice pot' of the central bank. The latter was fed by the Ministry of Finance, while local government administrations and the large state-owned enterprises were continuing to eat from 'the big rice pot' of the specialised banks.[48]

When one considers disciplining the financial demands made by state-owned enterprises on the banking system, particularly the large advantaged state industrial enterprises, it is clear, as I have argued, that production efficiency was not the criterion used to decide whether enterprises should be granted further funding or whether, alternatively, they should be either merged or closed. At the same time, China's Party/state leaders wanted to overcome the burgeoning problem of enterprise debt-chains and losses. At the time of the 1992 return to progressive reform it was the leadership's concern over the political consequences which could be expected to flow from closure of large advantaged state-owned enterprises that had decided which policy initiatives would be adopted. The managers of the Second Automobile/Dongfeng group did not expect that their metropolitan enterprises would be closed, but they were no longer able to expand in the same manner as they had previously. They were denied the avenue of growth that had been predicated on incorporating smaller enterprises into their conglomerate and they were no longer in a position to undertake the careering rate of expansion based on fixed asset investment that they had pursued during the latter half of the 1980s. Obviously they 'could not see the sunshine', nevertheless, today, the complex web of factories, enterprises and projects that make up the Second Automobile/Dongfeng conglomerate is again expanding and a substantial proportion of this expansion is attached to incorporation, but it is not of domestic manufacturers *per se*. It is by including foreign invested projects, connections to suppliers that may well encompass foreign investment and technical expertise and investment in an increasing number of limited liability share-based companies. The conglomerate has also had limited liability companies carved from enterprises in the group and, at the same time, is well on the way to becoming a joint stock corporation. The shares issued have continued to represent a useful flow of income that is somewhat removed from direct government regulation and control.

Share issue is not new to the Second Automobile/Dongfeng corporation. As I have already noted, in the latter 1980s share issues were used as an avenue for raising investment and operational funds that consisted primarily of the direct transfer of investment funds from other state-owned enterprises and to some degree from the personal savings of workers. What is new, is the formation of discretely owned shareholding limited liability companies. They are to be formed only after central government agencies have effected an exhaustive auditing process. It is a part of a newly constituted process of restructuring the ownership profile of China's state enterprises. This is the same process that has led to the advice that enterprises with good prospects should raise funds from society and at the same time absorb capital from abroad. The issue of Second Automobile/Dongfeng shares on the Hong Kong stock exchange falls into the latter category.[49]

STATE ENTERPRISE REFORM SINCE 1992: LANDING SOFTLY WHILE DEVELOPING A MARKET ECONOMY

Hardening the budget constraint

In the period since the 1992 return to progressive reform policy the Chinese leadership élite have focused on strengthening rules and regulations intended to harden the budget constraint and so discipline the self-interested claims of local government administrators and state enterprise managers. They have also sought to discipline economic growth through 'soft landings' that have been engineered using the central government's administrative apparatus, particularly the banking system and now, they are promoting the auditing and ownership restructuring of the state enterprises. Each of these measures is predicated on the Party élite's need to manage the opposition of interest now so clearly evident between state and local agents. With the 1992 return to progressive policy the immediate concern of the Chinese leadership élite was to ensure their continued economic success and so their continued political legitimacy. This meant that they had to first recognise and then manage the opposing interests of state and local agents in a manner that favoured both their short- and their long-term political objectives.[50]

With a legacy of a substantially increased national deficit, reduced taxation receipts, debt-chains and with a large percentage of state-owned enterprises stock-piling unsold goods and experiencing financial deficits (they were 'running in the red') bequeathed to them by the 1989–92 period of economic rectification, there was continued pressure on the leadership to use the centralised People's Bank to make tied sums available to the state-owned banks for distribution to state-owned enterprise circulating funds. These monies were to 'assist enterprises to repay long-standing loans' and even to assist in the payment of wages. In 1992, this situation resulted in the banking system following the leadership's newly-issued instruction to pursue 'flexible measures for extending loans' in the face of an increasing number of state enterprises defaulting on repayments. However, at the same time as these more flexible policies were being called for, the People's Bank was also being instructed to continue to strictly control and limit loans for capital construction. The latter, of course, would have been used for the expansion of state-enterprise fixed assets and production capacity that benefited local agents, albeit at the expense of the national interest.[51]

At the time of the return to progressive economic policy the Chinese Party élite were convinced that their firm control of the core of financial policy was necessary if social and political stability was to be promoted and their leadership continue, but very soon after January 1992, China's state planners began expressing concern over the situation where 'the central bank has experienced considerable pressure and difficulty in controlling currency issuance' and where 'Chinese banks [were] increasing credit and money supplies "by a large margin"'.[52] This concern over 'currency issuance' led to warnings about not repeating the critical inflationary situation experienced in 1988. It was advised that lessons should be drawn from that experience. Much was made of central bank lending quotas to its client state-owned banks, the so-called specialised and commercial banks.[53] There was the much-reiterated warning that 'no bank would be allowed to exceed its quota'. Stress was placed on the People's Bank's role in operating and policing loan quotas assigned to its client specialised and commercial banks. It was noted that this was 'the primary means by which the central bank controls money supply to offset inflationary pressure, which was showing no sign of easing' and which would have caused much more financial havoc, but for the increased rate of individual savings that became available for redistribution by the banks.[54] State economists argued that 'exercising management of credit limits . . . is based on current realities in China and that there is a positive role to be played by macroscopic financial management'.[55] This argument also recognised the extent of China's domestic deficit and, at the same time, inadvertently acknowledged that China's specialised banks had not been subject to hard budget constraint in relation to the People's Bank. It had become clear that, faced with the demands of local administrators and state-owned enterprise managers (particularly state-enterprise managers requesting funds in order to meet production costs, including wage payments), the client specialised banks had overrun their planned loan quotas and in that context enforcement of central bank loan quotas proved to be impractical. There were liquidity problems among the client banks and the People's Bank was obliged by the Ministry of Finance to again provide tied funds to be used to clear inter-bank debts.[56]

As Western economists have been keen to make us all very well aware, in a predominantly market-integrated economy, the government relies on indirect mechanisms for controlling the quantity of credit. Whereas in China, as is the case with economies in transition from centralised plan to market, where new financial institutions have had to be established, there has been uncertainty over the relationship between credit mechanisms such as discount rates, reserve requirements and commercial interest rates. Without overcoming the base problem of enterprise investment hunger and so removing the pressure on credit, China's leadership élite have felt an all-too-obvious need to have a reliable and effective means of braking the economy in the face of acute concern over growing inflation. But the control mechanism used has been a *very* blunt instrument. As I have noted and as was graphically illustrated during the 1989–92 period of economic rectification, cutting the volume of credit does not cut off those enterprises which have the lowest return. It forces those enterprises least able to service their interests to either be compelled (usually by self-interested local administrators) to merge with more powerful organisations or be closed.

Avoiding a hard landing

Party/state planners had argued that 'the basic spirit' of the banking regulations that were issued after the 1992 return to progress policy was to effect 'a top down change in the management mechanisms of enterprises', but it soon became clear that in terms of containing inflation promoted by the extension of productive capacity, this approach was no more successful in the immediate post-1992 period than it had been during the 1980s. The leadership and their state planners were then left to attempt to 'cool' the economy in the best manner available to them. Without the political urgency generated by the social unrest of 1989 and having more recently attached their political legitimacy to returning to the implementation of progressive measures for reform, they felt, I believe, unable to implement yet another period of harsh, contractive economic policy. This is why they chose instead to engineer an economic 'soft landing' for the Chinese economy, or what has more recently been referred to as 'a moderate tightening' of the economy.[57]

At this time, state administrators found it necessary to make much of their ability to avoid the 'hard landing' that the economy had been subject to in the period 1989–92. They boasted that such policy is not now 'consistent with objective reality'. The problem with their approach was the time that achieving a soft landing took to come to grips with the ever-rising rate of inflation. As late as the first half of 1995 the rate of increase in commodity prices remained at an estimated 21 per cent. It was not until the end of 1995 (two years after its initial implementation) that there were hopeful predictions that 'China's economy was now approaching a "soft landing"'. Self-congratulations could then be made over having 'correctly handled' the correlation between reform, economic growth and development and political stability and unity. Party/state administrators then argued that the reduced speed of economic growth and the reduced speed of increase in investment in fixed assets had demonstrated that 'the central government's macro economic regulation and control' had promoted political stability and unity. In other words, China's leadership élite had, by their own standard, been successful in managing the opposing interests of the state on one hand and local administrators and enterprise managers on the other.[58]

CONCLUSION

In post-reform China, the Communist Party leadership élite and central government administrators on one hand and local government instrumentalities and the managers of China's large state-owned enterprises on the other, have continued to pursue their differing and often opposing interests. In the latter half of the 1980s local government administrators and enterprise managers had found that the combination of economic reform and dissent within the central leadership had significantly weakened direct vertical control by the state and so had provided increased opportunity to advance their own agendas and interests. In other words, local agents realised that they had much to gain from milking and manipulating their relationship with the state: a situation that created outcomes that were unintended by the Party/state leadership and members of their central administration whose continued legitimacy rests on their ability to present themselves as governing in the national interest.

Obviously, the increasing autonomy of local administrative and enterprise manager decision-making varied across different local governments and different state-owned enterprises and it varied over time. As I have argued, in the latter half of the 1980s the management of large economically advantaged enterprise groups such as the Second Automobile/Dongfeng conglomerate were particularly successful in pressing their demands on the state. They were much more successful than the management of smaller state and collectively owned enterprises, many of whom had been attempting to piggy-back on the bargaining success of the larger enterprises. However in the period following the 1989 Tiananmen Incident, when those within the Chinese élite had their conservative policies cemented by the fear of social and political instability, local agents, even when they represented large and successful kingdoms, found that they were no longer able to be as effective as they had been in pressing their particular interests. By their own account they were unable to see the sunshine.[59]

Then, after the 1992 return to progressive economic policy, the investment in industrial fixed assets outside the plan again flagged the manipulation of policy and the economic gains that can be wrung from soft budget negotiation. Almost two decades after the Deng Xiaoping leadership introduced their programme for economic reform the need to 'put state-enterprise financial relations on a more regularised, depersonalised, "hands-off" basis' remained. Though in the 1990s the negotiation and manipulation of policy that flags the opposition of interest existing between the Party/state on one hand and local agents on the other has not been at the expense of the state appearing to be unable to control the demands made upon it. In other words, during the 1990s, China's élite have been able to project the appearance of having much more control than they had during the latter half of the 1980s. They have presented a united face.

2 Managers' interests versus workers' interests

Labour, housing and welfare reform

> The implementation of the [January 1995] labour law provides the deepening of enterprise reform with some rules of the game and establishes a statutory climate for the creation of a modern enterprise system. It gives the drive to protect legitimate worker rights and interests a legal basis. It is a legal weapon to be used in helping trade unions fulfil their responsibilities. It sets the standard for harmonizing labour relations and it establishes a legal framework for the labour system under a socialist market economy.[1]

In China in the period prior to reform and also for some time after the 1978 introduction of reform, there was, as Walder noted, no clearly discernible opposition of interests between enterprise managers and 'their' workers. This meant that China's leaders were able to identify and boast a common interest between enterprise managers and workers. Managers had negotiated with relevant government instrumentalities in order to satisfy their own *and* their workers' interests. However, this situation did not last. As I have already argued, within the province of China's state-owned enterprises a second line of interest opposition soon developed and by the latter half of the 1980s the manager/worker opposition of interests had come to reside incongruously alongside enterprise managers' concern to care for their workers. However, this initial coexistence of paternalistic management and a growing tension between managers' and workers' interests proved to be a temporary phenomenon. The well-established cooperation that ensured that workers should be cared for by enterprise managers was first eroded and then eclipsed by the aggressive nature of the developing manager/worker tension. During the latter half of the 1980s this was happening even as enterprise managers were choosing to raise the real wages of their workers in opposition to central government guide-lines.

In this chapter I discuss the industrial labour policy that has been adopted by China's leaders during the decade 1985–95. Again, I pay particular attention to the manner in which the management of China's state-owned enterprises have implemented policy, using the Second Automobile/Dongfeng corporation's approach as an example. This corporation was used to trial wage reform and bonus payment initiatives (trialed at the corporation in 1985) and housing reform (begun in February 1988). Today, it is at the forefront of the process whereby discrete sections of China's largest and most advanced state-owned enterprises will have their ownership profile restructured.[2]

The ownership restructuring of China's state enterprises will produce an élite stratum of workers employed by shareholding, publicly listed limited liability companies or by joint stock corporations, but this reform can only take place in the context of China's state-owned enterprises increasingly divesting themselves of both their surplus labourers and their welfare responsibilities. This means that the opposition of interests between state enterprise managers and workers will continue to sharpen and will require the Chinese leadership to both provide ever greater and more detailed legal protection for China's industrial workers and to slow the implementation of their ownership initiative. The Chinese Party élite have found that they must appear to represent the interests of workers if they are to continue to be in a position to present themselves as the custodians of their people's interests. The enactment of laws and regulations to ensure that enterprise managers effect the 'proper' treatment of industrial workers provides a convenient avenue for the leadership's representation of the constituency (the Chinese people, particularly workers) that they claim to represent, though, as I have noted, this resort to legal protection of workers' rights and interests can do nothing for those who find themselves unemployed and outside the factory gates.

LABOUR CONTRACTING AT THE SECOND AUTOMOBILE/DONGFENG CORPORATION

Workers, welfare and contracting

Though it was not as obvious when it was introduced in 1986 as it is today and though at that time it was not imposed on existing enterprise workers, the system of labour contracting was the first step in developing a market for labour time. It began a process that has eroded state workers' 'right' to life-time tenure of employment and it also paved the way for the current push to divest state-owned enterprises of their welfare responsibilities.[3] And, in the case of the Second Automobile/Dongfeng corporation, and many other large state-owned enterprises, the introduction of the labour contract system not only breached Chinese workers' expectation of life-time employment and paved the way for the process of divesting the corporation's managers of their welfare responsibilities, it also spelt the end of the practice of automatically adding workers' children to the group's work-force. The sons and daughters of Second Automobile/Dongfeng workers had expected a corporation position once they had completed their enterprise sponsored middle-school education. Their tertiary education was then usually commenced once they had been afforded their workplace position.

Initially, the Second Automobile/Dongfeng group's work-force was drawn from two sources. The first from industrial workers and managers transferred from the older and well-established First Automobile group and the second from educated youth that had been 'sent down' to the countryside during the Cultural Revolution. By the time I was living and working at the Second Automobile/Dongfeng headquarters in Shi-yan city in 1985 many of the latter group of workers had resumed their education, gained tertiary qualifications and had taken up enterprise management positions. By this time, they, together with their colleagues who had transferred from the First Automobile group, were in a position to reflect on their good fortune. It had become increasingly apparent that they were members of China's worker aristocracy. They were employed by a large economically favoured state-owned enterprise. At this time the Second Automobile/Dongfeng conglomerate was considered to be a member of China's élite top ten state-owned enterprises. Management had ensured that they were in a position to provide larger than average bonus payments and superior welfare services to their staff and workers. Not only were the Second Automobile/Dongfeng workers receiving a special 'hardship' allowance for living in a relatively remote area of north-western Hubei province, they also enjoyed a high level of healthcare and education facilities and the use of a well-heeled stock of housing and other urban services, including shops, a zoo and amusement park and enterprise sponsored music groups and sporting teams. Moreover, once government regulations and taxation policy had limited worker bonuses in money form to no more than a sum equal to three months' annual basic wage, enterprise management saw fit to provide for its own family by providing such advantages as steam heating for enterprise housing (the steam was drawn from the enterprise coal burning electricity plant), the very latest model shower heaters purchased in Shanghai, oranges brought north and supplied to workers during winter, cultural troupes from Beijing, a very large and well-appointed sports stadium and increased funding for middle-schools and the corporation's workers' university. The latter was afforded access to foreign currency for the purpose of importing its own engineering and language teaching staff.[4]

When the Chinese leadership decreed that all new employees of state-owned enterprises must be employed using the labour contract agreements, the management of the Second Automobile/Dongfeng group reacted to this edict in several different ways. First they used the policy initiative to give greater weight to their long standing argument with the Hubei provincial government over the number and type of workers the enterprise was obliged to accept from the provincial labour bureau. They then saw fit to award labour contracts for a considerable period of time, for example five or eight years. While this appeared to be a case of management acting on behalf of their workers, it was also a way of reacting against the continued heavy-handed approach of the provincial labour bureau and of ensuring that the enterprise continued to secure workers who possessed scarce labour skills. For some time Second Automobile/Dongfeng corporation managers had been using their well-heeled welfare services (particularly their stock of relatively new housing), extra wage and subsidy payments, working conditions, and growing enterprise prestige to attract skilled workers from other enterprises, often as a result of long and hard negotiation with the enterprise that had been employing the worker in question.

The two most prominent complaints that enterprise management made in the wake of the edict to introduce labour contracting for newly employed workers were that they continued to have a relatively large percentage of their work-force employed under the previous tenure system and the very common grievance among state-owned enterprise leaders that in spite of their best efforts, the local (in this case the Hubei provincial) labour bureau was continuing to 'recommend' workers to enterprise management, or more correctly, to foist unwanted workers on to the enterprise payroll.

Moving workers side-ways

At the same time as labour contracting began to be implemented, other features of worker employment were becoming only too clear. One was the practice of moving those workers who were deemed to be less productive (predominantly older women workers) side-ways and another was employing under short-term contract, skilled workers who had retired. In the first case there was considerable disgust among members of the enterprise work-force over the treatment of loyal long-standing workers when a large group of older women workers were moved from the enterprise's main truck producing factories to the new cap factory that management had seen fit to open. The overwhelming understanding was that enterprise managers were not interested in producing head-wear *per se*. They were interested in soaking up less productive workers whom at this point in China's reform process, they were not free to dismiss, but who could be re-positioned so that their wage entitlements and bonus rates were decreased and their claim on welfare provisions reduced. By way of contrast, the fate of highly skilled engineers who had retired was much brighter. They received their enterprise pension, continued to live in the enterprise housing that they had been previously allocated and had uninterrupted access to enterprise provided services and they were able to earn fees for contracted services. For their part enterprise managers gained the advantage of being able to access skills that they required while not being obligated to a long-term contract, not having to shop and negotiate in order to obtain suitably skilled personnel from other enterprises and not having to meet the costs associated with housing and servicing a newly employed worker. After all, the enterprise was already obliged to provide for its retired workers.[5]

Keeping workers on their toes

When the labour contract system was introduced both government administrators and enterprise managers envisaged that several advantages would be gained. The first was that it would discipline the labour force. The knowledge that your contract would not be renewed if your performance has not been satisfactory was intended to give workers pause for thought. It was also intended that work performance would determine the terms on which a contract was renewed, even in the case of satisfactory performance. It was said that this approach to 'breaking the iron rice bowl' would not only provide greater labour discipline and productivity, but also flexibility and mobility and that the respective responsibilities of labour and management would be more clearly defined. This approach has continued. Enterprise managers interviewed in 1993 and 1994 were very clear about the benefits of labour discipline predicated on undermining worker security. They announced that – 'Yes, we are purposely introducing a sense of uncertainty and risk' and argued that they wanted to put workers under pressure because this would ensure that they developed 'a good work-force with good work attitudes'.[6]

Even before the labour contract system was introduced some enterprise managers had seen fit to adopt Tayloristic attempts to squeeze greater productivity from workers. For example, in 1985 the director of the First Plastic Factory in Shijiazhuang (Hebei province) implemented a 'full-load work system' based on Taylor-type provisions that, in 1987, Premier Zhao Ziyang praised as being an innovative way to improve the economic efficiency of the state-owned enterprises, but from the vantage point of the present, we can see that this attempt was premature. The tension between the interests of enterprise managers and the interests of their workers had not yet matured to the point where it could bear such bald expression. It was much resented by the enterprise workers and was quickly rescinded by management.[7] Nevertheless, the attempt to squeeze the workers demonstrated enterprise management's evident interest in promoting worker productivity as did practices such as the Second Automobile/Dongfeng managers' measures to move workers side-ways and so clear the way for more productive workers to take on tasks central to enterprise productivity. When practised, these innovations did not yet threaten workers with outright unemployment. At this relatively early stage in China's reform process they were most likely a manifestation of management's attempt to meet central government set productivity goals and so please relevant government administrators. This would increase their future bargaining power and advantage their enterprise.[8]

FROM LABOUR FAMILY TO LABOUR MARKET

Stealth unemployment: blunting the opposing interests of managers and workers

In 1986 and 1987, in spite of the introduction of labour contracting, the Chinese leadership had continued to articulate a pride in its ongoing commitment to achieving full employment. Though there were urban young people waiting for jobs, urban unemployment had not reached the heights that the current drive for enterprise efficiency has now engendered. In spite of enterprise management's obligation to implement a system of unemployment benefits for their contract workers (from 1986 they were required to set aside a sum equivalent to 1 per cent of the annual standard gross payroll under the administration of local government labour agencies), at this point the expectation of secure life-time employment did not appear to be breached. Though labour contracting was widely used, Chinese state-owned enterprises remained bloated with workers. 'Unemployment on the job', later to be referred to as 'stealth' unemployment, remained in both the state and the collective sectors of the economy. Labour bureau administrators and enterprise managers alike had little enthusiasm for dismissals resulting from labour contracting and at the same time, industrial workers had little incentive to move away from their employment in state-owned enterprises. Their jobs still provided an apparently high level of employment security in combination with superior welfare services when compared with employment offered by the collective and the growing private sectors of the economy. The latter offered far less employment security and little or any welfare provisions. At this time, the majority within the Party élite continued their concern over 'the disruptive potential of urban unemployment', even though it was recognised that the previous 'too rigid and centralised distribution of labour [time]' was 'reproducing unacceptably low levels of labour productivity and retarding technological development' and so the faster this situation could be changed the sooner the problem of low labour productivity would be overcome.[9]

Continuing the practice of administrative distribution of workers in accord with immediate political priorities, rather than in accord with the dictates of market indices or even with reference to quantitative profit generated, functioned to smooth over and blunt the developing opposition of interests between enterprise managers and workers. The impression given to enterprise managers during the latter half of the 1980s was both that representatives of the Party/state were primarily concerned to avoid large-scale urban unemployment and that labour productivity gains were to be implemented within this framework. This meant that provincial government administrators and enterprise managers were still free to continue to count the success of their endeavours in terms of the size of their kingdoms, even when it was recognised that the administrative (political) distribution of workers would retard real economic growth. In this context it is not surprising that by the end of the 1980s, 'despite almost a decade of reform, the situation in state enterprises remain[ed] virtually unchanged: high job security, low labour productivity, and a weak link between performance and compensation'.[10]

Labour contracting: a controversial policy

Though the introduction of the labour contract system had preceded the then Party General-Secretary Zhao Ziyang's October 1987 promotion of economic reform, he had had a long interest in effecting labour reform based on labour contracting and so it became a central and controversial plank in his progressive reform programme. In the context of the tension within the Party élite over the end goal of reform, this reform was particularly controversial. Among the plethora of initiatives that Zhao had put before the Thirteenth Party Congress held in October 1987, was the progressive reformers' intention to promote the policies and institutions required for the development of a labour market. In the wake of the Congress, this intention received a disproportionate amount of attention from the conservative members of the Party élite. It provided considerable leverage for criticism. The conservatives were able to use the progressive reformers' trampling of the Marxist holy ground of cooperative labour relations as the basis for abrasive criticism. Nevertheless, after the three-year delay imposed by the post-Tiananmen period of economic rectification, development of a labour market was recognised as a fundamental and vital component in the bid to realise the goal of developing 'a socialist market economy'.[11] In the period since the 1992 return to progressive economic policy the development of a labour market has proceeded largely unimpeded by the leadership's squeamishness, wrangling and ideological concerns in relation to the commodification of labour time. The objections that were expressed in the late 1980s are no longer heard.[12]

In the 1990s the Party/state leadership's industrial labour policy is intended to promote a clearer definition of manager and worker interests, responsibilities and obligations in a situation where the 'web of interests' that Walder had identified as formerly existing between enterprise management and workers has already been severely eroded. No arguments are now put forward publicly expressing either objection to labour reform on Marxist theoretical grounds or on the basis of specific concern over the damage that labour reform will do to 'the important values of collectivism and loyalty to the firm ("loving the factory like one's family" [familyism])' that had been a past feature of cooperative manager/worker relations within China's state-owned enterprises. Even perceptive argument, such as that presented by the former head of the Chinese Academy of Social Science's Industrial Economics Institute, Jiang Yiwei, is now ignored. Jiang noted that 'the economic reforms have been bringing about a shift of power within the enterprise in favour of managers' and so 'care should be taken when implementing labour reform'. Rather, the extent of the separation of interests between management and workers has been made clear by the central government's perceived need to protect the rights of workers through the enactment of the regulations that by January 1995 had matured to become the Labour Law now in force.[13]

Renegotiated terms

Today, with the benefit of hindsight, we can see that, in spite of the immediate appearance to the contrary, the 1986 introduction of the labour contract system did breach the ethos of guaranteed life-time employment for China's state enterprise workers. It began the process of renegotiating the terms of the implicit contract that had hitherto existed between the Party leadership élite and the urban industrial labour force and opened the door for the future market distribution of labour-power and the unemployment that is attendant on this development and, at the same time, it provided both a precedent and a model for direct worker contribution to welfare payments.[14]

HOUSING REFORM

An exception to the rule: a reform initiative not delayed by economic rectification

It is not surprising that, in the wake of the 1989 Tiananmen Incident the push for developing a labour market that had been promoted under the banner of Zhao Ziyang's progressive reform package was put on hold by a leadership shaken by social unrest and now firmly united behind conservative economic policy. What was surprising was that at the same time as the Second Automobile/ Dongfeng group was attempting to cope with the dire economic effects of the conservatives' programme for economic rectification, the corporation's managers were also subject to pressure from the Hubei provincial government to effect further housing reform. It seems that housing reform like enterprise stock issues, was to be an exception to the leadership's delay in implementing policies promoted under the auspices of Zhao Ziyang's progressive reform package. It is tempting to argue that this may have been because housing reform pre-dated Zhao's 1987 programme, but this is not a convincing argument. A number of other reform initiatives, including labour contracting, were put on the back burner during economic rectification. They also pre-dated Zhao's progressive economic *putsch*. These reforms were not reversed. They did not raise much-valued funding for the state-owned enterprises and so were just left to simmer.

Housing reform had been put forward by Deng Xiaoping as early as 1980 when he declared that people should realise that housing, 'traditionally viewed as a welfare good, should become a commercial commodity'. Then between 1980 and 1984 it did not extend beyond being 'basically a ministerial-level concern'. Nevertheless, Deng had established himself as a 'chief engineer' of this policy 'in the sense that he provided the original ideas and the framework for housing reform' and it was widely held that subsequent housing initiatives had been implemented under Deng's influence and so with his approval.[15] By 1985 and 1986 when Zhao first took an active role in the Rent Reform Leadership Group of the State Council and in the housing reform trials that were to be implemented, it had become clear that Zhao, albeit under Deng's leadership, was actively associated with housing reform initiatives. He had publicly embraced and promoted housing reform and he then took it on-board and included it in his October 1987 programme for deepening and accelerating reform. In May 1987, just months before he had formally announced his progressive reform programme to the Thirteenth Party Congress, Zhao had endorsed the policy initiatives concerning housing put forward by then Secretary-General of the State Council, Chen Junsheng. By February 1988 a programme for housing reform had been enacted.[16] It included measures to raise housing rents, to effect reform of housing ownership and to promote the establishment of separate housing funds in state-owned enterprises as well as provisions charged with creating a healthy flow of funds (from wage and rent increases) into these housing funds.[17]

For its part, the Hubei provincial government had had a long standing involvement in housing reform. As early as 1986 it had been party to trials held in its provincial capital Wuhan, and then in the wake of the official February 1988 State Council authorisation of housing reform, had pressed Second Automobile/Dongfeng group managers to raise housing rents and to sell state enterprise housing stock. In response to this pressure they undertook to implement housing reform beginning in 1988. Nevertheless during 1991, possibly in light of the original intention that housing reform would be completed within three to five years from 1988, the Second Automobile/Dongfeng corporation's managers were again under pressure from the Hubei provincial government to further their housing initiatives. This meant that they were obliged to institute further reform in the face of the severe credit restrictions and economic disarray of the 1989–92 rectification period and, at the same time, they had to cope with considerable worker resistance. The latter was understandable when it is remembered that workers at Second Automobile/ Dongfeng enterprises had gained considerable benefit from their system of housing distribution. While China's state-owned enterprises, particularly the large advantaged corporations such as the Second Automobile/Dongfeng group, had been providing their workers with housing (the group had more than doubled its housing stock in the period 1980–88 and had also greatly improved the standard of housing during this period), government administrations and less advantaged state-owned enterprises were unable to provide in anywhere near such an adequate fashion for their workers. Collective and privately owned enterprises usually did not provide housing at all. Their workers were thrown back on local government resources for their housing requirements. State-owned enterprise workers had usually paid around a mere 1 per cent of their monthly incomes for housing: an amount that failed to meet even a small portion of the cost of housing maintenance.[18]

World Bank support for housing reform

No doubt driven by their concern to spread the ideology of free market integration, in 1991 the World Bank executed a study of China's urban housing and concluded that 'there is a need to cash out housing in-kind benefits'. The study provided icing for the Chinese leadership's already much publicised intention to implement a housing reform programme that would either be completed by 1991 or, at least, would be within striking distance of completion by 1993. Today the World Bank is continuing to underwrite loans for housing. It began to implement this policy in 1991. Under China's five-year plan – 1996–2000 – the Bank sponsors housing mortgages made available through the Industrial and Commercial Bank of China. The World Bank's administrators stipulate that these mortgages only be made available 'for genuine home owners'. These loans are to be based on an Industrial and Commercial Bank mortgage of up to 70 per cent of home value repayable over a maximum period of ten years. The loans are only to be advanced on the basis of guaranteed security. The optimistic argument presented by the World Bank's officials is that 'the more attractive terms' of their scheme will 'see a rise in the number of new home owners'. A guide to the extent of the implementation of urban housing reform is given by the Beijing Municipality figures that estimate that, to date, around 60 per cent of workers under its administration have taken up the option of housing ownership. Though it should also be noted that this is in the context of the

Municipality's innovative and partially subsidised market approach to housing reform. Municipal administrators are currently selling housing stock at market prices to high-income families, at cost price to middle- and lower-income households and to those people who 'have real difficulties' in buying houses, they will sell at a special lower than average price.[19]

Worker contribution to housing cost

In line with the central government's housing reform guide-lines, in the latter half of the 1980s the Second Automobile/Dongfeng corporation's management increased rental for housing at the same time as implementing housing ownership reform. Both initiatives were predicated on direct worker contribution to cost. In the case of housing ownership reform, the arrangement during the period 1988–91 was that a cash contribution was required from the worker, together with a specially allocated bank loan combined with a direct enterprise contribution to cost of 'purchasing' a housing apartment. The usual form of this arrangement was approximately one-third worker cash input, one-third bank loan and one-third enterprise subsidy plus a money wage subsidy to assist in off-setting the saving funds that the worker had been obliged to use for housing purchase and the deduction from wages that the bank loan required. This money was in effect a housing purchase incentive, even a bribe by management in order to ensure worker compliance with the housing policy that local administrators were pressing on them. It should also be noted, however, that these funding arrangements were in a form consistent with the housing reformers' bid to make the housing subsidy received by state workers an open rather than a hidden subsidy and it was useful in creating the government ideal of 'a healthy circulation of funds' into the enterprise housing fund.[20]

Ironically, after it had been imposed on the Second Automobile/Dongfeng management, housing reform became an asset to them. It came to provide another conduit (parallel to raising bond monies and the limited floating of share issues that I have discussed in the previous chapter) for individual savings to be drawn for use by China's state-owned enterprises. In other words, it opened another avenue for government mobilisation of individual savings and it did this without the need to siphon these savings through the banking system and so without any need to adhere to the rules and regulations associated with bank funds. Central government sources had been noting that 'low housing rents have diverted money in [to] the hands of the

Chinese people'. By promoting a programme for housing reform that ensured that a significant proportion of funding for housing is drawn from individual savings, that diversion of money into the hands of the Chinese people was to be reversed. In theory, funding would be provided for infrastructural development in response to housing demand without use of either government or state-enterprise investment funding, but this was a best case scenario. In many state-owned enterprises the outcome was that funding from the sale of enterprise housing (like the funds raised through the sale of other enterprise assets, including land use sales) was able to find its way into general enterprise income and even when this did not happen, other enterprise funds were now freed from the need to invest in housing stock. The result was that the provision of untied funds to management provided a sweetener for the trouble of implementing unpopular housing reform policy, while at the same time ensuring that a hidden tax payment was pushed on to the shoulders of the workers. Nevertheless, it should be noted that once enterprise managers had offered cash incentives to their workers in return for their participation in housing reform, they had not gained as much financial benefit from the reform as had first been thought possible. Payment of rental subsidies and housing purchase incentives turned out to be a larger than originally intended part of workers' money wage package. This served to provide a greater proportion of the real wage in cash payment, but it also constituted an enterprise commitment which mortgaged future enterprise income against the immediate funding gain from the sale of existing housing stock.

Further government pressure for housing reform

The 1992 return to progressive economic policy meant that the Second Automobile/Dongfeng group's managers were subject to yet another surge in government pressure to promote housing reform. The managers responded by further standardisation of their enterprise housing policy and by the end of 1995 a system had developed whereby enterprise staff and workers who 'chose' to buy their housing requirements would wait until they believed they had realised their promotion prospects. This was because the size of the housing that you were entitled to buy had become directly related to the seniority of your employment position.[21] Once purchased your home could be inherited by your spouse, child or children, but it could not be sold on the open market. If another place of residence was required through employment transfer to another location within the Second Automobile/Dongfeng conglomerate or to another enterprise, then the home must be sold back to the corporation at its purchase price (the 1995 purchase price was as low as eight to ten thousand yuan if you paid the price as an initial lump sum, rather than deciding to pay a higher price over time using deductions from wages). While owning the home the resident is responsible for maintenance and repairs. This is really a partial ownership scheme in which the corporation's workers are urged to participate.[22]

A member of the Second Automobile/Dongfeng group's work-force put it to me that this was a very good system, not least because it ensured that maintenance was carried out on housing and because it prevented the problem of the same list of the most senior and well-connected people requesting a housing transfer every time the enterprise saw fit to construct a new block of apartments. The list virtually stayed the same each time: 'the same people at the top and the same people at the bottom'.[23]

A system of partial purchase

Obviously, in view of the price of new housing and the enterprise management's unwillingness to allow house 'owners' to sell their apartments on a market, the Second Automobile/Dongfeng group was continuing to subsidise the cost of worker housing. As I note above, the worker has effected only a partial purchase of the property. Indeed, management is apparently playing two games at once. Monies are being raised through the 'sale' of housing to enterprise workers and housing reform is taking place, but at the same time, seniority within the enterprise work-force continues to be re-enforced and the worker's real wage continues to be subsidised. This subsidisation includes both open and hidden subsidies. The latter involves access to enterprise facilities and services: a situation that becomes very clear when it is noted that for senior members of enterprise staff telephone connections to homes are paid for (in 1995/6 figures this amounted to a one-off salary subsidy of around 1,250 yuan) and that enterprise workers pay approximately one quarter of the amount paid by citizens not attached to the enterprise for both their water and their electricity. Moreover, since shortly after the 1984 construction of a coal-burning electrical generating power-station, the piped steam heating that I have previously mentioned, has been provided without cost to almost all the apartments of core enterprise workers.[24]

Housing reform: a first step

Though it was not made explicit at the time, like the labour contract system instituted two years earlier, the nation-wide programme for housing reform that began in 1988 was a vital first step in a far more comprehensive reform initiative. In other words, while the labour contract programme was the first step in developing a market for labour, housing reform was the first step in the process of divesting the state-owned enterprises of their welfare responsibilities. Today the Second Automobile/Dongfeng group's managers find that they, in common with the rest of China's state-owned enterprise management sector, must divest the enterprise group of all welfare responsibilities. Even in the face of increased wage payment in money form, the process of divesting the state-owned enterprises of welfare responsibilities is expected to reduce enterprise expenditure. Nevertheless, from the point of view of enterprise managers, the welfare divesting process is a double edged sword. As in the case of the still incomplete housing reform, the pressure on scarce operating funds will be reduced and one-off sales may even raise funds, but at the same time, enterprise managers will find that their discretionary power has been eroded.

DIVESTING THE ENTERPRISES OF THEIR WELFARE RESPONSIBILITIES

Separating out service provision

Beijing is now insisting that state enterprise funded and operated institutions such as schools, medical facilities, childcare centres, dining halls, and guest houses, operate using separate accounting systems. In other words, the subsidies that these facilities and services have received from their parent enterprise are to be phased out. The service providing companies that result from this policy are to stand alone. They are to operate as separate accounting entities.

At the Second Automobile/Dongfeng conglomerate the process of divesting the enterprises of their welfare responsibilities, or as it is sometimes put, 'lightening the enterprises of their social burden', is well underway. But at the same time, these are facilities in which enterprise management has invested heavily, particularly during the enterprise boom period of the latter half of the 1980s. The services that enterprise management have provided for their workers have taken up a significant proportion of the profit-related investment available to the enterprise. They have been a badge of management success and of the status of their enterprise kingdom. As I have noted, even as the introduction of the labour contract system was driving a wedge between management and workers, investment was being made available to provide for the development of worker facilities. Not only did enterprise managers continue to derive status from providing for their enterprise family, they were also able to continue to use the superior welfare facilities of their enterprise or enterprise group to attract workers who possessed scarce labour skills. This is investment and opportunity that enterprise management has been told it must now relinquish.

Welfare services as wage subsidies

In the past, as is obvious by the discussion above, a large portion of a Chinese worker's real wage has been met either by the direct provision of services (even when in return for a token payment), or by the provision of services at below market-clearing rates. Indeed, it has been 'the incomplete accounting of subsidies, especially subsidies of publicly provided housing' that has been the main cause of hidden (or at least 'significantly underestimated') urban income and of the gap between urban and rural household incomes. While wages have been estimated to be 'the single largest source (44 percent) of urban income . . . aggregate subsidies [have been identified as] a close second to wages as a proportion of income'. A recent study by a group of China scholars from various countries has estimated that subsidies account for 39 per cent of urban workers' income, with housing accounting for 18 per cent of this 39 per cent.[25] These are figures that differ somewhat from those presented in the Chinese government's own 1995 estimation of state worker subsidies. In the latter it was estimated that 'at present, the amount of funding defrayed by the state and enterprises for social security' is equivalent to 54 per cent of the total spent on wages. The breakdown of this figure is: housing – 22 per cent of social security funding; old-age pensions – 20 per cent; medical care – 10 per cent; and unemployment insurance – 1 per cent, with work-related injury insurance taking up a further 1 per cent. The percentage contributed by workers is still estimated to be very low. It is a mere 3 per cent.[26]

In light of the above understanding of the economic significance of the role of subsidies to China's urban industrial labour force (regardless of which set of figures are considered), it is obvious that not only has national per capita income usually been significantly underestimated, but the forthcoming removal of enterprise and government subsidies to China's state enterprise workers has the capacity to alter significantly the present pattern of income distribution if the money wage of the workers is not substantially increased. It is not surprising that both state enterprise managers and the government decisionmakers have been keeping a careful watch on the income of state industrial workers. Enterprise managers have seen fit to provide the workers with cash subsidies such as the Second Automobile/Dongfeng group housing subsidy that I have discussed above. These subsidies have been in return for their cooperation in the reforms that they (the managers) have been pressured to implement. In other words, state enterprise managers have been pressured to effect enterprise welfare reform, but they have then had to bridge the evermore clearly defined division of interest between themselves and their workers. The use of money wage subsidies has provided this bridge. While at government level, there are now public discussions that focus on the question of 'how much will workers tolerate' and it has even been observed that inflation provides an opportunity to decrease the real wage of workers while not appearing to do so. The argument is that if inflation rises and money wages do not match this rise, then workers' real wages have decreased and the enterprise ratio of fixed investment to profit is likely to have increased. Divesting the state-owned enterprises of their welfare responsibilities must surely present government with the same opportunity for economic gain, that is, if enterprise management can be persuaded not to off-set workers' costs with open money subsidies.

The rising cost of welfare services

In the period since the 1992 return to progressive reform, Chinese economists and planners have consistently argued that, if state-owned enterprises continue to 'shoulder a heavy social welfare burden', it will be 'difficult for them to compete on a equal basis [in the market] with enterprises of other types'.[27] After all, the cost of providing welfare services is constantly rising. An example is the Second Automobile/Dongfeng experience with regard to the rising cost of housing during the 1980s that I have previously noted. Expectations are constantly rising, often with the agreement of a Party/state keen to promote its credentials as the provider of increasing living standards by announcing aims such as providing Chinese workers with eight square metres of housing space by the year 2000, when in the period 1978 to 1994 the average living space per person has already increased from 3.6 to 7.7 square metres. There is also the situation where, because there has been an active and 'successful' population control policy, China will enter a period of population ageing at the end of this century. The latter is a complex problem that many argue will become increasingly acute.[28]

Social security: connecting workers' rights to their obligations

At the same time as Party/state administrators are pressuring state enterprise managers to divest themselves of responsibility for worker welfare provisions, they are pointing out that there is a need for a 'sound' system of social insurance. They constantly reiterate their preference for the introduction of a system consisting of unemployment, healthcare and age pension insurance. Party/state sources argue that this will be 'the backbone of the basic framework of social security'. They point out that it is to be 'a key guarantee for preserving social stability'. In future, workers will be obliged to contribute to social insurance from their money wage: a situation that the leadership élite have applauded as one that overcomes the previous situation where a worker's rights were not connected to his obligations. Under the new system of social insurance, workers are to be made aware of the need to make provision for medical and other expenses and so, it is optimistically argued, their sense of responsibility will be promoted and 'unnecessary waste' will be avoided.[29]

Government sources recognise that a comprehensive system of social security insurance requires sound standardised legislation. Previous fund decentralisation is now to be seen as too diverse and unclear and without uniform coordination. It has offered too many opportunities for 'varying degrees' of misappropriation. Enterprise managers have been warned that 'social security fund surpluses must not [any longer] be directed to make up fiscal deficits'. Moreover, unemployment insurance funds must be clearly separated from pension funds and health insurance monies collected by enterprises from employees must be paid into an established health insurance fund. Fund management agencies are to issue health insurance cards to enterprise or individual insurance policy-holders and then healthcare would be provided by hospitals designated by the relevant health fund management agency. At the moment the situation is that within a given quota, patients would not be required to pay costs and if the expenses exceeded the given quota the individual patient would be required to pay a set percentage of the cost.[30]

Party/state sources argue that today the social security burden is to be shared 'by the state, enterprises, and individuals. It is to be pluralized'. The latter means that the funding should be diversely sourced and that each form of social security, for example, unemployment, health, old-age security should be accounted for by routinised and uniform policies using the administratively separate pooling arrangements that I have noted above. Moreover, individual funding of supplementary or simply privately funded insurance is also to be encouraged. After all, 'while the basic living conditions [of workers]. . . must be guaranteed, how much they enjoy social insurance should be linked to the amount of premiums they pay'. Also, there is what I see as an ominous warning in the discussions promoting this brave new world of social security provision. It is that China's social security model must be 'determined by national conditions of an enormous population and vast territory, an urban/rural gap, and uneven economic development'. It is a reform that must 'first of all' recognise 'the level of development of the productive forces in China . . . that the level of the productive forces is low'. Urban work units and industrial workers are to share the cost of social security provision with the state, but in rural areas matters such as 'peasant old age will be secured mainly by families', though attention is to be paid to establishing an all-encompassing system of insurance for enterprise work injuries and there is some commitment to 'improving the rural cooperative healthcare system'. It is worrying that it is intended that in the future pension insurance 'with differing standards' will be available to rural residents in order to secure their healthcare needs and their living in old age.[31]

In view of the recognised need for uniformity in urban social security arrangements, Party/state sources argue that it is 'imperative' that a national agency ensuring uniform security management is established. This agency would be responsible for social security plans, policy and action. Statistics are to be kept and social security legislation promoted. The latter will clarify 'rights and responsibilities, limits and standards' for social security fund management.[32]

Reform expectations

Economic reform was introduced with the promise of improved living standards. It is an expectation that has been built into the very foundations of the reform process and one that has been fed, first by the ever-rising living standards of the 1980s and now the 1990s and second by the leadership's ongoing need to legitimate their rule on the basis of their ability to meet the economic expectations of the Chinese people. However, members of the leadership élite have courted the option of decreasing workers' real wages under the guise of rising inflation and at the same time promoted labour reform initiatives that have done much to undermine the security of China's workers. Social security reform is implicated in both these issues. Figures that show that 'China's existing social security system . . . begun in the fifties', costs as much as '54 per cent of the total spent on workers and staff wages' are lamented by the leadership that would like to effect a significant reduction in this portion of the industrial worker's 'real' wage, while at the same time, members of the same group are observing that social security arrangements are a part of the 'safety valve' needed 'to keep risks [associated with social discontent] at a minimum'.[33]

As in the case of the mediation and arbitration procedures and the Labour Law that are now in place, the Party/state leadership are presenting their social security initiatives as evidence of their 'concern for the people'. They note that social security reform is the reform that 'workers are most concerned about' and argue that it is a reform that is in step with China's market needs and 'more importantly], is conducive to social stability and economic development'.[34]

Developing a market integrated economy

Because social security reform, including housing reform, will clearly separate the state-owned enterprises from their welfare responsibility, it will be particularly conducive to the development of China's market economy. In a situation where 'banks are obliged to continue providing enterprises with working capital' and where the liquidity of working capital is severely hampered by welfare obligations and enterprise losses are hidden – often in the form of welfare fund deficits – China's bankruptcy law has obviously been ineffective in imposing hard budget constraint on enterprise management decision-making. In short, divesting the state-owned enterprises of their welfare functions will further open the way for the market disciplining of China's industrial enterprises. The development of alternative social security provisions will bring enterprise closure closer to a socially digestible reality, while at the same time promoting the leadership's increasing role as the legislative protector of the Chinese worker.

WORKER ARBITRATION, RIGHTS AND INTERESTS

Introducing formal arbitration procedure

In January 1992, when progressive reform policy was put back on the Chinese leadership's agenda, it was decided that a system of state enterprise worker arbitration and mediation would be quickly trialled and then implemented. Worker arbitration regulations had been passed by the State Council in July 1987, but this is as far as this initiative went throughout the three years of economic rectification. After the return to progressive economic policy worker arbitration trials became a forerunner to the July 1993 adoption of national Regulations for Handling Enterprise Labour Disputes that in turn became the precursor to the 1995 Labour Law.

When the trialling of the arbitration procedure began it was only implemented in foreign-funded enterprises. From our post-Labour Law vantage point this seems to be a rather strange way for the central government to proceed with what has become, among other things, a comprehensive project to standardise workers' rights and interests. However, on reflection it can be seen that these enterprises appeared as a good choice for a government wanting to introduce regulations that would increase the concept of workers' rights and interests. By trialling the arbitration initiatives in foreign-funded enterprises the government could present the employer/managers as entrepreneurs who were accustomed to considering their profit margin above all else. Government sources pointed out that 'workers in foreign enterprises were the first in China to understand the survival of the fittest, a cruel truth rooted in the market economy' and, too, they are 'the first to learn reliance on law to protect their legal rights and interests'. Indeed those arguing on behalf of the Party/state have continued to use the ploy of pointing to the need to discipline the actions of foreign investors. For example, in January 1996 it was noted that 'a South Korean boss in a foreign-funded firm in southern China' had erred in her treatment of the firm's Chinese employees and that 'a mounting public awareness of workplace rights, and a willingness to fight for these rights' had ensured that the foreign employer had been suitably criticised, fined and forced to amend her behaviour toward her Chinese workers. The opposition of interests in the foreign-funded enterprises has not usually divided cleanly along the line between managers and workers. The division has been between foreign managers and Chinese managers and workers. This has made it quite safe for Party/state sources to point out repeatedly that disputes over working conditions are more prevalent in foreign-funded enterprises.[35]

After a relatively short trial period the worker arbitration system was widely implemented in China's domestic state-owned enterprises. It was an innovation that China's workers wasted no time in using. In 1993 alone 'arbitration committees nationwide . . . [heard] more than 12,000 cases'. This is an estimated 52 per cent increase over the number of cases heard in 1992. By 1993 half of the provinces, municipalities and autonomous regions in the country had established labour supervisory and arbitration institutions and, by 1995, the arbitration committees heard almost 13,000 labour dispute cases in just the first six months of that year. This was a staggering increase of more than 100 per cent over the 1993 figure. The substantial escalation in workers' use of arbitration was said by Party/state sources to have been promoted by 'an increased awareness by workers of their employment rights' and also to be a result of the January 1995 passage of the new Labour Law.[36]

The 'increased awareness by workers of their employment rights' is a situation that the Chinese leadership élite have found that they must watch carefully. While the arbitration and mediation institutions that have been established are formalising and ameliorating the opposition of interests that is now clearly apparent between state enterprise managers and workers and while they are effective in protecting the rights and interests of individual workers, they are also providing public credence and legitimacy for subjectively determined individual interests.

A national labour law

The introduction of a national labour law in January 1995 was an obvious attempt by the Chinese leadership to both manage and mediate the opposition of enterprise manager/worker interests, but it was also adopted as a means of off-setting the negative consequences of a rising rate of urban unemployment. Both the 1993 Regulations for Handling Enterprise Labour Disputes and the 1995 Labour Law have attempted to establish state control and regulation of worker conditions and so they are provisions that effectively erode, or at least discipline, enterprise manager decision-making. Like the 1993 Regulations, the 1995 Law stipulates that the rights of workers must be protected, but whereas the 1993 Regulations concentrated on the conditions and terms laid out in labour contracts and the subsequent fulfilment of the contracts, the 1995 Law has focused on establishing and developing an orderly labour market. This focus has meant that the Law includes 'for the first time' an attempt to protect workers who are to be dismissed or who 'want to change jobs'. Then it seeks to protect minimum wage rates that have already been set by local provincial authorities.[37]

In the period since the introduction of the 1995 Labour Law Party/state leaders have again stressed that the worker arbitration and mediation institutions are to be used to ensure that the Law functions as 'a vital instrument to protect the rights and interests of employees [and] employers'.[38] To date, protecting these 'rights and interests' has included employers incurring a 25 per cent extra charge when there has been a failure to pay the 50 per cent compensation required when an employer is found to be in arrears with wages, including overtime payments. It is then not surprising that government sources are now reporting both 'a mounting public awareness of workplace rights, . . . a willingness to fight for these rights' and a significant reduction in wages owed. Wages and social security funds 'embezzled' by management were also to be promptly recovered by the newly constituted central, provincial and municipal labour supervisory committees.[39]

At this point, we should note that the role of government in China is changing. In time, as ownership reform is implemented, it will cease to be the largest employer of China's urban workers. With this situation in mind and in the face of China's maturing labour market reforms, the leadership and government agencies are positioning themselves as national regulators. Their power increasingly lies in their legislative authority. Their laws are intended to both regulate and, if necessary, discipline employers, both government agencies and private employers. In short, increasingly the government, both at state and provincial level, has a new brief. This is to legislate on behalf of China's workers. If handled in a considered manner it is a brief that will serve to off-set the danger to the leadership's authority that an increased grass roots recognition and 'willingness to fight' for individual rights and interests presents to the authoritative basis of their political rule. The issue is then one of timing. The authoritative basis of the leadership's rule must not be significantly undermined before the Party/state's role as the legislating champion of the people's rights and interests has been firmly established and legitimated.

Political stability and unity

Conservative members of China's Party/state apparatus have continued, albeit quietly, to express their concern over the nexus between promoting further reform initiatives and continued 'political stability and unity'. However, for the majority within the leadership élite who champion the further development of the institutions, laws and mechanisms required by a market integrated economy, it has been a matter of ensuring a continued increase in peoples' living standards and, at the same time, it has involved the provision of various 'safety valves' for workers. People's income is estimated to have increased by 23 per cent in the period 1990 to 1994 alone with the volume of consumer retail purchases rising an average of more than 9 per cent each year during that period. Though the possession of a private automobile will continue to be outside the reach of the majority of China's workers for a considerable period to come (in spite of the government's current promotion of automobile production for China's domestic market and assurances that the rapidly expanding Chinese economy will lead to 'a robust demand for cars') central government sources are mostly correct when they note that the commodity consumption of urban workers has 'already grown beyond traditional consumption patterns and standards'. It has 'shifted from watches, sewing machines, and bicycles to televisions, washing machines, refrigerators, telephones, computers, and automobiles'.[40] By 1995 it was estimated that the average income per head of China's urban workers had risen some 22 per cent over the previous year, though once the rate of inflation was included in this calculation the percentage increase may well have been only one-third of that figure.[41] There was, nevertheless, a continued and substantial increase in urban workers' income and consumption. The problem for the Chinese leadership is that ensuring the continued growth in the economy that increased worker incomes and consumption depends upon is predicated on the implementation of progressive reform initiatives. These initiatives, in turn, depend on increased productive efficiency and this must include increased worker productivity, routinised working conditions and discarding 'surplus workers'. The latter has created an obvious and understandable insecurity among workers that is constantly shadowed by the leadership's concern over political stability. The latter amounts to code for the leadership élite's continued political authority.[42]

The rising demand for arbitration

Party/state sources have repeatedly discussed the need to balance investment and consumption. They have also worried at the problem of promoting 'reform and development' while giving 'full consideration to the tolerance of various parties' and today they report the leadership's concern over unemployment. There is a great deal said on the topics of how best to absorb 'surplus labourers', the wisdom of 'diverting' the surplus labour force in many different directions and the need to 'expedite the institution of the unemployment security system'.[43] Moreover, as the substantially increased use of worker arbitration procedures suggests and as Party/state sources point out, the 'increased awareness by workers of their employment rights' has meant that the Ministry of Labour has continued to have had to 'cope with an increasing number of labour disputes'. In other words the number of labour disputes brought to mediation and arbitration has continued to reflect the rate of increase already established in the period since this avenue of dispute resolution has been available to China's industrial workers. By 1995 there were an estimated 20,000 cases of enterprise manager/worker dispute of which about 80 per cent were resolved using mediation and arbitration procedures. Though the percentage of resolutions had dropped from the 1994 figure of 90 per cent, this was not because workers had not had a continuing increase in the number of manager/worker disputes that they wanted resolved by the formal channels established for mediation and arbitration. It was due to the shortage of available arbitration personnel. It is interesting that in 1995 a much larger percentage of labour disputes that were heard by the mediation and arbitration proceedings arose over the issue of employment dismissal. Surely this is an issue that is more difficult to mediate and solve than issues arising from workers or employers failing to abide by matters such as the pay and leave condi-tions laid out under a contract agreement.[44]

A new role for trade unions

It is pointed out that 'employees can negotiate [to ensure that they receive their rights] in a group' and they can do this alongside or by using the enterprise trade union. Since their inauguration the arbitration and mediation committees have been required to include workers' and trade unions representatives and enterprise (management) representatives. The trade unions have now been afforded both a changed and an 'expanded role in the modern enterprise system'. They are to be recognised as a 'vital component of China's "brand new" labour relations'. Like worker mediation and arbitration this changed role for the trade union system was first instituted in China's foreign-funded enterprises and then it was progressively introduced to the state-owned enterprises, often under the auspices of provincial governments. In 1993, in Guangdong province, where trade union representation of workers in foreign-funded enterprises had already been well established, provincial administrators approvingly estimated that 'trade union organizations with half a million members have been set up in half of the nearly 20,000 foreign-funded companies' and that 'in many foreign-financed firms in Guangdong, trade unions are considered the most powerful organizations speaking for workers'. Both provincial government and Party/state administrators are now arguing that China's trade unions must be further promoted as the "'mouthpiece" of the interests of staff members and workers' in both foreign-invested and domestic enterprises and that with forthcoming 'introduction of "the company system" to state-owned enterprises', trade unions must use their extended role to effect 'protection of the legitimate rights and interests' of staff and workers. It is in this context that it is pointed out that trade unions too are to join the ranks of the "'antishock valves" enabling reform to progress in a stable society'. Government sources also point out that if trade unions are to fulfil their new role 'they will have to win the workers' full trust. And this can only be done if the workers believe that unions act in their interests'.[45] It has been the need for continued reform and social stability that has been behind government administrators' focus on the 'antishock valve' role for the worker mediation and arbitration system, national labour regulations and laws and China's trade unions.

UNEMPLOYED URBAN WORKERS

Slowing the growth in urban unemployment

By the end of 1995 the Chinese leadership felt that they could congratulate themselves over managing to slow the rate of inflation and the economic growth rate and to even, it was then claimed, reduce the rate of urban unemployment. The snag to this very encouraging picture was first the authenticity of the unemployment figures (or at least the scope of those included in the category of unemployed) and second the rise in real unit labour costs. Figures published in the first weeks of 1996 noted that 'roughly 160 million, or 26 percent of China's [total – rural and urban] workforce' is underemployed and that this number of underemployed workers (that is, workers who are employed, but have nothing or little to do and who, without policy that mediates the process of labour reform, will face the prospect of unemployment) will be a part of China's economic scene at least until the year 2005. In the meantime, in the urban industrial sector, the rise in real unit labour costs is estimated to be more than the gain in labour productivity. In the circumstances it is a price that the leadership has obviously felt the need to pay for the 1995/6 'soft [economic] landing' that it had engineered.[46]

In a bid to slow the rate of urban unemployment a five- rather than six-day working week has now been introduced, but this innovation will further aggravate the rise in real unit labour costs. With the 'soft landing' of the economy 'the urban unemployment problem has [in reality] become more serious'. Nevertheless, Party/state sources have not been shy in terms of congratulating themselves on their success in economic management. They point out that at the end of 1994 they decided to 'make control of inflation the main goal of macroeconomic regulation and control'. It was deemed to be the centre-piece of 'handling the correlation among reform, development and stability'. The rate of investment in fixed assets slowed and the 'hard landing' experienced in 1988 and more particularly during the economic rectification following the 1989 Tiananmen Incident, was avoided. The question then was how long should, or could, the economy be slowed without the economic downturn that would also promote political instability. Already enterprises were 'complaining that they cannot bear the central government's macro-economic regulation and control'. State enterprise managers found that their immediate economic dilemma may well result in their control by direct administrative fiat, while at the same time, they were subject to the leadership's increasing attempt to justify their political authority by legislating regulations and laws governing management decision-making. Meanwhile state-owned enterprise losses increased and the need for enterprise reform and increased efficiency continued to be pressing.[47]

Soaking up the unemployed

It is now very clearly recognised that without further reform initiatives the 'too high debt rate' of the state-owned enterprises will not be solved. Ownership reform is proposed with its attendant injection of capital from share sales, but this is a reform that will increase the level of urban unemployment. It is then little wonder that representatives of the Party/state are encouraging provincial government administrators to establish further job training programmes as a means of soaking up the unemployed and even to create jobs directly for workers who have been, or will be, deemed to be surplus. In some cases local governments are even being encouraged to give preferential treatment to collective and private enterprises hiring the unemployed. They will be given access to bank loans and some tax exemptions. In addition, managers of state-owned enterprises are being told that they 'should enhance their "internal capability" to digest the surplus labour'. They are to do this by developing 'new growth points'.[48] This policy directive is very similar to the Second Automobile/Dongfeng group's innovation in the late 1980s whereby the group opened cap (headwear) and bottled drink factories in order to 'absorb' older (often women) workers that it continued to employ under tenure and so make room for more skilled and therefore more productive, and usually much younger, male workers. The productive 'wings' such as the Second Automobile/Dongfeng cap and soft-drink bottling factories are now each to be administered separately from the main enterprise group that has spawned them and they are to be given 'blood transfusions' from the main enterprise for only a limited period.[49] The problem here is obvious. If these wing enterprises are unable to return profits on their manufacture or, in some cases, the service that they provide, the workers that have been shuffled into them will only have had their unemployment status delayed. Over time, these workers will surely stand in stark contrast to those who are lucky enough to be employed by the shareholding limited liability companies or joint stock corporations that are now to be constituted as the process of restructuring the ownership profile of the state enterprises proceeds. Unless the wing factories are successful as discrete accounting units, the former workers, together with others who during the process of ownership reform find themselves joining the ranks of the urban unemployed, will be the victims of reform, the latter group will be the triumphant benefactors.

The recent 1996 leadership edict that decrees that the Party/state's 'major task' must now be the 'promotion of employment' has replaced the 1994 argument that 'taking control of inflation [is] the main goal of macro-economic regulation and control'. Administrators from the Party/state's Ministry of Labour now declare that from now until the end of the century, China's urban unemployment should not exceed the present 3 per cent, but even if this was possible, this 3 per cent is an inaccurate figure. China's hidden urban unemployment cannot be ignored. It 'is considerably more serious' than government sources have been willing to admit. It seems that around 30 per cent of the employees of large state-owned enterprises are surplus to production requirements and this is before ownership reform has been implemented on a wide scale. As the projected ownership restructuring of China's state-owned enterprises takes effect, the number of urban unemployed will rise quite dramatically.[50]

Macro-economic policy and control

China's leadership élite have now announced that 'current circumstances suggest that if macro-economic policy is right, a growth rate of about 10 per cent can be supported'. This growth is expected to be fuelled by the expansion of market mechanisms and the increasingly effective use of investment. The latter is to include investment in the infrastructure necessary to support productive capacity and, probably even more importantly, widespread direct shareholder investment in China's state enterprises. The extent of macro-economic control (using rules and regulations and the banking system) that will be required in this scenario is obvious, particularly when it is combined with the leadership's continual caution that 'fairly tight macro-economic policy' cannot yet be abandoned.[51] The spectre of inflation decrees that macro-economic policy is to continue to be used to manage the opposition of interests between the Party/state and local agents, but, at the same time, a continual and significant rate of growth, or at least a constant increase in worker consumerism, is also required if workers are to accept a decrease in their employment security and the growing tension in enterprise manager/worker relations. The leadership's increasing legislative role in protecting the rights and interests of China's industrial workers is unlikely, on its own, to be sufficient to ensure social and political stability. Add the problems of finding a growing number of employment opportunities for those who have been deemed to be surplus to enterprise requirements, or even the requirements of government administrations, and, even with a constant increase in levels of worker consumption, there is an obvious potential for political unrest.

CONCLUSION

In the second half of the 1980s, as the opposition of interests between enterprise managers and enterprise workers grew and became ever more entrenched, the labour-force of China's large, economically privileged state-owned enterprises became China's labour aristocracy. By the mid 1990s, these same workers were faced with the consequences of labour contracting, housing and social security reform and, even more importantly, as state enterprise ownership reform is implemented, they will be subject to the employment insecurity engendered by that ubiquitous Western term – 'down-sizing'.

Under the manager/worker cooperation that Walder identified, China's state-owned enterprise workers saw their take-home pay double during the first half of the 1980s. The rise in their pay-rate was far in excess of labour productivity and can only be explained by the community of interest that prevailed between enterprise managers who were deftly manipulating their newly found economic freedom in the context of a soft budget constraint and a work-force eager to assist the Deng Xiaoping leadership to meet their initial reform pledge to 'meet the needs of the broad masses'. Then, during the second half of the 1980s, advantaged state-owned enterprises such as the Second Automobile/Dongfeng group were more than matching the increase that their workers had had in their take-home pay with an increase in the provision of welfare services. As I have noted, housing stock was improved and increased. Educational, medical and childcare facilities were developed, shopping, sporting and other leisure activities and even shower-heaters were provided and oranges even materialised in winter to be distributed to enterprise staff and workers, but now, China's state workers have been toppled from their secure economic pedestal.

Throughout the 1980s enterprise managers' manipulation of the soft budget constraint had made transparent the difference of interest between the general concerns of the Party/state leadership and the particular concerns of enterprise managers and local government administrators and as this line of interest cleavage grew the second line of management/worker opposition developed. At the Party/state's behest, enterprise managers were directed to implement first the labour contract system and then housing reform. These initiatives laid the ground for generalising labour contracting to all China's state industrial workers, the development of a market for labour time, the provision of workers' 'real' wages in money form and divesting the state-owned enterprises of their welfare responsibilities. This will mean that enterprise managers can no longer see their success mirrored in the care that was afforded workers within the province of the enterprise kingdom that they administered.

By the 1990s it was clear that the Chinese Party/state leadership believed that the cooperative and inclusive 'familyism' of the large state-owned enterprises (the 'web of interests' that Walder had lamented and a situation often epitomised by a wall built around the site of the core factories of the enterprise) must be broken if the hard budget constraint of market integrated economic relations is to be facilitated. Interestingly however, once market manifestations such as employer/employee tension over wage distribution and unemployment have appeared, China's Party/state leaders have also assumed that their present political authority can only be reproduced if they provide for formal and standardised rules and regulations governing wage payment and working conditions, dismissal procedures and employer/employee mediation and arbitration mechanisms, yet these are the same measures that promote a perception of individual worker rights and interests. The Party/state leadership élite have also seen fit to promote a 'brand new' worker protection role for China's trade unions and have identified the willingness of enterprise managers to cut corners in worker entitlements, withhold wages, or use social security funds for other than intended purposes. In other words, the leadership élite have positioned themselves as national regulators of formalised employment conditions and employee entitlements in the context of a growing opposition of interests between enterprise managers and enterprise workers.

3 Banking, price and taxation reform

Accounting for actually existing circumstances

> The difficulty with hardening [the budget constraint] is that it involves changes in people's expectations about the level of economic security and equality in society. People are willing to accept nominal marketization, as long as they are under the paternalistic protection of the state. However, withdrawal of the paternalistic protection of the state is a different matter. Thus, while better strategy for economic reform might include both hardening and marketization, its success will depend on the sequence and pace at which these two aspects are carried out.[1]

At a theoretical level China's state leaders, economists and planners have now adopted a market integrated economy as their goal. However, in practice the problems of China's actually existing administrative, economic and political structure combined with social expectations dictate that the development of a mature market mechanism be slowed and ameliorated. The Chinese leadership's need to manage the opposition of interest between the state and local agents, while at the same time appearing to act on behalf of China's workers, has led them to promote institutionalised arrangements and policy initiatives that go some way to compensating for the social and political cost of reform. This is most clearly illustrated by their continuing political need for the Ministry of Finance to exercise control over China's centralised banking system, even when there is ever-increasing economic pressure for far greater decision-making independence for the People's Bank of China and indeed for the commercialisation of China's state-owned lending institutions. The problem is that even a publicly declared, clearly articulated decision to promote the development of a market integrated economy does not automatically lead to the political tolerance required from the populace for the implementation of policies that will effect economic discipline.[2]

In this chapter I outline the Chinese leadership's choice to forgo fundamental banking reform (that is, to forgo the development of a market for capital in relation to funds held and credit advanced using the banking system) at this stage in the process of economic reform and then I canvass the increased pressure for pricing and taxation reform that the 1992 return to progressive economic policy impressed on China's policy-makers.

Initially, reform policy decreed that the banking system, pricing and taxation all be used as 'economic levers' by the Party/state élite. These levers were intended to replace the discipline otherwise administered directly by China's previous centralised command form of economic organisation, or by the mature market mechanism that is now the goal of China's reform. For much of the post-reform period the focus of Party/state planners and administrators has been on pacing the progress of reform by the percentage of prices released from government control, rather than on the use of price as an economic lever, but both the banking system and taxation policy have continued to be seen as mechanisms that would be used to curb the demands made by local agents. However, as the reform process has matured the taxation system has played only a reduced role in this form of state control. It has come to function primarily as an avenue for government revenue raising and has combined with price reform, the latter being seen merely as a measurement of the maturity of the overall reform process, to increase substantially the pressure on the banking system to function as the state's 'most important monetary tool'.[3]

THE PEOPLE'S BANK: CREDIT CONTROL WITH MINIMAL SIDE-EFFECTS

Eating from the big rice pot

Under reform policy China's centralised People's Bank is charged with functioning as the bank of the state-owned so-called specialised and commercial banks. The latter are obliged to bank with the People's Bank. In theory these client banks are 'required to keep their credit balance by themselves' and to ensure that 'their loans are dependent on their deposits', but in practice they have depended on funds from inter-bank borrowings, particularly funds that they have borrowed from the People's Bank. Even so, the intention is that these borrowings will be kept within the scale of the national credit plan. However, in the context of the soft budget constraint experienced within the banking system, the client state-owned specialised and commercial banks have continued 'eating out of the big rice pot' of the central bank. In other words, borrowings by the client banks have exceeded overall credit plans in a situation where they do not believe that they will be called upon to account for their credit quota over-runs. This has happened to the point where state economists and planners now insist that 'the intermediary target' of their monetary policy is for the state to be in a position to be able to control the scale of credit and volume of money supply. In the present context this is both a modest and an ambitious goal.

11Overstated book profits and soft landings

Members of the Research Institute of the centralised People's Bank have argued that at any given time as many as 10 per cent of the client banks' loans could not be recovered and these loans have not been written off as bad debts. Central government approval is required for the periodic writing off of debts and until the recent decree that in the few cases of bankruptcy the debts owed to the bank by the enterprise concerned must be immediately written off, permission has not been forthcoming. In other words, as is usual in the context of soft budget constraint, market discipline does not decree that financial institutions periodically write off the debts that they will be unable to collect. The client banks' book profit has therefore been consistently overstated.[5] In overdrawing or expanding access to funding and in overstating actual profit, the soft budget constraint behaviour of the state-owned industrial enterprises has been replicated in the behaviour of the client specialised and commercial banks.[6] In this context it is not at all surprising that 'local bankers found it almost impossible to turn down the pet projects of local officials'.[7] It is then ironic that the centralised banking system is also the means by which the state can better manage the opposition of interest between itself and local agents. It is the primary means by which the state can discipline the financial demands made by local administrators and enterprise managers, but in the context of endemic soft budget constraint, this means of disciplining investment hunger is restricted to the use of the very simple and blunt economic technique of reducing the overall volume of available credit.

Throughout the 1980s centrally induced periods of economic contraction were used to 'cool' the economy, culminating in the hard economic landing promoted by the rectification policies of the 1989–92 period.[8] Then, in the period since 1992 the brief given to the banking system has been to fine-tune the economy by 'controlling credit with [or while creating] minimal side effects'. This is the genesis of the current use of economic soft landings, or using more recent language – 'moderate economic tightening' – as a means of dampening, rather than cooling, the economy.[9] It was in this situation that an apparently surprising thing happened. During 1994 and 1995 the client state-owned specialised and commercial banks took in more new deposits than they lent in new loans. This was 'at a time when many enterprises are short of funds', but the whole thing was in fact a mirage created by simplistic accounting. It was not that the client banks had 'failed to make loans at a rate commensurate with their flow of deposits' and so intentionally worsened the 'cash crunch', albeit a moderate cash crunch, felt by the enterprises. From the deposits that they have taken the banks have been obliged to contribute 13 per cent to their deposit reserve fund lodged with the People's Bank and they have been required to hold back funds in order to meet their own operating needs. Today the latter takes up between 5 and 7 per cent of monies deposited. Thus, in 1995 the accounts of all China's formally sanctioned financial institutions showed a total of 5,033 trillion yuan in deposits with loans made totalling 4,972 trillion yuan: equivalent to 98.8 per cent of deposits. However, after paying out the required amounts to their deposit reserve funds and to the provisional fund that covers their operating costs, the institutions had a 1995 loans to deposits ratio of 122 per cent and in the case of the state-owned client banks, their ratio was higher. It was estimated to be over 135 per cent.[10] We should therefore conclude that during the first half of the 1990s economic tightening was indeed moderate and we might also note that, unlike the situation in Western market integrated economies, the banks have earnt little from the interest rate and charges that they levy on their largest borrowers, the state-owned industrial enterprises.

Lessons learnt

In China in the 1990s, Party/state economists and administrators are putting into practice the advice that many Eastern and Central European economists would offer in light of their reform experiences. With the considerable benefit of hindsight they argue that while 'the excessive expansion of credit can clearly lead to inflationary pressure' it must also be remembered that 'hardening the budget constraint too rapidly, or in the wrong way, can lead to a separate set of problems'. Among a plethora of problems that can result they note that if interest rates are raised sharply, enterprises may well be left with insufficient operating funds and so national productivity will be substantially reduced. They also cite the problem that I have discussed above. That is, while it is important that during the transition from centrally administered to market integrated economy credit is cut off to those enterprises with the lowest return on funds invested, the distinction between enterprises 'is difficult to ascertain'. A central political problem is that while volume of credit is in principle relatively easy to control through a single centralised bank, the indirect mechanisms used by market integrated economies may well 'be viewed as an excessively risky way of controlling the volume of credit' and this is why, in China, these market mechanisms are being introduced only tentatively and at a very slow rate.[11]

Debts, rescues, tariffs and deficits

Apart from its use as a faucet for credit flow, as the 1980s unfolded and the post-reform expansion of productive capacity increased inflationary pressure and strained the availability of investment funds, the banking system's importance as a vehicle for collecting funds from individual savers and redistributing them in the form of state enterprise loans grew. Then, during the 1989–92 period of economic rectification, this redistributive function was even further extended. The banking system was obliged to take part in rescuing state-owned enterprises which were contributing to the development of the debtchains that, in turn, were threatening to stall, or at least reduce the function of monetary exchange. When faced with debt-chains and the need to supply their production needs state enterprise managers had made unprecedented use of barter.[12]

Once rectification policy had, at least temporarily, forced the managers of the state-owned enterprises to cease their careening bid to expand their productive capacity, the previous shortage of many producer goods (particularly semi-finished goods) became an unprecedented surplus. Enterprises began to stock-pile unsold semi-finished products. It was at this point that the debt-chains became widespread. State-owned enterprises were not paying their suppliers and these suppliers in turn were not in a position to meet their financial obligations. Faced with this situation many state-owned enterprise managers were obliged to barter and squeeze credit by delaying payment of monies owed and at the same time, local (provincial) government administrators erected tariff barriers in order to ensure that products produced within their province were sold. Throughout the period of economic rectification state enterprise profits fell sharply and so too, government tax receipts. It was in this context that a number of provincial governments found that they were unable to pay for the grain that peasants in their areas had grown under quota. The peasants were issued with white papers (IOUs). At the macro-economic level, the national deficit rose sharply. This deficit was often hidden within the accounts of both the banking system and the state enterprises. As I have noted, apart from the relatively sparse cases of individual enterprise bankruptcies, the Chinese banking system has not written off bad debts. The banks have not periodically cleared their uncollected debts nor have the monies owed by the specialist banks to the People's Bank been periodically cleansed.

The actual deficit

In mid 1992 in the context of yet another debate over the question of bank loan 'overruns', concern began to be expressed publicly over the state's increasing domestic deficit. In this context it was argued that it was time that the central government's Ministry of Finance began to include references to the 'actual' deficit. Party/state economists advised that 'the financial deficit should include . . . government debts to banks, and enterprises' potential losses'.[13] They also noted the approaches of various countries in handling deficits and cited them as: '1) tax increases; 2) raising loans; and 3) issuing more banknotes'. They then recognised that 'China has resorted to the last two approaches' and argued that these 'have not been helpful to the state's stability'.[14] We are left to note that observations such as this make it very clear that it is the concern for 'the state's stability' that continues to tie the Chinese leadership élite to their commitment to continue direct central government control of credit volume.

IN THE CIRCUMSTANCES

The question of the banking system as a separate entity

In China, the persistence of 'the big rice pot' (or the 'iron rice bowl') approach to credit coupled with the state's concern to maintain stability and unity has meant that even though just a few large and medium-sized state-owned enterprises with high levels of debt are merged or even closed, the Chinese banking system has not yet come within any reasonable distance of the role which Chinese state planners outlined for it in the mid 1980s. That outline announced that the Chinese banking system has begun to be restructured into a system in which the People's Bank of China would be akin to the Federal Reserve Board in America, or more precisely, to the Federal Republic of Germany's Bundesbank. It was argued that the People's Bank would make loans to the state-owned specialised and commercial banks (including the Agriculture Bank, the Construction Bank and the then newly established Industrial and Commercial Bank), which would use these central bank funds in conjunction with deposits that they collected, to make loans. Since this time the client banks have been required first to use their own capital and deposits to meet their loan commitments. Then, after suitable People's Bank examination and approval, further funds required are drawn via a lending facility provided by the People's Bank.[15] As I have argued above, both the potential to exploit and manipulate the prevailing soft budget constraint and the intended centralised monetary control function of this procedure are obvious. In the latter half of the 1980s the former situation prevailed over the latter. By that time it was clear that 'an expansionary, even inflationary, macro-economic environment had become the normal condition of the Chinese economy': a condition that, as I have argued, was significantly exacerbated by tension within the leadership élite over the appropriate end goal of the process of reform.[16]

In the mid 1980s the debate on the problem of 'over-expenditure' on fixed assets sanctioned by local government administrators and initiated by state-owned enterprise managers had gone as far as canvassing arguments to the effect that the banking system should assume direct control of all enterprise funding. The debate included the view that direct funding of state-owned industrial enterprises via the banking system would reduce that system to a passive arm of the industrial ministries. Nevertheless, it was decided that the banking system must be retained as a separate and discrete entity. Party/state economists argued that the banking system alone should hold the power to issue currency and to charge interest rates and that this power should not be directly merged with the responsibilities borne by the industrial ministries. It was maintained that a discrete banking system could better withstand pressure to meet state enterprise funding demands via the expansion of money supply. At the time this policy was in line with the reform intention of separating direct government administration from enterprise-level decision-making, but the question to be asked today is – has the banking system been in a position to operate as a discrete entity in post-reform China? The answer to the question is that it has not.[17]

Interest rates and merely passing laws

Commentators, both Chinese and Western, argue that the People's Bank of China must be 'free to formulate a monetary policy independently' and that it must not continue to be 'determined solely' by what the Party/state leadership wants and by what state enterprises managers can get. They argue for a clear administrative separation between the People's Bank of China and the Ministry of Finance so that China's central bank is 'independent and free to formulate a monetary policy'. The Bank should be free to manage its goals of developing the economy and stabilising the currency, but to date this has been 'a very remote prospect'. Some commentators then go further. They argue that with adequate 'clarification of the central bank's role' it will be possible to further develop China's banking industry as a whole. Once the client banks are practising independent accounting they will modify their operations. 'Real' interest rates will then be used with the investment priorities of China's enterprises responding to changes in interest rates. However, other Chinese economic commentators recognise that 'China still does not meet the preconditions' for this form of market discipline to be implemented. For the moment, direct control methods must be used. Credit planning, credit ceilings and the restricted use of interest rates must therefore be retained. Nevertheless, these commentators argue that an independent People's Bank of China is both possible and advisable, at least in economic terms. The reason that this is not happening is the Party élite's political concern to continue to control investment priorities and, above all, to be in a position to use the centralised banking system to rescue those state-owned enterprises that are thought to be too politically expensive to close. The closest that China's leadership élite have come to granting independence to the People's Bank is in formally considering and then passing the latest draft of the Law on the Central Bank. Economists and state administrators promoting this Law sought to use the legal system to provide 'a clear-cut definition of the status of the central bank and [of] the objectives of its monetary policy'. The law is intended to shield the bank from interference by state ministries, though those supporting the adoption of the law were realistic enough to temper their argument by noting that it is impossible to solve problems overnight by 'merely passing a law'.[18]

Decentralisation and local administrators

At the opposite end of the scale from the interference in bank decision-making exercised by the Ministry of Finance, there is the interference that local bank officials receive from local government administrators. Today this is given as a reason why further reform of the banking system cannot yet be effected. The argument is that 'financial restructuring can hardly be conducted ahead of investment, financial and taxation restructuring'. If investment power is relegated to localities it would mean that local agents would quickly seize resources in order to develop their own localities. Commentators note that local administrators would resort to 'various means' in order to do this, but as I have argued, even without significant restructuring of the banking system, the soft budget constraint of the client banks leaves their administrators vulnerable to pressure from local government administrators who are bent on ensuring that the enterprises within their jurisdictions receive as much funding as can be arranged. This situation is particularly acute during periods of economic contraction when state-owned enterprise profits may well decrease and when the process of economic reform has itself led to a significant decrease in both central and local government tax receipts. In these circumstances local government administrators, and often state ministries responsible for particular enterprises, pressure the banks to extend excessive bank credit in order to ensure the continued operation of 'their' enterprises. The state's monetary control is then significantly undermined. This situation has now reached the point where it has been said that the client banks 'are controlled by local authorities' and so officers from the central offices of the various client specialised and commercial banks are now sent to inspect the economic decision-making of local branch administrators. In addition, state administrators have decided that under the state enterprise ownership trials taking place at the moment, they will require enterprises to bank with the central office of their bank and not the local, provincial or city office. It is thought that administrators at the central office will be in a better position to stand against the demands made on them. The enterprises that are currently taking part in the ownership trials are also to have their existing bank loans reassessed. Fixed asset loans will be converted into circulating funds loans and once the enterprises have agreed to this formula their interest payments will then be based on the relatively low rate of just 3 per cent.[19]

WHAT IS THE OPTIMUM RATE OF INFLATION? MERGERS AND BANKRUPTCIES

Yielding over loan repayments and the ongoing question of how to relieve the pressure on inflation

After the 1992 return to progressive reform policy, Party/state planners and administrators had to admit that not only are the state-owned specialised and commercial banks 'yielding' over loan issues and the terms and conditions of repayment, but the central People's Bank is also 'yielding many times'.[20] The implementation of policy that will allow the state to effectively discipline the decision-making of local agents continued to be a long way away when, even aside from the difficult issue of whether market rates should now be paid for state enterprise investment funds, it was extremely difficult to control loan issues to the state-owned enterprises. It is in light of this situation that government sources found it prudent to canvas the question – what is the optimum rate of inflation? Then, they quickly noted that it must not be a rate 'that exceeds most people's tolerance' and putting the best possible face on the situation at hand, they argued that inflation can accumulate funds and advised that 'inflation can covertly transform part of the people's consumption funds into accumulation funds'. In other words, people's real wages can be depreciated under the politically useful guise of inflation. Then they proposed that funds drawn from what amounts to this new form of 'price scissors' should go only to government prioritised construction, particularly infrastructure. However, with the continued lack of effective hard budget constraint within the banking system, in local government dealings and on state enterprise decision-making, the root cause of a rising rate of inflation remains unsolved in spite of confident announcements by state government officials claiming that greater macro-economic control has now been successful in terms of relieving the pressure on inflation.[21]

Mergers and closures

Closing an enterprise and distributing the assets as payment for monies owed is, of course, the ultimate act of market discipline. Today in China, not only does this act of market discipline continue to be thought to be too politically expensive to be implemented, there is a further complication: 'many enterprises operating in the red have accumulated huge debts' and in some cases the monetary value of these debts exceeds the total assets held by the enterprise. Bankruptcy would mean that even if the workers' claims were given priority, funds would be insufficient to cover their claims. To date, China's workers have been encouraged to 'firmly believe that socialism means employment for everyone, common prosperity, and everyone having enough to eat and wear'. It is obvious that bankrupting the state-owned enterprises that are running in the red would not serve to satisfy this expectation and would be particularly politically counter-productive when, at the same time, the Party/state leadership are attempting to present themselves as the protectors of workers' rights and interests in the face of the growing tension between state enterprise managers and their workers. Obviously, the only politically realistic government option is to attempt to 'revive' enterprises where losses exceed asset value, together with those that are deemed to be the victims of non-operational losses, but this means that the non-negotiable (hard budget) aspect of market discipline is significantly corrupted. When it comes to the issue of overcoming the excessive debts carried by many state-owned industrial enterprises, China's state planners have resorted to politely arguing that 'a diverse approach should be taken'. They have advised that different methods should be used to adjust and regulate the debt structure of the enterprises. Some went as far as arguing that state enterprise public debts and equity losses should be written off. They argued that non-performing state-owned enterprise loans should be cancelled and that the non-performing loans owed by the specialised banks to the People's Bank should also be cancelled. Then they added that interest payments on outstanding loans should be stopped, loans should be advanced to state-owned enterprises only in the form of direct (tightly administratively controlled) investment and, in the case of enterprises 'which conform to government policy and which require major assistance', outstanding loans could be converted into government shareholding or joint stock investment. The funds extended under these conditions would then be considered to be state capital. This approach could be combined with the process of restructuring the ownership of the state enterprises and it would increase the assets held by the state.[22] However, by the end of 1995, this argument had passed the peak of its popularity. The favoured approach was for the People's Bank to issue instructions to the client banks on the best way to promote industrial reform. First, the client banks *must* 'enthusiastically support' a demand for circulation funds from large and medium-sized state-owned enterprises which manufacture products that are marketable. The managers of these enterprises must prove that 'they will not divert these loans' (presumably into funds invested in fixed assets) and that they will pay both the required interest and principal. Second, the state-owned client banks are to support large and medium-sized enterprises involved in production for export. Third, they are to 'apply the credit lever' in order to support increased investment in technology or the increased use of technologically based skills. Fourth, the client banks are to support pilot projects that are favoured by the State Council, in other words, those projects that have direct leadership priority and approval and fifth, the banks must facilitate financially advantaged enterprises merging with (taking over) less economically able enterprises. In this latter instance the banks must abide by the rules set out by the People's Bank in relation to interest suspension or exemption on the debt owed by the enterprise that is to be merged. In the very few cases where it has been decided that an enterprise in financial trouble will declare bankruptcy, administrators from the client bank concerned must oversee and support the enterprise manager's bankruptcy declaration. Moreover, once claim settlements have been decided, +bank administrators must cancel all remaining enterprise debts. The latter includes any monies still owed to their bank.[23]

Treating some enterprises more favourably than others

In line with the current diverse approach the client banks are to take toward their state enterprise customers, it is now proposed that 'flexible interest rates' be used, but these rates are far from the rates that would pertain to a market for capital. For example, enterprises that are to be given the most favourable rates are those that are to be supported in accord with the state industrial policy. They are enterprises such as those making up the Second Automobile/Dongfeng group. They are to produce those items or to provide those services that are uppermost on the state's industrial shopping list. By way of contrast, 'those enterprises that are restricted in their development based on industrial policy' are to be subject to 'an upward float' in their interest rates. Moreover, an enterprise that has a credit rating that 'is comparatively poor', is overstocked with unsold product and/or is deemed to have excessive debts, must be subject to higher interest rates. If state-owned enterprise managers are deemed to have misused funds through real estate speculation, illicit stock trading or fixed asset investment, the loans will be recalled. The nexus between enterprise performance and the rate of interest to be paid on monies loaned is, of course, close to the dictates of a market integrated economy, but it is overridden by the Party/state's intention to implement its industrial development priorities. Obviously, the Chinese banking system continues to be primarily a mechanism for Party/state macro-economic control.[24]

Mergers, closures and unemployment

As I have been arguing, in the case of the merged and the small number of bankrupted enterprises the biggest problem in terms of political stability and unity is the increase in the number of unemployed, particularly the urban unemployed. As we would expect and as the 1989 Tiananmen Incident demonstrates, it is these people who have higher expectations and who are the most sophisticated in terms of education and ability to articulate their political dissatisfaction. When an enterprise is merged or closed, workers are inevitably shed. There is then concern expressed over what is being called 'stealth unemployment'. When enterprises are obliged to be merged with what are often larger, more economically advantaged enterprises, it is the underemployed workers who are shed. The current statistics are frightening. They project that by the year 2005 there will be 'about 150 million surplus workers, or around 21.5 per cent of our [total wage-labour] work force' (and this figure is below the 30 per cent of underemployed wage-earning workers that I mentioned in the last chapter). Chinese Party/state economists have had to recognise that 'as our market economy develops, our ratio of open unemployment will grow, possibly causing social unrest'. Again as I noted in the last chapter, while the majority of the unemployed are rural based, it is nevertheless obvious that mediation and arbitration and even rules and regulations covering dismissal procedures, can only go so far in terms of off-setting the potential for social unrest that large numbers of unemployed urban wage workers present and, at the same time, a similar lack of confidence must apply to comments by state administrators that stress that unemployed urban workers must be innovative and help themselves.[25]

THE SECOND AUTOMOBILE/DONGFENG CORPORATION: BANKING AND FOREIGN INVESTMENT, PRICE AND TAXATION

The banking system is not independent

Though managers and economists from the Second Automobile/ Dongfeng corporation have long complained of a shortage of both circulating and investment funds and though they now fester over the need to recoup monies owed to the corporation, they also correctly argue that the banking system will continue to advance them circulating and investment funds. This is the case even though the conglomerate's accounts are now running in the red. As economists from the group pointed out 'the banking system is not independent' from the Party/state and 'the banks run to rules, not to the market'.[26]

Financial difficulties and potential

The Second Automobile/Dongfeng group is, after all, a 'giant' enterprise that has good potential even when sales of the sedans that it is producing are falling. Both automobile and automobile spare parts production and so the Second Automobile/Dongfeng enterprise group have been afforded a high priority in the state's industrial plan. With Party/state sources presenting the corporation as one of the 'three bigs' of China's domestic automobile production, the picture of the future is painted as being very rosy and the Second Automobile/ Dongfeng group's potential is heralded and its status is suitably nourished. Nevertheless, Party/state sources noted that in 1995 'the Dongfeng Motor Corporation . . . has been caught up in [financial] difficulties'. It seems that overall automobile production has been experiencing what is presented as a temporary 'downward movement'. Indeed, by the first half of 1996 the Automotive Industry Department of the Ministry of Machine-Building Industry was forced to admit that the number of stock-piled automobiles had risen from 88,000 at the end of 1995 to 116,000 units.[27] The assumed temporary nature of this situation means that it has not made any difference to the Second Automobile/Dongfeng group's plans to build a second site for car production in the city of Wenzhou near Hangzhou (the provincial capital of the east coastal province of Zhejiang). After all, the current projected capacity of China's vehicle production is between 2.8 and 3 million vehicles per annum, 'including 1.3 to 1.5 million sedans' and by the time the industry has matured 'into a pillar of the national economy' it is said that it will be producing an estimated 'six million vehicles a year, including four million sedans'.[28]

Joint ventures and foreign investment

The Second Automobile/Dongfeng group's first car plant is in the city of Wuhan (the provincial capital of Hubei province) where the local government has put aside a section of the city as a special economic zone. The provincial government has provided services, tax breaks and so-called simplified administration to its special economic zone in the hope that it will attract foreign investment. Funds have also been made available for the Second Automobile/ Dongfeng group's increased participation in auto-parts manufacture. As I have already noted they have enterprises in Xiangfan that produce Cummins truck engines and there are other long standing cooperative and joint production arrangements. These include the production of thermostats in cooperation with Thomson International and a disc-brakes project located in another venture in Xiangfan city involving the Hubei Asbestos Product Mill and an Italian manufacturer (ALA). The management of the Second Automobile/Dongfeng group have also investigated using the Pudong Development Zone (opposite Shanghai's waterfront Bund) to process automotive parts in cooperation with Japan's Nissan Motor company. It was intended that these would substitute for imported knock-down Nissan diesel kits. There have also been other types of cooperation with Nissan. As I note in Chapter 1, the Nissan company has provided technical assistance to the Second Automobile/Dongfeng group for the production of truck and bus cabs and axles, transmissions and chassis and both Nissan and the Second Automobile/Dongfeng corporation have direct investment in the Zhengzhou Light Truck plant (located in the provincial capital of Henan province). The Industrial and Commercial Bank of China and Thailand's Sammitra Motor Group are other investors in this project. And now, there is yet another joint venture for spare parts manufacture on the Second Automobile/Dongfeng drawing board. This time it is with the South Korean based Hyundai group. In the same manner as car manufacture for the domestic market is a priority on the leadership's industrial development list, spare parts manufacture is currently an industry that is to be encouraged. It is this industry that is 'to serve as a foundation' for the automotive industry. It is said that 'a strong auto parts industry is the indispensable basis on which a healthy automobile industry rests'. It is now understood that investment in China's emerging automotive parts industry has been low relative to investment in the automotive industry as a whole and that as long as this situation remains China will not have the opportunity to enter the increasingly global manufacture of automotive parts. It is recognised that the automotive parts industry will become increasingly specialised, that it will be based on large-scale production runs and that China has relatively cheap labour costs and raw material prices. This situation has already attracted 'foreign companies looking to relocate automotive production facilities' and it has been recognised that these relocated production facilities will require semi-finished automotive parts.[29] Ideally, economists at the Second Automobile/Dongfeng group would like to access the state Economic Development Fund for loans that can be used to extend both their automotive manufacture and their automotive parts ventures. This is because the loans offered from this fund attract a lower interest rate than bank loans. With the central government's continued support of the automotive industry (at the beginning of 1996 an official of the Automotive Industry Department of the Ministry of Machine-Building was announcing that a further '11.2 billion yuan will be used for infrastructure in the [automotive] industry and 12.8 billion yuan for technological renovation, particularly in auto parts development') it seems certain that government sanctioned development funds will be made available to the management of the Second Automobile/ Dongfeng corporation and that these funds will be available on favourable economic terms.[30]

In spite of the situation in relation to the Second Automobile/ Dongfeng corporation's current profit line, after a rigorous process of audit the central government administrators had given their permission for the group's shares to be listed on the Hong Kong stock exchange. Again, it is the status and the potential of the group that is to determine the price of the shares rather than current investment to profit ratio. When I asked senior members of the corporation's group of economists to explain the interest in listing on the Hong Kong stock exchange, I was told that raising money was important, particularly at the current juncture in the group's development, but it was not the most important facet of listing on this exchange. The most important aspect is the pressure that the corporation's managers would subsequently be in a position to put on representatives of the state now that the corporation was an 'overseas' listed company. It would be most useful in getting the monkey (the centre) off the back of the tiger (the corporation). The economists argued that the corporation's listing on the Hong Kong stock exchange would mean that more attention would be paid to accumulating profit and that this would mean that the corporation's managers would be less likely to be forced to agree to do their 'political duty' by accepting discharged army engineers on to the corporation's payroll. After all, 'the automotive industry must adjust to the market', particularly now that the rate of inflation has been slowed. Indeed, 'all enterprises should be subject to the market and workers should too'. The senior economists that I was talking to admitted that there was often tension between the goals that they would promote and those that the government thought suitable. (At the beginning of 1996, when the Second Automobile/Dongfeng group's managers applied for permission to list on the New York stock exchange they argued that now that reform had advanced to the point where China's best enterprises could be listed on international share markets, there should be no central government impediment to their group being listed in New York.)[31]

Pricing enterprise product

Of the Second Automobile/Dongfeng group's vehicle production, 80 per cent continues to be various types of trucks, but now the group's managers deal directly with their buyers. Today they even negotiate directly with the army. The military price is still lower than the price that the group earns from other buyers, particularly individual buyers, but in proportional terms the army now buys less of the group's total product. Management negotiates the military price within the range set by the Ministry of Trade (usually cost plus 5 per cent). The sales structure of the Second Automobile/Dongfeng corporation has changed over time. Today buyers are predominantly individual purchasers. Particularly when it comes to the sale of the Citroën sedans produced by the group, the management economists are complaining that 'before sellers chose their customers, now buyers choose'. The latter is serving to ensure that the private/retail price that many individual buyers find that they must pay does not increase too rapidly. In this respect it is a market price, but the issue of pricing the Second Automobile/Dongfeng group's product is obviously more complex than this buyer/seller equation suggests. For example, the price of the raw materials and semi-finished products purchased by the group is not a market price. It is an artificially low price relative to the market. At the same time, the corporation has been obliged to purchase a large proportion of the parts it requires for automobile production on the overseas market. Central government sources have boasted that first 60 per cent and now up to 80 per cent of the semi-finished product required for domestic automobile production is available on the Chinese domestic market. In 1994 they declared that already 40 per cent of the parts used in assembling cars must be made in China and that the 150,000 1.4 litre ZX sedans that were to be built in 1995 at the Dongfeng plant in Wuhan would have a component of 60 per cent domestically manufactured parts. Yet, at the end of 1995 only an estimated 20 per cent of the Second Automobile/Dongfeng group's requirements for manufacturing the Citroën sedans were being met by domestic suppliers. In part this is because, as I noted in Chapter 1, the group's buyers believe that the quality of a number of domestically manufactured components continues to be too low for the group's joint venture requirements. The group's foreign earnings have offered the option of buying foreign manufactured parts and so when quality requirements are deemed to be too low, even after the group's buyers have used their foreign connections to press domestic producers to improve quality, they spurn the domestically produced item. They do this even though the buying price is lower. Indeed, the management of the Second Automobile/Dongfeng group have a history of adopting innovative ways of solving the low quality input problem. For example, the group had bartered scrap steel from its manufacturing plants for pig iron with the Linxian Steel Plant. This has meant that the Second Automobile/Dongfeng factories have had greater access to the pig iron that they needed to make up shortfalls. In part these shortfalls had come about because buyers from the group had refused to accept any sub-standard portion of the steel that they had been allocated by the Wuhan city and Chongqing city steel mills.[32]

In interviews held in 1991 with senior research economists at the Second Automobile/Dongfeng group's headquarters in Shi-yan city (often laughingly referred to as China's Detroit), I was told that like enterprise policy concerned with purchasing raw and semi-finished materials, the so-called double track for pricing was extremely complex and continued to be the cause of significant economic and policy problems. However, by the end of 1995 Second Automobile/ Dongfeng corporation economists were telling me that hardly any of the goods and services purchased by the corporation still had more than one price. The complexity of the double track pricing system came from two and sometimes three and four different prices for the same product. For example, as I note in Chapter 1, the government continued to ensure that manufacturers have access to the proportion of their raw material needs required for production under mandatory plans. For the Second Automobile/ Dongfeng group this is for the trucks that it produces for the Chinese army. The raw materials provided for mandatory production quotas are supplied to the manufacturer at a lower price than the remainder of the required raw and semi-finished materials. This is the case even when a large state-owned enterprise such as the Second Automobile/Dongfeng corporation acquires the largest proportion of its production needs from other state-owned enterprises. In other words, buyers from the group purchase the same or similar products from the same or similar sources and yet they pay different prices. They have rarely needed or been tempted to venture into the private market-place.

One of the most cited and obviously much resented problems connected with the use of double track pricing was demonstrated to me in a 1988 interview with a friend from the Second Automobile/ Dongfeng group. I was told the tale of an administrator who worked as a supply officer for the group's workers' university. A local Shiyan department store, also a member of the Second Automobile/ Dongfeng group, decided to boost its sales figures by offering a coloured television set at state price (the lowest formal price available) to any customer who exceeded what was a very high quantity of purchases. The administrator decided that the workers' university desperately needed new desks throughout and that these desks were the type that could be bought from the local department store. The university had new desks and the administrator had his state-priced television set that he was then able to sell at the substantially higher private retail price. It could be said that he had been the right person in the right spot at the right time.

Taxing the Second Automobile/Dongfeng corporation: a thorny issue

It was also during interviews that I had with people from the Second Automobile/Dongfeng group that I heard the often repeated comment that they would welcome the 'real' separation of enterprise profit from enterprise taxation. By 1991 economists from the Second Automobile/Dongfeng corporation were arguing that the enterprise's taxation commitment was too high, particularly when other taxes were being foisted on them. For example, by this time they had to pay between 10 and 15 per cent of their budget for fixed asset investment to government to offset the cost of providing energy and transport when the enterprise group had already invested in its own small hydro-electric plant and more recently a coal burning plant. Moreover, they could use workers to drive their trucks to purchasers and they were 'on very good terms with the railway station' (it seems that the local railway station staff decide loading priorities) and so their transport needs were already met. Managers and economists from the Second Automobile/Dongfeng conglomerate negotiated directly with representatives of the state over the taxation payments that they would be obliged to make during a set period of either one or two years ahead. However, even the highly prized right to undertake direct negotiation (and often soft budget based manipulation) of taxation obligations, did not overcome the sensitivity surrounding the payment of tax.[33]

Tax-for-profit

In common with other managers from large advantaged state-owned enterprises, in 1985/86 managers and economists from the Second Automobile/Dongfeng corporation had lobbied against the introduction of the second stage of the Zhao Ziyang sponsored 'tax-for-profit' programme. As early as 1982–4 Zhao Ziyang had favoured a tax-for-profit approach and this had been supported by both Deng Xiaoping and by conservative reformers within the Party élite, including their nominal leader Chen Yun. Zhao had argued that it was an approach that would enhance the independence of decision-making by the managers of the state-owned enterprises. It was also an approach that in Zhao's formulation should be a two-stage project. The second, more radical stage, of this reform was planned to begin in late 1984, but 'the transition between stage one and two made heavy weather during 1985–6' and was finally abandoned in the spring of 1987 when it was announced that financial relations between the state and the enterprises would now be organised in accord with the 'contract responsibility system'. Subsequently, China scholars have asked the question – 'why was it possible for enterprise profit contracting to replace tax-for-profit less than three years after the tax scheme had been implemented?' The answer is that there does seem to have been a 'fast oxen stampede' of local government administrators and large state-owned enterprise managers lobbying against tax-for-profit and in favour of the contract responsibility system. In other words, the implementation of the tax-for-profit system was unsuccessful due to the minimum cooperation and even lobbying and resistance from both local government administrators and state-owned enterprise managers.[34]

The tax-for-profit system had had the effect of decreasing the revenue collected from the state-owned enterprises by local government administrations in favour of increasing state revenues. For their part the managers of state enterprises believed that the taxation burden placed on their enterprises had been increased. They argued that this increased financial responsibility 'hampered enterprise initiatives which were to be the core of the reform'. Moreover, mandatory planning requirements such as the then one-third of production that the Second Automobile/Dongfeng group had been obliged to provide to government mainly for purchase by the army, the persistence of the 'irrational' pricing of a large number of goods and services and the endemic interference by government in enterprise decision-making, meant that they could not yet be held responsible for their own profit and loss and so should not be taxed on profit without the formal opportunity to put their case and so negotiate and bargain the amount of their tax payments. The last minute *ad hoc* addition of an adjustment tax levied on the most profitable state-owned enterprises did provide opportunity for this type of negotiation, but still the tax-for-profit system was opposed. Indeed, the rational, impersonal, non-negotiable aspect of the tax system had been compromised by this *ad hoc* arrangement and yet the system continued to be resisted. In its second stage the tax-for-profit system was to specify eleven different taxes payable to the state. Party/state sources argued that this form of taxation would boost the use of tax as a means of disciplining enterprise level decision-making. In other words, it would boost the role of taxation as an economic lever to be used by the Party/state. In this capacity taxation could also function to offset the unfair discrepancies in profit that had grown out of the irrational pricing system. Ironically, under tax-for-profit the state only accessed a slight increase in taxation revenue in part because many elements of the tax-for-profit plan had not been put in place in the face of concerted local opposition.[35]

By 1986 a large number of state-owned enterprises were reverting to the previous contract responsibility system now glorifying in its new name of the ‘contracted management system’. Not surprisingly, this trend continued. At this point the Second Automobile/Dongfeng managers argued the then commonly agreed point that the tax-for-profit system had not worked and so they had no other option than to return to profit contracting. By 1987, almost 80 per cent had returned to profit contracting. The managers of the very large state-owned enterprises had won. They had demonstrated that they had considerable political clout and that they were prepared to use their direct association with ministries such as the Ministry of Heavy Industry, to play ‘an active political role within the ministerial industrial systems’. Indeed, the whole experience of opposing the tax-for-profit system had promoted their common interests and they had demonstrated to themselves that they were a coherent political force that must be reckoned with.[36]

While the tax-for-profit policy had certainly had its problems, these were not necessarily solved by reverting to the contract responsibility system. The contract system continued to promote the familiar coalition of state enterprise management and local government officials. Local administrators and *apparatchiks* attached to particular state ministries, colluded with enterprise managers to ensure that their enterprises paid less, or even evaded, tax payments. While it should be recognised that there has been recurrent targeting of state enterprise managers and local government administrators over the problems in the taxation system, authorities estimated that as many as 'seventy percent of enterprises practised some form of tax evasion'. When I asked about this extensive tax evasion in interviews with the economists and managers of the Second Automobile/Dongfeng group I was told that they had 'no option' other than to pay the taxation amounts requested of them and that if 'taxation evasion was overcome' the problem of government debt would be solved. Of course, the problem with this scenario is that members of the Second Automobile/Dongfeng management had been very energetic in terms of negotiating and bargaining the terms of their tax contracts.[37]

Taxing the Second Automobile/Dongfeng corporation today

It is obvious that the return to the contracted tax system could not be regarded 'as a further hardening of the budget constraint when compared with the former tax-for-profit system' and one of the additional problems is that taxation contracting has tended to last for relatively short periods of time and so tends to shorten enterprise planning horizons. The longest period is five years. The agreements struck by the Second Automobile/Dongfeng group were, as I have noted, for either one or two years ahead and like other contracts of this nature can be cancelled at any time with the agreement of both contracted parties.[38]

Today, the bulk of the Second Automobile/Dongfeng corporation's tax bill is made up of two parts. First they must pay the 'exchange transaction' (value-added) tax and second an enterprise income tax. The corporation has had to pay 15 per cent value-added tax with the announcement already made that it will be 17 per cent in future. However, as the enterprise group is running in the red and now shows no profit, it is excused payment of income tax on enterprise profit for 1996, but the rate that they have paid since the 1994 introduction of tax reform has been 33 per cent. The group is also obliged to pay a tax of 33 per cent on dividends and bonus income received from investment in shares. These shareholdings are predominantly in other state-owned enterprises and in some of the collective enterprises that remain as clients to the group. Economists from the Second Automobile/Dongfeng corporation felt that the combination of the value-added and profit and dividends taxes resulted in a level of taxation that was much too high. They graphically demonstrated their point with actions indicating a slit arm. They argued that the state was subjecting the large state-owned enterprises to blood letting, even though, at the moment, enterprise managers were 'putting up with this'.[39]

Though taxation reform had been flagged in 1992, it was not until 1993 that constructive discussion within the Party/state élite led to a substantial change in the form of China's taxation provisions. These changes began to be implemented from January 1994. Introducing the tax-for-profit programme and then amending the fiscal contracting system in order to 'correct' both the endemic tax avoidance practised by the managers of the state-owned enterprises such as the Second Automobile/Dongfeng corporation and the imbalance that had grown up between state and local government revenues, had both failed. The new tax system had to be a substantial change from the previously unsuccessful taxation systems, but it was not going to be primarily a vehicle for impressing leadership priorities on local level decision-making. It was overwhelmingly to be a means of revenue raising.

IRRATIONAL PRICES

A golden opportunity for price reform

When the Party/state's attempt to institute the second stage of the tax-for-profit system was aborted in the face of opposition from local agents, the opportunity to use the taxation system to overcome the state enterprise profit disparities predicated on irrational prices was lost. It is then not surprising that soon after the 1992 return to progressive economic policy, price reform was once again high on the agenda of China's Party leaders and state administrators.[40] Once again they argued, as they had throughout the 1980s, that China's programme for reform was being impeded by the relatively slow pace of price reform. State economists advised that the double-track pricing system that had grown up during the 1980s must be phased out because 'the advantages of the double-track system of prices have become less than the disadvantages' and because the double-track pricing system 'violated the principle of fair deal and the values of equality among all exchanges in [the] market'. They also pointed out that 'a golden opportunity to carry out price reform' had been missed, not only during the 1980s, but also 'in 1990 and 1991 when [under the influence of economic rectification] the market slumped and demand was low'.[41]

In other arguments presented by state economists in the wake of the 1992 return to progressive economic policy, they noted that if the problem of irrational pricing is not soon overcome it will be very difficult to motivate the state enterprises to increase production of relatively low priced raw materials and semi-finished goods. Enterprises involved in relatively low priced areas of production are not motivated to adopt new technology or to reduce expenditure. They are unable to show a profit. Moreover, in many cases price does not reflect quality of product. There is no difference in prices between good and poor quality goods. The best quality items disappear quickly. In other words, the problem of consumers (both wholesale and retail) substituting for their first choice of product comes into view and with it the practice of nurturing a relationship of obligation and responsibility with supplying enterprises is promoted in order to have access to the best quality materials available. As I have argued in Chapter 1, this is what the management of the Second Automobile/Dongfeng corporation do in order to ensure the quality and availability of the raw and semi-finished products required for their vehicle and automotive parts production.

A low price paid

Another problem born of the irrational price mechanism has been the low price paid for public utilities. During the 1980s many of China's very large economically advantaged state enterprises (again the enterprises belonging to the Second Automobile/Dongfeng group offer an example) by-passed government provided utilities on the same grounds that they by-passed domestically produced products for foreign manufactured goods. The price was relatively low, but the quality and supply was poor. While the Second Automobile/Dongfeng corporation used government railway facilities, they had, as I have noted, provided for their own energy needs and for many of the services required by their workers, including schools, shops and even a piggery and the zoo and public park in the centre of Shi-yan where the corporation's headquarters are located. Again, the example of housing comes to mind. Rent paid for housing has been no more than a quarter of the cost of maintenance, regardless of whether it has been provided by local government administrations or state-owned enterprises. (The quality and supply of the latter is far superior to the quality of the former.) It has even been pointed out that the average cost of a bath in a public bathhouse was only 0.26 yuan (in 1992 figures) and that this price did not even cover the operating expenses of the bathhouse.[42]

Price legislation

Recently a price law has been put before the National People's Congress. This law is to regulate price-fixing bodies and to standardise and regularise the price controls that continue to be used. For example, in Beijing in 1994 the market price of grain, cooking oil and eggs and meat all increased by over 30 per cent. The expected rise in retail prices nation-wide in 1994 was already 21 per cent. The Beijing price rise and indeed a proportion of the national price rise, was driven by an imbalance in supply and end consumer demand, but it was politically unacceptable and therefore required control. It is a situation that appears to be at odds with the 1990s recognition by China's state economists that it was wrong to delay or weaken price reform on the assumption that the relaxation of restrictions on prices is the only cause of inflation, but this is not the case. Price controls on the products in question had already been lifted. In other words, these prices had already been subject to reform. They were already sporting 'rational' market based prices. The controls put on agricultural goods by the Beijing municipal government were controls that were to be imposed on a temporary basis *after* price reform of these products had been effected and in view of the likely political cost that would be associated with such large market driven price rises for staple products.[43]

Price and inflation

By the 1990s, Chinese state sources were arguing that the primary cause of inflation was not scarcity in the face of end consumer demand, but 'over expenditure on fixed assets and the over-issuance of banknotes'. The point is that over-investment in fixed assets is the primary cause of China's persistently rising rate of inflation, but it is not the *only* cause. Inflation may also be promoted when government control of a selection of prices stops. This is because the price that the government has set is well below the level of a shadow price, particularly when the goods are raw materials or a product or service that has previously subsidised the real cost of workers' wages, for example, healthcare, education and housing. This means that when the government releases prices they rise, or to put it another way, 'the previously concealed higher price' is revealed and now must be paid. The structurally based economic subsidy has been removed. Another cause of price rises is when consumers believe that prices that have been released from government control will increase. They buy in anticipation and the supply of the relevant goods is stressed. This happened in 1988. Inflation was increasing rapidly, government price controls on a range of items had been recently lifted and panic buying led to a substantial increase in what were already sharply rising prices. Yet another important cause of price rises is when rural producers, operating in accord with hard budget constraint and using market prices for the product that they sell after satisfying the requirements of their government-set grain quotas, find opportunity to raise the price of their products. This happened in many areas, including Beijing, in 1994, at the same time as fixed asset investment that followed the 1992 return to progressive economic policy, was once again being promoted by local agents.[44]

When compared with the previous simple 'unbalanced economy' explanation of the cause of the cyclic inflation that had been experienced in China since reform, the 1990s perception that 'uncontrolled capital construction and rapid money supply expansion' is a fundamental cause of inflationary pressure, offers a much more sophisticated explanatory thesis. However, there was some truth to the earlier 'unbalanced economy' point of view. When the increasing state-owned economic sector of China's productive capacity was expanding even further, particularly during the second half of the 1980s, there was, as I have argued in Chapter 1, an ever-worsening discrepancy between the supply and demand of raw materials and semi-finished products required for manufacture. In other words, there was an imbalance between demand and supply, but as I have argued, the primary cause was not an imbalance in supply and demand in end consumer markets. It was the successful pull on bank funds for the purpose of fixed asset investment that had been effected by local agents, the array of other government subsidies both official and unofficial that had been won by negotiation and manipulation of Party/state policy by local agents and the scarcity of raw and semi-finished materials resulting from the rapid expansion of China's industrial productive capacity that had been predicated on the fixed asset investment initiated by local agents.[45]

Another point should be added for consideration at this stage in my argument. This is that China's underlying rate of inflation 'remains higher than the official figures indicate'. It is because price reform has been postponed. That is, the extent of China's reforms in relation to the price reform that has been undertaken and so the artificially low prices for raw materials and the low price paid by consumers for staple goods throughout the 1980s, particularly for grain and coal, has had the effect of reducing the rate of inflation. The price paid by both manufacturing entities and end consumers for basic necessities has been heavily subsidised and to a lesser, but still significant extent this subsidisation continues. It includes decentralised subsidisation. In spite of the decree that they must divest themselves of their welfare responsibilities, state-owned enterprises continue to subsidise worker housing, albeit in a somewhat different manner. As I have argued, they offer lower purchase prices for housing to their workers and offer wage subsidies for those who have agreed to purchase their housing needs. State enterprise managers also subsidise the price of wages (the labour time required for production) when they retain those who are stealthily unemployed. There are also numerous cases that parallel the Beijing municipal government's control and their subsidisation of prices that have already been left to the market to determine. In 1994 when the price of a wide range of staple foods rose, the Beijing municipal government was forced to spend an estimated five and a quarter million yuan on subsiding market set prices. This was over one billion higher than the cost of subsidies in the previous year.[46]

Juxtaposed to the scenario outlined immediately above, by the early 1990s China's state economists were arguing that 'if administrative power [at any level] is integrated with the buying and selling in the monetary economy, it will destroy the market force'. They noted that price distortions result in the continued need, even after more than a decade of reform, for the state to intervene through price subsidies, tax breaks, or the extension of credit in order to off-set allocative inefficiency created by a distorted price system. They then argued that a market is 'worse than none if it has been twisted by administrative power and becomes noncompetitive'. They cautioned that this situation provides opportunity for corruption, negotiation and bargaining and so causes inefficiency and they pointed out that it may even lead to the economic disorder that they described as the "'India Syndrome", [the] "Marcos Trap" of the Philippines, or [the] "Latin America[n] Phenomenon'".[47] Then, having argued that past opportunities had been missed, particularly the opportunity that the 1990/91 situation afforded 'when the market slumped and demand was low', they advised that now no time should be lost in promoting further price reform. This point was then linked with the advice that, from the low cost/high benefit point of view, it would be best to ensure 'that the prices of raw and semi-finished materials, energy, transportation, and other means of production should be reformed first'. This was seen to be preferable to offering taxation breaks, credit priority and price subsidies to these vital sectors of the economy.[48]

There has, of course, long been considerable Party/state and local government concern in relation to the extent of both direct and indirect price subsidies paid. This concern has been exacerbated by the increasing problem of rising government domestic deficits and lower taxation revenues and has been presented together with the lament that direct government subsidies are continuing to be extended to loss-making enterprises. Like end consumer subsidies, enterprise subsidies are also seen to be politically useful, but they are undermining monetary policy. Chinese state economists now argue that 'the amount of subsidies for prices and for deficit state enterprises are excessive'. They also note that the 'serious distortion' of prices and a 'too heavy burden for government finances' has been the unwanted and unsustainable result.[49]

Undermining monetary policy

Today, China's Party/state economists argue that even though direct administrative price subsidies have been steadily reduced, the Chinese economy is 'in the red because [to date] we have had no choice' other than to provide price subsidies. After all, 'forcing a balance between revenue and expenditures with disregard to necessary conditions would produce [unwanted] side effects'. Thus, price and state enterprise subsidies and the pace of price reform have had to 'take into account the tolerance of enterprises and citizens'. They find that they have had to advise that 'too much haste will not help'.[50] Their argument is tantamount to stating that political concern dictates the adoption, or otherwise, of specific economic policies, even when it comes to price reform: a reform that is no longer seen as an economic lever that can be used by the state to influence the developing market, but is seen as the litmus test for judging the progress that is being made in China's bid to develop a market integrated economy.

True profits

There are obvious and significant problems arising from irrational prices. For example, state-owned enterprise profit calculation has been difficult. The perception of 'fair' profits provides a basis for equitable methods of calculating enterprise bonus rates and ongoing eligibility for bank loans. It is also the basis of taxation payments that adequately reflect real income and profit earnt. If the management of a state-owned enterprise contrives to make a loss by reducing the sale price of their products they are excused their taxation obligations and may well qualify for government subsidies. Moreover, the nexus between price and equitable rates of taxation would not be solved by the introduction of value-added tax (VAT), rather than enterprise profit tax, as the main source of government financial sustenance. Nevertheless, often value-added tax is perceived to be fairer and it does overcome the problem of enterprise losses equalling no taxation obligation. In short it is 'a better accounting measure of "true" profits and losses in traditional [state-owned] enterprises' and the pressure to exempt not only those collectively and privately owned enterprises that are already subject to hard budget constraint, but also the reforming state-owned enterprises from paying this tax, 'would be minimal'.[51]

TAXATION REFORM IN THE 1990s: A PRESSING NEED FOR A NEW SYSTEM

Reduced receipts

The reduction in government taxation receipts is one of a number of the disquieting effects of reforming centrally administered economies. As I have argued, with economic reform the state's centralised administrative apparatus is consistently weakened. 'Decision-making and [even] effective property rights devolve' and this leads to a situation where, 'because of the implicit nature of the old system of taxation', an increasingly serious revenue crisis emerges. As the reform process continues and state-owned enterprises come closer to being entities 'that are no longer controlled by the government', the government reaches a point where 'enterprises can no longer so easily be used as revenue (cash) cows'.[52] In China that point (where the state industrial enterprises can no longer be the government's cash cows) has been accelerated by the stringent economic policies approved by the leadership during the 1989–92 period of rectification. That period of contractive economic policy (implemented against the backdrop of over-extended production capacity that in the latter half of the 1980s had been promoted by China's local agents) resulted in state-owned enterprises no longer showing their previous level of profit. At that stage, at least one-third and more likely almost one half of China's state-owned enterprises moved into the red, with some sources suggesting that once the new accounting system had been put in place at the beginning of 1994 and the losses 'hidden' in state enterprise accounts had been 'uncovered', more than 60 per cent of China's 70,000 state-owned enterprises were in deficit. The Chinese state, like other reforming governments in 'desperate need of revenue' has initiated 'continual and unpredictable reinterventions' in the economic affairs of its state-run enterprises.[53] That situation has led to wide-spread discussion and to the subsequent adoption of a new taxation policy.[54]

In China, as the tax-for-profit debacle suggests, even before the drop in the state enterprise profits associated with the 1989–92 period of rectification, central government taxation revenue had fallen substantially. It has been estimated that 'between 1979 and 1989 the proportion of China's central government revenue to the country's gross national product [had] dropped from 19.9 per cent to 6.9 percent', while in the period from 1986 to 1992, with the gross national product growing at 'an average 15.9 percent annually in terms of current prices . . . the average annual growth rate of our [all government – central and local] financial revenues (excluding bond revenue) was a mere 8.4 percent'.[55] The share in the national revenues of the government's financial income has dropped steadily throughout the period of economic reform. In 1979 it was an estimated 31.9 per cent of national revenue, but by 1991 this proportion had dropped to 19.54 per cent (excluding government monies raised via bond issues). The latter was recognised as a percentage that was 'less than the minimum revenue that the state should possess in order to carry out its financial functions'.[56] Moreover, by 1992 it was clear that monetised government deficits would increase the pressure on inflation. When this inflationary pressure was released it, in turn, would have an adverse effect on government tax collection. This is because at high inflation rates the tax system, 'with its collection lags and the disruption of economic activity, yields less and less revenue'. The result is a round-about in which the deficit is aggravated and there is then still more pressure placed on money growth.[57]

Obviously, if the Chinese government's revenue raising is to be effectively maintained (and if possible, increased), new taxation measures had to be implemented. This is the only way of effectively addressing the immediate concern of China's economists and planners to overcome the situation where 'the growth of central financial revenue lags far behind that of the national economy'. The central government was plagued with budget deficits. It was estimated 'in 1992 the decrease [in government taxation receipts] had been 33 percent [and] in 1993, from the first to third quarter, the decrease had been 38.5 percent'.[58] Clearly the new taxation system would need to look past state-owned enterprises for sources of government revenue. Nevertheless, much of the focus of taxation reform came to rest on the question of how to make state-enterprises pay taxes. At the same time, the taxation system was to continue to be charged with performing two functions. First and foremost, it was to be made responsible for raising revenue for government and second it was to be obliged to assist in the state's bid to discipline the decision-making of local agents. The first function is an obvious requirement of effective government and the latter is in line with the leadership's bid to strengthen financial tutelage of local government and state enterprise decision-making while at the same time pushing enterprises toward the market. Obviously, the ideal taxation system from the point of view of the state would be functioning to restrict the endemic and unwanted investment hunger, while at the same time operating to raise revenue in what is to be an increasingly market-integrated economy.

A new system for taxation: a VAT

By 1994 the Chinese leadership had agreed that the core of the much needed new taxation system would be a re-vamped value-added tax (VAT). They announced that a value-added tax would apply to 'the whole process of commodity production and circulation'. The tax would be levied on the manufacture, production, import and transfer of goods at a rate of 17 per cent, with goods deemed to be essential attracting a lower 13 per cent rate. The tax would be recoverable on all raw materials which have been used in manufacture and production processes. In line with the requirements of a market-integrated economy, this form of revenue collection was touted as 'impartial, neutral, universal, and simplified'. Its strength was said to be that of 'a good taxation collection climate' and would reduce 'the occurrence of repetitive levies'. It was argued that it would overcome the bargaining and negotiating that had been a feature of post-reform taxation payments.[59] To some extent this is what happened, but it was nevertheless misleading to present the new VAT as the main vehicle of a simple taxation process. The new VAT was implemented together with a number of other taxes including the existing business tax that had been left in place. This retained tax would continue to be used to tax service sector enterprises, including those engaged in transport, communications, real estate and insurance and it was to reside alongside tax levied on enterprise profits. There was also to be a consumption tax of between 5 and 45 per cent levied on luxury items such as tobacco, alcohol, cosmetics, cars and refined oil. A blanket and simplified value-added tax which stood alone could have been expected to reduce the opportunity for soft budget negotiation and bargaining between representatives of the state and local agents, but tax rebates on exported product and the retention of tax on enterprise profits (complete with tax deductions for interest paid on enterprise loans, donations to education or poor relief and wage and worker welfare provisions) will keep that avenue of soft budget tax negotiation open, even though that was not what state administrators had intended.[60]

Promising not to increase tax rates

During the discussions leading to the adoption of the new tax measures, Party/state administrators used comparisons with Western market economies to promote their argument that China's taxation system must be overhauled and, at the same time, they pointed out that taxation reform was not intended to increase the tax burden borne by either state-owned enterprises or consumers. Indeed, it was said that reforms 'would neither give enterprises added tax burdens nor trigger price increases'. Central government administrators also went to considerable trouble to point out that the reforms will not upset tax policy applying to foreign investment. They often stated that the tax reforms have 'followed an important policy of not increasing the tax burden on enterprise with foreign investment'.[61]

With the suitable reassurances that had been given that prices and the overall tax burden would not be increased, the newly constituted consumption, individual income and resource taxes did not appear to meet much opposition. The consumption tax was wisely presented as a tax which 'does not directly affect commodity prices' and in any case applies only to commodities other than daily necessities, but the land value-added tax that was introduced at this time was in effect a property gains tax which represented a completely new taxation initiative and so it was hotly debated.[62] However, this was not only because it was a new tax. It was also because it was thought to be 'quite possible [that] the tax is a precursor to a full Capital Gains Tax . . . on all property'. In essence this value-added tax reflected the central government's dual concern to raise revenue while at the same time disciplining the boom in real estate investment that had been taking place in southern China. State administrators sought to exercise some control over the burgeoning real estate market which had been plagued by speculative dealing by those with particular (rather than national) interests and who ignored concern over such issues as the decrease in China's most productive farm-land. This is one instance when Beijing was very keen to exercise both aspects of taxation policy. In other words while they were pleased to collect revenue from this tax they were anxious to use the tax as a means of 'regulating trading order in land and property markets'. State administrators were seeking 'to put the rights to grant concessions and exemptions on real estate outside the power of provincial and city governments' and others, so as to curb the speculative opportunities of state-owned enterprise managers who had an interest in real estate transactions or more usually, companies that were sub-sections of their enterprises or even of state-owned banks. The tax went some way to achieving that aim. For as long as negotiation between provincial and central governments did not undermine its measures, the tax was a useful means for strengthening the Party/state's macro-economic control over both the burgeoning (and very often undisciplined) early 1990s local government and enterprise bond issues and real estate transactions.[63]

The need for standardised taxation procedures

During 1993, discussions of taxation reform placed considerable stress on the need for the standardised, impartial and legal enforcement of taxation initiatives. This focus was consistent with the central government's recurrent drives to ensure that enterprise taxation is paid on time and in full. China's procuratorial organs were put on notice that they must 'strengthen supervision over law enforcement when they handle [taxation] cases'. They were told that when they are concerned with taxation cases 'they must pay attention to discovering various irregularities in the handling of tax law enforcement'. At the same time, Party/state sources again noted that 'there have been great losses in taxes' and that a system whereby 'enterprises pay [a value-added] tax plus a percentage of profits [would] strengthen supervision of tax collection by law'.[64] The principal feature of the new tax measures that were under review in 1993 and introduced at the beginning of 1994 was the determination more effectively to overcome the situation where 'the proportion of central [state] revenue has decreased by a large margin'.[65]

Raising funds

Though the three-year period of economic rectification was over by 1992, the concerns of those representing both the state and local government interests and also, the concerns of managers of China's state-owned enterprises, were still dominated by their need for funding. Faced with a taxation system that could not deliver sufficient monies to fund even existing commitments, the state and local provincial governments increasingly depended on bond issues as a means of raising funds. Government bond issues then 'increased quickly year after year', while at both the national and local level the soft budget deficit was used to both balance revenue with expenditure and to support further economic development and growth.

During the first months of 1993, China's state economists and planners were arguing that maintaining financial influence is vital to the successful promotion of a mature market-integrated economy. At this time, there was some redefinition of the economic responsibilities of the state and provincial governments, with the return of more control (at least in theory) to the state, but that is not all there was to the reforms in taxation. While Chinese economists and planners were 'emphasizing the active role of fiscal and taxation policy' in both raising revenue (via new taxation policy) and disciplining local interests (now primarily via the banking system), they were also proposing that taxation be used as a vehicle for 'readjusting social economic structures and social distribution'.[66] At the stage that China's reform has reached that is a very tall order. It was clear, however, that China's economists and planners were considering the possibilities of a well-developed taxation system in terms of effecting progressive redistribution. One should add that for that taxation possibility to be realised in its most developed form – that is, redistribution to individuals on the basis of routinised welfare criteria – there needs to be further development of an understanding of individual rights and interests. We can see the beginnings of this in measures such as the regulations on minimum wage rates, terms of dismissal and maximum working hours that have now been adopted.[67]

Negotiation, arrears and bargaining

In spite of the economists from the Second Automobile/Dongfeng corporation's claim that the new taxation system has been bleeding their enterprise dry, state administrators claimed that it is too early to tell whether large state-owned enterprises are better or worse off under the new tax regime. This was two years after its initial implementation. They claimed that 'the new tax system operates in complicated ways' and that the tax burden of state-owned enterprises 'will go up or down depending on their industry', but the Second Automobile/Dongfeng group of enterprises are in an industry that is high on the state's list of industrial priorities and they believe that their tax rate has risen. My view is that with a reduced scope that a value-added tax has provided for negotiating and bargaining over their tax rate, the tax burden of the group has probably risen. Moreover, they are adversely effected by transport expenses not being made tax deductible and, like cigarettes, liquor and cosmetics, cars and refined oil, are in the higher taxed consumption category and so their sales may well be affected. Indeed, this may go some way to explaining their growing stockpile of unsold automobiles.

Nevertheless, the new taxation system has appeared to have done what it was primarily intended to do. By 1994 it was increasing central government tax receipts by almost 6.5 per cent for the first nine months of the year and local tax receipts by 'a striking 37.1 per cent'. By 1996, this time over a six-month period, it was increasing state taxation revenues by as much as 7.5 per cent and local government revenues by over 28 per cent. Some observers have argued that these results are 'not so impressive' when viewed from the point of view of the relationship between tax receipts and gross domestic product and when state and local government receipts are compared. However, Chinese sources argue that the new taxation system has been successful, though they continue to complain that the state-owned enterprises have been slow to meet their tax obligations and they tell provincial taxation departments that they must 'crack-down on all activities involving tax evasion and fraud' and that they 'should adopt measures to collect unpaid taxes'. By the end of 1995, it was being argued that while state enterprise funds are tight and so many enterprises are finding it difficult to meet their economic obligations, the managers of state-owned enterprises are choosing to delay their tax payments, rather than delay meeting other commitments. This has meant that 'enterprise tax arrears are already crimping the increase in tax revenues' and in the period since the introduction of taxation reform, it is these tax arrears more than any others that have resulted in taxation payments falling below the amount projected in the annual plan.[68]

As the opposition of interest between the state and local agents has been both promoted and made increasingly transparent under reform policy, the negotiating and manipulating strength of local agents in relation to the state has increased. This situation was reflected in the local opposition that resulted in the failure of the tax-for-profit programme. It has obviously not been in the interests of local agents to reduce their negotiating opportunities. After all, not only did state enterprise managers bargain with state and local administrators over the terms of their tax contracts, but local government officials also bargained with state administrators over their provincial taxation contracts and in their turn, counties would bargain with their provincial governments over the taxation that they were obliged to remit to them. The question now is – why has the central government been able to implement a new taxation system that is far more standardised than the previous system? State-owned enterprise managers are complaining and local government officials have stated that the interests of local government have been 'sacrificed' for the state, though the provincial governments seem to be resisting their impoverishment. For example, the Wuhan City tax bureau has been caught circulating an internal document that lists as many as sixty-three provisions that counter the new tax regulations and have resulted in the state losing a very large sum of taxation revenue.[69]

Dividing taxation received

The taxation reform formulated in 1993 and introduced in 1994 represented a paradigm shift. Indeed, some scholars have asked why such sweeping taxation reforms were introduced at this time. Their answer has been that 'by 1992 the psychology of the political participants had shifted'. Leadership 'nerves' had settled down. The 1989 Tiananmen Incident was now behind them and, at the same time, the period of economic rectification had further 'exposed' the weakness of the government's financial position.[70] Accordingly, the new taxes were divided into three categories: those belonging to the state; those taxes to be shared by the state and provincial governments; and taxes belonging to local government. Only the consumption tax levied on cigarettes, cosmetics, cars and refined oil belongs directly and exclusively to the state, but this tax does amount to 10 per cent of overall taxation receipts and it is the tax most likely to grow as living standards, particularly those enjoyed by the urban élite, continue to rise.[71] Even more importantly, the new taxation system has represented a victory of the state's interest over that of local agents. While the new taxation system is primarily a revenue raising mechanism, rather than an avenue for impressing state priorities on local level decision-making, its implementation has, nevertheless, been a victory in terms of the Party/state's management of the opposition of interests between those who represent the state and local agents.

CONCLUSION

The Chinese leadership élite have had a long history of combining theoretical considerations with actually existing economic, social and political conditions. In the period following the 1992 return to progressive economic policy, this combination of theory with actually existing conditions led to the adoption of policy measures that members of the leadership intended to use in order to successfully manage the increasingly transparent opposition that they now recognised as existing between the state and local agents. They also sought to promote an ongoing climate of political stability and unity. However, in the immediate future this climate of stability will have to be purchased with the leadership's willingness to forgo substantive banking reform. As I have argued above, the brief of China's centralised People's Bank is to control credit with minimal (social and political) side effects, but the reasoning behind the taxation reforms implemented during the same period is quite different. During the 1989–92 rectification the existing problem of relatively decreasing government tax receipts became an acute problem. Moreover, while the return to progressive economic policy promoted the renewal of price reform and so reduced the level of irrational pricing, it did nothing to solve the problem of declining tax receipts. Indeed, the ongoing process of reform exacerbates the problem of declining government taxation revenue. In other words, reform makes it increasingly difficult for the state to maintain its financial viability unless taxation reform is instituted. Tax revenues must come to depend on sources other than the qualitatively assessed profit of the state-owned enterprises. In China the decline in taxation receipts was considerably exacerbated by both the perceived unfairness of irrational pricing and the behaviour of local government administrators who negotiated and manipulated economic relations in their own favour. They husbanded their resources for projects and enterprises within the scope of their jurisdiction, even exploiting the soft budget constraint enjoyed by the specialised and commercial banks in order to satisfy their interests.

In the immediate post-January 1992 period, the intention of Party/state administrators to discipline local interests while promoting price reform and other measures associated with the development of market exchange, combined with their bid to avoid significantly high rates of inflation, explains their unwillingness to initiate fundamental reform of the banking system. This is the situation that has provided political support for further strengthening the supervisory role of the People's Bank. China's leaders began to consider policy initiatives informed by the question 'What domestic fiscal and monetary reforms would be necessary and sufficient to constrain enterprises . . . from overbidding for the economy's scarce resources?' In other words, how best could they manage the opposition of interests between state and local agents?[72]

Very soon after the 1992 return to progressive reform policy it became clear that the regulatory role of the People's Bank was not to be undertaken without intervention from various government ministries, particularly the Ministry of Finance. For example, the Bank was, and still is, obliged to follow ministerial guide-lines, and at the end of the day, loans for its client specialised and commercial banks are advanced in accord with the industrial development priorities established by the Party/state. Recent guide-lines have dictated that the client banks authorise loans for enterprises such as the Second Automobile/Dongfeng corporation, even when these enterprises are running in the red. The result is that the Second Automobile/Dongfeng group continues to raise circulating funds and development capital on the basis of the group's past success, its size and the number of urban industrial workers that it employs, its status and its position as one of the ‘three bigs’ in China’s planned future automobile and automotive spare parts production. Monies are advanced on the basis of the group’s priority in the industrial development plan of the state’s industrial ministries. The corporation is too politically important to close.

4 Ownership reform

Establishing a modern enterprise system

> Through transformation to the shareholding system, we are beginning to be able to resolve deep-seated economic problems such as readjusting the industrial structure and enhancing the vitality of state-owned enterprises.[1]

Having chosen to forego the introduction of a market for capital that would be facilitated by the banking system, Party/state sources have been in a position to boast that they have been successful in instituting macro-economic control. In other words, the opposition of interests between the Party/state and local agents (particularly the opposition of interests between the state and the managers of China's largest and most politically important state-owned enterprises) are seen to have been successfully managed. However, at the micro-economic (state-owned enterprise) level it is a different story. The situation at the level of the enterprises is a matter of concern, particularly to those who represent the Party/state. As I have argued, enterprise debt-chains have continued, tax arrears are commonplace, unsold goods are stock-piled, state enterprise managers continue to neglect to pay, or are at least slow in repaying bank loans, debt is hidden within the accounts of the state-owned enterprises and a large number of these enterprises, even those on the state's industrial priority list (for example the Second Automobile/Dongfeng corporation) are now running in the red. In this context architects of China's progressive reform initiatives are advising that, at this point in China's reform programme, powers that need to be centralised should be 'held firmly' by the Party/state, but powers that need to be granted to lower levels should be decentralised without reservation. China's centralised banking system falls into the former category and ownership of state enterprises is now to be assigned to the latter.

It is against this back-drop that China's leaders have decided to promote the ownership reform policies that I discuss in this chapter.

Their much heralded initiative has been to support the ownership reform policy that they have already trialled using one hundred carefully selected state-owned enterprises. In spite of the opposition from conservative members of the Party élite during the latter part of the 1980s and the opposition and the need for caution that is being voiced today, the decisions of the recently convened Fifteenth Party Congress make it clear that there are core members of the Chinese Party/state leadership who believe that further restructuring of the ownership of China's state enterprises can be accommodated within the scope of China's authoritarian political rule.

Restructuring the ownership of China's state enterprises has the potential to overcome not just one, but two and possibly even three increasingly pressing reform problems. The first is the Party/state's need to continue the process of developing a market economy. After all, the continued political authority of their Party depends both on their ability to foster ongoing political stability and unity *and* their expertise in implementing policy that promotes their agreed and much published goal of developing a market economy. As commentators have pointed out, 'to be tentative or pusillanimous [in relation to reform] is disastrous'.[2] The second problem is the need to overcome a situation that I have referred to above. It has been aptly described as macro-economic control and micro-economic chaos. In other words, while labour, banking, pricing and taxation reforms have all been seen to contribute to either macro-economic control or the development of a market-integrated economy, China's state-owned enterprise reforms have not yet delivered either a real separation between government administrative and state enterprise decision-making nor enterprise management decision-making based on investment to profit ratio. The third and potential problem that this reform would solve is that it would remove the Party/state from direct responsibility for issues such as price rises, enterprise debts and taxation defaults, workers' conditions, welfare and social security provisions and unemployment.[3]

DEBATING OWNERSHIP REFORM

The case for ownership reform

Those among the Party/state élite who argue for the restructuring of the ownership of China's state enterprises maintain that the development of a market economy is currently impeded by the lack of mobility in state assets. They caution that the use of state assets is becoming less and less satisfactory and they argue that the reason is 'the immobility of considerable quantities of low-efficiency and ineffectively allocated' assets. And, they argue that the endemic problem of low efficiency must once again be sheeted home to the absence of clear lines of responsibility for enterprise performance and to the enterprise 'burdens' of debt and 'excessively heavy social responsibilities'. The latter includes the provision of housing, health and education facilities for enterprise staff and workers and is coupled with work-forces that carry 'surplus' personnel and exhibit unacceptably low worker productivity. The pro-ownership reformers' concern to overcome the social responsibilities currently borne by the enterprises is reflected in the current pressure to press labour reform as far as politically possible coupled with the Party/ state decree that enterprises no longer attend to the welfare needs of their workers. At the same time, the problems of enterprise debt and the lack of clear lines of responsibility for enterprise performance serve to underline the inappropriate economic decision-making adopted by enterprise managers. In essence this issue comes back to the enterprise managers' habit of manipulating and negotiating policy in the context of their soft budget constraint. As I have argued, the adherence to rules, regulations and policy continues to be negotiated and state enterprise managers have not yet been diverted from their belief that cost overruns will be recouped from government sources. At the same time, they complain of government interference. They are particularly sensitive over situations where government pressure has been applied, as for example, when provincial labour bureaux foist workers on to enterprise payrolls. However, in some quarters, it is not only the managers of state-owned enterprises that are being blamed for the economic problems of the moment. Government administrators are also being asked to take a share of the blame. While it has long been recognised that local labour bureaux have been keen to push their own interests without concern for the wider reform ramifications of their actions, it is now recognised that government administrators at all levels, including those state administrators who inform the policy choices of the Party élite, have not been sufficiently concerned with profit rate. They have not seen it as an important part of assessing official achievements. Rather, they have used state-owned enterprises to fulfil other policy objectives. In this argument those favouring ownership reform recognise that managers of state-owned enterprises have been rewarded for continuing to be 'only cognizant of their position in the national planned economy'. Their enterprises have accumulated significant debts while their concerns have continued to revolve around 'the condition of channels of supply, production, and sale within the [parameters of the] planned economy'.[4]

Others from within the ranks of the pro-ownership reformers argue that macro-economic policy can currently be counted as a success in terms of its management of the demands made on the state, but they warn that it is already 'under considerable pressure'. They offer a scenario where 'the economy will touch down, only to take off again' and point out that unless further structural reform is implemented 'investment will inflate [and] the economy will overheat again'. Moreover, under the present macro-economic regime and central regulations and controls 'local government administrators and enterprise managers are complaining'. This group of pro-ownership reformers then point to the extent of state enterprise losses and to the urban unemployment problem that continues to 'become more serious'. For our part, we should not be surprised that these pro-ownership reform economists argue that the answer to these problems does not lie in further tightening of macro-economic control. They argue that this is a flawed economic 'solution'. It was the solution offered by the conservative faction within the Party élite during the 1989–92 period of rectification. The 'hard landing' prescribed at this time squashed inflation and reduced the over-extension that had occurred in productive capacity, but, as I have argued, it exacerbated a range of existing economic problems and generated others. The rectification period offered little in the way of structural reform when it is structural reform that provides 'real' answers. These pro-ownership reform economists reinforce their preference by arguing that it is 'only the intensification of reform' that will lead to 'the economy genuinely entering a benign [economic] cycle' and that, at the moment, the biggest problem facing China's reform programme is the situation that many large and medium state-owned enterprises occupy. Not only do they have too high a debt rate, heavy social burdens and too many unneeded personnel (though I fail to understand how a likely solution to this problem would overcome local government and enterprise worker complaints about the rising rate of urban unemployment), they continue to be subject to an 'unclear separation of government administration and enterprise management'. These reformers stress that the way forward is to remedy these problems through further and very thorough ownership restructuring.[5]

The case against ownership reform

Those opposed to the introduction of ownership reform present their arguments in a manner reminiscent of the conservative position as it stood in the latter years of the 1980s. They ask the question – what is socialism? Then they argue that 'the essence of socialism does not come from nowhere'. They maintain that 'it comes from the public ownership system'. They argue that if public ownership is not preserved then 'the eradication of exploitation or the elimination of bipolarization to reach the goal of common prosperity is nothing but nonsensical talk'. They express a concern that with ownership reform state enterprise workers will no longer be the owners of the means of production. They will be employees. Though, we might note that they are not currently using this argument in relation to labour market reform.[6]

Another strand of argument used by those who press Marxism into use as a bulwark against state enterprise ownership reform, charges that it is special interest groups who are pursuing privatisation. In an argument mirroring Mao Zedong's Cultural Revolution position that vested interest groups would undermine China's socialist revolution, they press their view that special interest groups have self-interested agendas that have nothing to do with reform. These groups, they argue, 'take advantage of the confusion created by reform and reap staggering profits by undermining state property'. This is an argument that has been made believable by the self-interested behaviour of many during enterprise-owned land, service industry and share-based privatisation that has already taken place. Leaving no useful stone unturned, those opposed to privatisation have also harnessed the confusion they find in Central and Eastern European nations and the former Soviet countries to their cause. They argue that privatisation's 'serious distortion of the intention of Marx, in essence resembles the current open practice of Eastern Europe and Russia'. Then, taking another tack, they argue that as share ownership is a central tenet of state enterprise ownership reform, it should not be thought that this reform would allow legal owners to influence management practice. After all, under share ownership 'the ownership and management of large and medium-sized enterprises (or companies) become increasingly separated'. Share owners have a very restricted role, or more often, they 'play no role at all'. Therefore, those who promote enterprise privatisation and so 'advocate economic Westernization' are pressing a 'great regression in both theory and practice' on China's socialist society.[7]

In spite of their tirades against state enterprise ownership reform, many of those promoting the argument that is presented against restructuring the ownership of state enterprises do not rule out private ownership as an integral part of the Chinese economy. In a manner that is a rerun of the plan and market argument favoured by conservative members of the Party/state élite in opposing Zhao Ziyang's reform initiatives, the opposition's argument allows that private ownership is acceptable in a socialist society as long as public ownership remains the dominant mode. As long as exploitation is kept within limits, they argue, the gap between rich and poor will not develop into a bipolarised society. They go on to caution that they must be extremely vigilant at the moment. This is because 'extremely harmful arguments' have been 'spread everywhere'. These spurious arguments claim private ownership is superior to public ownership.[8]

The case for caution

The claim that private ownership is superior to public ownership is also an argument that bothers those who are counselling care in the adoption of ownership reform. State economists and planners in this group include Ma Hong. He is a former president of the Chinese Academy of Social Sciences and he was the architect of the ill-fated tax-for-profit programme that I discussed in the last chapter. In an article that he co-authored with a member of the Industrial Economics Institute of the Academy of Social Sciences, he has argued that the popular understanding 'that property rights reform is tantamount to practising privatization' should be examined carefully. It is, he counsels, an uncritical assumption based on the proposition that 'private ownership enjoys a higher efficiency than public ownership'. It does not give sufficient recognition to the manner in which reform has been implemented. He notes that since the introduction of reform the private sector has grown strongly in both the urban and agricultural sectors of the Chinese economy, but that the publicly owned sector of the economy, including the state-owned enterprises, has played a central role in both improving people's living standards and in the 'gradual' development of 'market socialism'. Writing during the first weeks of 1995 he points out that even as late as 1993, the state-owned and collective enterprises combined accounted for 80 per cent of total industrial output. (In the first half of 1994 state-owned enterprises alone contributed an estimated 53 per cent of total national output. During this period state-owned enterprises paid 66 per cent of all profit and tax payments to government.)[9] Ma then changes tack. He advances the view that the preferred path would be to recognise the importance of upholding public ownership, but without assuming that 'the old form of public ownership needs no reform or has little room for reform'. He has a checklist. First, particular people and administrative institutions must take responsibility for managing state-owned assets. These assets belong to the whole people. Enterprise managers have been given a mandate to administer enterprise assets, but this does not mean that the assets belong to them, nor has it meant that they have been allowed to take discrete management decisions on behalf of the enterprise. Government interference has continued. When errors of judgement have occurred or enterprises have continued to be in debt, 'no one [has] seemed to be responsible'. Moreover, those enterprises that have been involved in becoming corporations that include joint stock holdings and even share based limited liability companies have continued this no fault tradition and even though further enterprise ownership reform has reached the point of being trialled, 'the question of who can act as the shareholder of state shares' has not yet been resolved.[10]

The second problem that particularly concerns Ma and other cautious reformers, is the issue of the undervaluing of state enterprise assets that have already been converted to either joint stock arrangements or shareholding limited liability companies. Exasperated economists have argued that 'the drain of state assets that is going on among many State firms' has not been effectively checked by government administrators. They advise that 'efforts already made by government departments in halting such losses are like a bamboo crate, which cannot hold oil without leaking'. In an effort to bolster government control of the management of state assets, Supervision and Management Regulations have now been drafted and adopted. They are administered by The Enterprise Bureau of the State Economic and Trade Commission in order, it is said, to 'make it clear that state assets in enterprises belong to the state' and to 'supervise the maintenance and increase in the value of enterprise property'.[11] However, Ma is still concerned. He argues that, even aside from the issue of 'plundering' assets that belong to the Chinese people, 'no one can guarantee that a small number of people, who have successfully grabbed state assets . . . will invest their money in production instead of throwing money about like dirt'. The ownership regulations that he would like to see adopted would include both a state instigated process of standardising the process of property transfer and the use of rules and regulations intended to ensure that if those responsible for enterprises chose to take economic risks, they would be held legally responsible. Ma's preference would be for a well organised, even gradual, process of property transfer that leans heavily on the effective implementation of standardised and legally binding laws and regulations that apportion responsibility. He is not advocating that the process of ownership reform be stopped. On the contrary, he warns that 'immobility will lead to even heavier losses to state assets' and that 'just because something has gone wrong with state property transfers', does not mean that this avenue of further reform should not be followed.[12]

For the cautious ownership reformers the way forward must not only include the increased use of the law, but also policy that will promote the 'technical renovation' of China's productive capacity. This requires improved production machinery and technical training for workers and it means that those with the greatest technical expertise in management must be pushed forward. Promoting technical renovation has been a repeated and difficult to implement reform policy. Even when we leave aside the often inflexible and relatively low price paid for industrial labour time, as long as status in extending quantitative productive capacity, rather than investment to profit ratio, is the measure of enterprise success, incentive for technological upgrading will depend only on riders attached to credit access and possibly favourable rates of taxation for those abiding by this Party/state priority. Moreover, the advice to employ managers who have the greatest expertise in market relations is difficult to implement. It is more complicated than it would first appear. It is not only a matter of selecting enterprise managers from those considered to be the most market aware and so the most 'efficient'. The managers of China's state-owned enterprises have honed their negotiating skills in the context of their soft budget constraint and, as I have argued, this has proven to be the most effective way for them to satisfy their interest in managing their ever larger and more prestigious enterprise kingdoms. They have gained power and status through this economic behaviour. Obviously, it would be difficult to enforce a requirement that managers neglect the connections that they have fostered and invested in over time. Even when shareholders or government bodies appoint managers to state corporations and enterprises, it will be difficult to replace enterprise managers who have power, status and connections with managers whose stock in trade is primarily market skills. At a bare minimum, their market skills would need to show that at the present stage in China's reform process, they generated more advantage for property owners than the finely honed negotiating skills that managers have used to date.[13]

The cautious reformers also advocate that state assets be restructured using mergers, joint operations, bankruptcy and auction and that competitive ability in the market must now be imposed as a criterion of enterprise efficiency. Those who support ownership reform even while recommending caution, recognise that to date, market based competition has been ‘inadequate’. What they see as ‘the malpractice of monopoly’ (for example, the monopoly exercised by the Second Automobile/Dongfeng group when they use the sale of their product or their shares, sometimes on particularly favourable terms, as a means of ensuring loyalty that will translate into the supply of scarce or better quality production resources) has been promoted, rather than extinguished, by the introduction of the lateral economic ties that are necessary for the development of a market integrated economy.[14]

The approach of those who recommend restructuring the ownership of China’s state enterprises, but who counsel caution, has been to produce a reformer’s wish list. Matters such as the need to promote technical improvement and enterprise management techniques, the need to develop market competition and overcome the monopolistic behaviour practised by managers of state-owned enterprises, indeed, the need to overcome all the economic problems that are plaguing the state-owned enterprises, is agreed by all the parties to China’s reform process. The public debate on the issue of ownership reform is then not aimed at promoting agreement among the leadership élite. Rather, it provides a vehicle for discussing the way in which these enterprise problems might be solved and it offers a legitimate avenue for the expression of concerns over a particular policy innovation. These concerns may well influence the speed at which the present push to restructure the ownership of the state enterprises is implemented. Moreover, open discussion centring on the issue of ownership reform does well to continue the practice of eliminating the element of surprise from policy choices. It is therefore instrumental in building up a constituency who will become used to the idea of ownership reform and so is more likely to accept the theoretical re-thinking and the economic, social and political side-effects of the policy. Another consequence of policy surprises is an unwanted nourishment of the belief that a particular economic environment is not a good risk for foreign investors. Obviously, this should also be avoided.[15]

Useful suggestions

I think that a particularly useful example of the public debate that has surrounded ownership reform is provided by a discussion cited in the last chapter. It was suggested that outstanding state enterprise loans be converted into government investment. The funds extended by the state for the purpose of debt clearance would then be considered to be state capital. This would be a ‘one-off’ approach that would be accompanied by a thorough auditing procedure that would find and estimate the extent of any hidden debt carried by the enterprise. Debts owed to other sources could then also be converted into shares. Another suggested approach was that banks could pay out the debt owed them by state-owned enterprises and in return be issued with shares to the value of monies owed. These arguments also note the need for the state enterprises to shed their 'welfare burdens' and their 'excessively heavy social responsibilities'. It is recognised that once shareholding, including shareholding predicated on exchange for debt, is put in place, 'too much' capital must not be tied up in non-productive investment and obligations, otherwise there will be an unacceptably low return on equity. It is also worth pointing out that in this context once share issues had installed share-owners who would appoint enterprise managers, these managers would be expected to mimic the behaviour of managers of enterprises listed on capitalist stock markets where share value is predicted on profit return on investment, but as my argument in this book demonstrates, we cannot expect that they will replicate either the interests or the economic behaviour of the capitalist company manager. The obvious question then is whether or not the legal sanctions that Ma Hong has suggested in tandem with shareholder appointment of enterprise managers would be sufficient to hold managers solely responsible for profit and loss calculated on ratio of profit to investment.[16]

Leaving aside the important question of whether legal sanctions would be sufficient to discipline enterprise manager decision-making, an example of the need for state rules and regulations is demonstrated in advice given to the newly constituted, or more correctly, the potential Chinese stock-holding audience that state enterprise ownership reform will establish. It is advised that the state should ensure that a set percentage of the funds raised through share issues be used 'to replenish working capital' and to 'repay part of bank loans' and other debts. It is then noted that this is important, because 'it has now been verified that most of the funds raised by joint-stock enterprises through selling shares are spent on fixed assets'. Enterprise managers have not considered changing either their priorities or their fund allocations. They do not consider reducing their debt loading because 'they hold that bank loans in hand are advantageous'. A reduction in debt would increase the dividends returned to shareholders, but only if debts owing were a part of profit calculation. They must not be hidden and the idea that debts, particularly bank loans and taxation commitments, need not be paid must be overcome. An added advantage of state regulation of debt repayment from monies raised through stock issue would be that pressure on inflation would ease.[17]

RESTRUCTURING THE OWNERSHIP PROFILE OF STATE ENTERPRISES

Past and present enterprise reform and the need to liberate one's thought

A programme for the reform of the ownership structure of China's state enterprises had begun well before the announcement ratifying its adoption had been issued by the Fifteenth Party Congress. Some commentators argue that it was initiated at the beginning of the 1980s with the introduction of the reform process and others prefer to argue that 'enterprise reform today has some connection with past enterprise reforms but with differences'. Both groups begin by pointing out that until the mid 1980s enterprise reform focused on decentralising decision-making from the state to local agents and that enterprise property restructuring continues to depend on this separation. They then point to the increased use of contracting between the state, local governments and the state enterprises during the second half of the 1980s and the 1988 introduction of the Enterprise Law. The Enterprise Law was expected to be effective in separating the economic and management responsibilities of government from those of enterprise management. It has not. After the 1992 return to progressive reform policy a number of legally binding regulations were added to this law in order to boost its effectiveness. Contracting, laws and regulations were intended to give enterprise managers the right to make decisions over a clearly delineated economic province in a manner not unlike that conveyed by property rights as they are practised in Western market economies, but, as I have pointed out in Chapter 1, these contracts, laws and regulations have not proved to be strong enough to fulfil this charter.[18] In the meantime policy allowing China's state-owned enterprises to issue shares was implemented, though, as I have argued, in the latter 1980s and the first years of the 1990s these shares did not realise their ownership potential. They were primarily an enterprise fund raising mechanism. Though a secondary market in shares was established, it was both 'thin' and informed in a manner other than enterprise profit to investment ratio.

The issuing of enterprise shares, like the introduction of policy that promotes the development of a market for labour time, led to the need to rethink some of the main tenets of Marxism as it had been practised in China. Today too, the enterprise ownership reform that is to be implemented requires 'liberating one's thought and departing from traditional concepts'. Party/state editorials in favour of restructuring the ownership profile of the state enterprises argue that 'we cannot restrict Marxism to what Marx (Engels or Lenin) said. We cannot judge whether something is or is not Marxism simply on the basis of whether the founders of Marxism said it or not'.[19]

The one hundred enterprise trial

The one hundred enterprise trial that has been the official starting point for the current push for ownership reform began with the State Council nominating enterprises located in key economic or geographic places. These were first audited and then they had their assets revalued, their debts assessed and reduced to a manageable level, their 'surplus' workers transferred or dismissed and their welfare functions removed from their administration. They are also to be funded for technological improvement. The enterprises were then converted into shareholding limited liability companies, or in just a few cases, to joint stock holding corporations. Both ownership forms are to be subject to bankruptcy procedures if the economic losses of the enterprise reach the point where they cannot be recouped. Those holding shares would then be liable for the losses in proportion to the scope of their investment. Enterprise managers are to be representatives of capital contributors. The managers will be appointed by the contributors and liable to them and when it comes to state and local government investment players, they will have only shareholder rights and interests. They will *not* function as government administrators. In other words, state and local government entities can be institutional shareholders, but they must not be involved in enterprise administration beyond the rights associated with their status as shareholders. Indeed, it has been argued that a group of shareholders can be used by either enterprise managers or enterprise management committees to help companies avoid direct administrative interference by government departments.[20]

A number of China's state economists have pointed out that the one hundred enterprise trial must be conducted in such a way that the ownership reform policy that it precedes is 'capable of guiding reform in all areas'. After all, compared to the one hundred enterprise trial 'reform is a long-term undertaking'. The trial was scheduled to last only two years from the end of 1994 when most of the enterprises concerned had completed their preparatory planning for inclusion in the 'pioneering project'. The limited liability companies that result from ownership restructuring are to be holding companies that have a relatively large number of shareholders, while in the case of limited joint stock companies only a relatively few investors are listed and this can only happen after there has been a rigorous process of examination and approval.[21]

Party/state sources note that under this latest property reform initiative, shareholding can be operationalised in a number of ways. The most obvious is investment shareholdings. However, there can also be shareholdings based on merger agreements, government shareholding (and where the state continues to have sole ownership of an enterprise it is advised that a state properties management agency should be used), employee shareholding and the conversion of both bank and non-bank creditor rights into share-based equity rights. It has even been suggested that 'creditors' rights can be sold to social intermediary institutions'. These institutions would be in the business of converting creditors' rights into equities.[22]

Enterprises that the government retains

Under state enterprise ownership restructuring it has been advised that those enterprises that are to continue to be wholly owned by government should not be too numerous. The majority of state-owned enterprises should open themselves to 'capital investment from all sources'. The government will retain a majority share in those companies deemed to be 'pillars of the economy'. All other companies should be charged with attracting investment from a variety of institutions, non-official and private investors. Foreign funding is to be welcomed. Indeed, it is argued that 'it will be necessary to continue to attract and utilize capital from abroad and from Hong Kong, Macao and Taiwan',[23] though a number of cautious ownership reformers also counsel that there is a need to prevent the unauthorised expansion of business entities through the use of foreign capital. In other words, foreign capital has been used for fixed asset investment that the Party/state has been keen to limit. It is yet another avenue used by local agents to further their interests outside the discipline that would be exerted by the Party/state. Cautious reformers note that there is a pressing need for the procedures established to govern foreign-funded projects to be observed. They are particularly concerned that the size of international commercial loans be strictly controlled and that monies raised from foreign sources through compensation trade and bonds are also closely monitored.[24]

Working conditions in foreign-funded enterprises and preferential treatment for foreign investors

There has long been resentment over the separate and preferred government treatment afforded foreign-invested companies, particularly when they are solely foreign-funded undertakings. Government policy-makers realise that 'attracting foreign investors is a cut-throat and competitive business' and so while criticising the foreign managers of foreign-funded companies for their treatment of Chinese workers, they have been much less keen to address the workers' employment conditions. The result of a 1994 survey carried out in Guangdong province (a province that has been a mecca for foreign investors) showed that almost half of the workers employed by foreign-funded enterprises in the province usually worked more than eight hours a day and that 'overtime is mandatory', often without extra pay. Almost a third of the workers in the companies surveyed said that they were receiving 'a below minimum wage'.[25] As long as the industrial unrest that I have cited in Chapter 2 is avoided, this obviously reduces the cost of employing Chinese workers and so reduces the production costs borne by the foreign investor.

Foreign investors have also been afforded an array of officially sanctioned preferential treatments. For example, they are given particularly generous taxation breaks. An instance of this policy is that foreign-funded banks who are operating in China must pay only 15 per cent in income tax. Domestic commercial banks (including the Second Automobile/Dongfeng corporation's own bank) must pay 33 per cent in tax on income, while the four leading state-owned banks (the Agricultural Bank, the Construction Bank, the Industrial and Commercial Bank and the Communications Bank) must pay 55 per cent of their income in tax. This is one reason why there has been opposition to the foreign-funded banks engaging in domestic currency (renminbi) transactions. Since 1994, when the taxation system was overhauled, there have been discussions among China's state economists and planners suggesting that the preferential tax categories for foreign-owned enterprises should be abolished. The present push for property reform has renewed that call and we can expect that the varied forms of ownership that will ensue will make it an even more palatable proposal.[26]

Auditing, ownership rights and fairness

A number of those within the Party/state élite who belong to the group that I have dubbed the cautious reformers reacted to the one hundred enterprise ownership trials by warning that while 'building a socialist market economy means establishing a modern enterprise system with corporate property rights' it should be remembered that a modern enterprise system does not mean 'simply share listing, internal [and foreign] fundraising, or changing names from enterprises to corporations'. Above all, it means first preparing state enterprise for reform by imposing a period of rigorous auditing and second that, within the bounds of Party/state regulations, shareholders must be free to exercise ownership rights. They also point out that the debt carried by the state-owned enterprises has usually been a result of past history. They note that these debts should no longer be carried by enterprises that are considered for ownership reform and that other enterprises must then wait for their turn to reform. The managers of these waiting enterprises are then counselled that they should not feel that debt relief extended to reforming enterprises is a result of an unfair policy initiative. They insist that debt relief is not a case of partial treatment by the state. They have even wheeled out the argument that the history of the state-owned enterprises has been harder than that of either township or foreign-funded enterprises and so the social burden borne by state-owned enterprises has been unfair. They single out the Yanzhou Coal Mining Bureau in order to make their point. It is a big mining enterprise directly employing 65,000 staff and having responsibility for 18,000 workers in collective enterprises contracted to it. The cautious reformers point out that 'besides the livelihood and work of staff members, the enterprise must undertake responsibility for their workers' children's education'. This has been unfair because township and foreign-funded enterprises are not responsible for the provision of these services. What is missing from this argument is the situation that I have canvassed in Chapter 1. When large enterprise groups such as the Yanzhou Coal Mining Bureau or the Second Automobile/Dongfeng corporation have been faced with periods of economic contraction (particularly during the especially harsh 1989–92 period of economic rectification) they have chosen not to honour their production contracts with township and village enterprises. The latter do have a hard budget constraint and during periods of economic contraction their numbers have been significantly reduced. I am therefore not at all sure why their situation should be considered to be fair when compared with what I and others would judge to be the protected and relatively advantaged economic history of the state-owned enterprises.

Slow progress, political expediency and many more trial enterprises

At the beginning of 1996 it was announced that the pilot one hundred enterprise programme had been progressing rather slowly and this resulted in a new late 1997 deadline for the end of this programme. This is a full year later than originally intended. On hearing this Hong Kong newspaper editors were quick to seize on the rather churlish argument that this 'is symptomatic of that constant in [mainland] Chinese affairs: economic reform being sacrificed on the altar of political expediency'.[27]

In spite of the attention that was drawn to the one hundred enterprise programme there were many more state enterprises involved in trialling ownership reform. Aside from the one hundred enterprises ratified by the State Council, other enterprises and corporations considered to be suitable for ownership trials were selected by the State Council and state ministries responsible for enterprises and provincial and municipal (city) governments were permitted to 'each select a few pilot [enterprise based reform] projects'. These were all required to adhere to the Corporation Law that took effect on 1 July 1994 and its attendant regulations. Apart from the one hundred enterprises, the State Council chose a further fifty-five corporations to take part in the reform and eighteen governments of so-called 'pivot' cities were also involved. Under the Corporation Law the trial enterprises are no longer required to have a parental government body. It was thought that this initiative would overcome the ongoing 'mother-in-law' problem. This is where separation between government administrations and enterprise management is not practised and enterprise managers liken the administrative interference that they experience to the meddling of a mother-in-law. Today, administrative and paternalistic overview and attendant interference in enterprise management is to be replaced by property rights that are to make enterprise managers beholden to shareholders. The latter are to 'enjoy rights and interests in proportion to the amount of capital they have invested'. This is the policy that has been ratified by the Fifteenth Party Congress.[28]

Revisiting the question of workers' shares and the problem of worker redundancies

The allocation of shares is often to state enterprise workers. However, in spite of the profits that shareholding has offered to some, state workers seem no keener to own these shares today than they did in the late 1980s when they were required to purchase shares as a means of augmenting enterprise funds. They complain that allocating shares to workers and/or 'letting employees purchase stock is asking them to share enterprise losses with the State'. Not surprisingly this is particularly the case when the managers of state-owned enterprises that are considered to be inefficient contemplate this avenue of stock issue.[29] As the workers' concern suggests, it is intended that investors in reformed state enterprises will enjoy financial benefit and conversely if the enterprise is forced to declare bankruptcy after sustaining long-term losses, they will assume limited liability for enterprise debt. It is expected that investors will participate in enterprise policy decision-making even to the point of taking part in the selection of enterprise managers. At the other end of the story the problematic connection between ownership reform and worker redundancies is clearly recognised. Like the provision of welfare services for workers and any number of other issues such as the irrational structure of prices, the employment of workers deemed to be 'surplus' to requirements is presented as a problem bequeathed to current reform initiatives by the former centralised administration. There is some truth in this claim. It is argued that 'the former policy of "full employment" has been the major cause of redundancies' and that it is worker redundancies, or more correctly, the lack of them, that presents a major hindrance to the profitability of state-owned enterprises. Problems such as the debt burdens of the enterprises, hidden losses and credit sales (that usually involve either delayed payments that add to the debt-chains or barter for production needs) are also to be recognised as 'lingering historical problems', though these are not strictly problems left over from the pre-reform centralised administration of China's economy. These are problems promoted by the post-reform periods of economic contraction that have been used to 'cool' the rate of investment and inflation.[30]

A modern enterprise system

In most discussions of property reform initiated by Chinese state planners and economists it is claimed that the present restructuring of ownership rights will push China's state enterprises forward to the point where they are a part of 'a modern enterprise system'. As my discussion above indicates, this view is nurtured by the vision of enterprises funded by shareholders, divested of both their 'surplus' workers and their welfare responsibilities and faced with the disciplining effect of bankruptcy when sustained losses have been incurred. Ownership restructuring is then presented as an 'opportunity' that industrial enterprises must grasp if they are to be a part of this brave new world. The problem is obvious. From a political and even from an economic point of view, the dismissal of a large number of surplus workers from China's industrial enterprises must be a slow, regulated process. I cannot see how it can be solely at the discretion of the managers of the state enterprises concerned. As in the case of the labour reforms that have already been implemented, 'a certain degree of shock [will be felt] in society', and, as I have argued, this shock will need to be tempered by a Party/state élite who will need to be careful when considering the speed at which this reform will be implemented.[31]

An urgent need for new sources of urban employment

In Chinese Party/state sources there continues to be a great deal of discussion of how best to 'appropriately rearrange redundant employees' and there is a recognised need to 'mobilize the resources of government' in an attempt to manage this issue. Apart from fostering the establishment of employment service companies, suggestions have included adopting measures ranging from government encouragement of the tertiary sector to pressing workers who have been deemed to be surplus in one enterprise to seek jobs in other enterprises and other areas.[32]

An International Labour Organisation (ILO) survey conducted at the end of 1995 found that more than half of the state-owned enterprises that they surveyed reported that they had 'on-leave' surplus labour. As I have noted, these are workers who continue to belong to the enterprise, but who are not active in the work-force. There are various estimates of the number of China's 'in-job unemployed'. In the first months of 1995, the director of the Employment Department of the Ministry of Labour estimated that there were around twelve million concealed unemployed workers within the ranks of China's state enterprise work-force. A range of other estimates suggest the figures that I have used earlier in this text. They argue that 'roughly 160 million, or 30 per cent and in some estimates even more, of China's current work force, is "stealthily unemployed" or underemployed'.

A large number of China's openly unemployed are rural workers who are unable to access wage-paying jobs, but in the urban sector the large state-owned enterprises have been the largest contributors to urban industrial jobs and, at the same time, the largest contributors to urban unemployment. And now, these enterprises are 'going to contribute less [and less] jobs'. Again, the argument comes back to the need to promote the tertiary sector of the economy. Medium and small enterprises are to be seen as the most likely avenue for soaking up unemployed former state workers, but they are unlikely to be able to absorb the urban unemployment that would result from the current enterprise ownership initiative. Under this enterprise ownership restructure 'China's current large surplus work force is most likely to join the ranks of the [officially] unemployed'.[33]

The cohort of 'stealthily unemployed' who continue to be the responsibility of China's state-owned enterprises must obviously slow the unburdening that is to precede the process whereby enterprises become shareholding or joint stock companies. Indeed, it seems to me that at the moment the only way that ownership restructuring and a socially acceptable rate of urban unemployment can be managed is by carving off sections of existing state-owned enterprises or corporations and making these sections into shareholding or joint stock companies, but the problem with this scenario is that if it continues to be practised for too long, there will be an enterprise rump that would be left behind in the ownership restructuring stakes. It would be required to function as a holding structure for both surplus workers and those sections of enterprises or corporations that are less appetising to prospective shareholders than others, possibly due to a lack of past status, the type of manufacture, the technological level of factory machinery or even the relatively high level of uncleared debt.

Divesting the state-owned enterprises of their welfare responsibilities is seen as an avenue that can be used for soaking up surplus urban workers. What are now being called 'community service industries' are presented as 'a new growth point in China's tertiary industry'. In other words, not only will divesting state enterprises of their welfare responsibilities make them more attractive to shareholding investors (and more easily made bankrupt in the case of long-term losses), it will also provide an avenue for much-needed urban employment. The argument is that once the provision of social services has been separated from the state enterprises it can be handed over to the communities where the state enterprise is located. This is to be done by 'compensated transfer forms such as leasing or auctioning'. The argument is that private capital must be encouraged in community service industries.[34] From the point of view of China's urban industrial workers, welfare reform has brought them unemployment benefits and unemployment agencies and it is in the process of providing alternate avenues for healthcare and insurance, age pensions and alternative means of meeting their housing, educational and even their entertainment needs. However, there are concerns in some quarters over the 'confusion' that currently exists in providing for workers' social security needs. Provisions are also fragmented leading to a call for far greater standardisation of these urban provisions, and if you are among the ranks of China's urban unemployed I think that you should be particularly worried. Even at this early and relatively protected (though at times confused, fragmented and non-standardised) stage in the process of social security reform, unemployment benefits last only for a limited period. Payments usually last for two years, with reduced payments in the second year (in rural areas they are all but non-existent). By divesting the state-owned enterprises and government bureaucracies of their direct responsibilities first for worker housing and then for other social services, Party/state leaders also expect to be free from their direct responsibility for worker welfare services and payments. In other words, at least in theory, after the process of ownership reform has been completed, central government sponsored bank loans and direct subsidies will not be forthcoming on the basis of workers' welfare needs. As market integration of the economy proceeds, responsibility for workers' welfare will no longer rest with the state enterprises and beyond that with those who represent the Party/state. It will ultimately rest with the worker who must ensure that he (or she) has adequately attended to his own insurance and welfare needs.[35]

The surplus of urban workers in China's industrial centres lies like a social and political time-bomb under the current ownership reform initiative and this is why Party/state authorities decided that in 1996 the rate of urban unemployment must not exceed 3 per cent. (Rural unemployment far exceeds this figure.) One group among those advising caution with respect to ownership reform are even advising that, given China's abundant labour resource, a solution to the 'jobs problem' must be seen as a prerequisite for the formulation of socio-economic development strategy.[36]

A sensitive brief

Today, Chen Qingtai is the person in charge of enterprise reform for the State Economic and Trade Commission and so is effectively in charge of implementing the socially and politically sensitive brief of restructuring the ownership of China's state enterprises. He is a former leader of the Second Automobile/Dongfeng corporation. Indeed, he is one of several Second Automobile/Dongfeng corporation leaders who have attained high office in Beijing. He is one of the early leaders of the Second Automobile/Dongfeng conglomerate credited with the formation of the corporation using the previously established Second Automobile works as its base. The operation of the corporation was presented as a model to be followed by other enterprise groups. Today, Chen Qingtai's brief is described by using the rather wide phrasing of forming 'strategic targets for enterprise reform between now and the turn of the century' by promoting the establishment of 'the framework and operational mechanisms of a modern enterprise system suited to the socialist market economic structure'. This has included launching the trial projects that I have discussed above and, in time, is to include providing all China's industrial enterprises 'with operational mechanisms approximating those of their counterparts abroad'.[37]

OWNERSHIP RESTRUCTURING AT THE SECOND AUTOMOBILE/DONGFENG CORPORATION

The dumber they are the more they must pay

State sources proudly claim that the Second Automobile/Dongfeng corporation is now in the process of being converted into a joint stock conglomerate, while managers of the corporation argue that the latest Party/state initiative to restructure their enterprise property relations is just one further step in a process that is already well underway. They point out that the corporation has already been obliged to ensure that its cap, soft-drink and other miscellaneous 'wing' factories operate using a system of separate accounting. As I have noted, the corporation's shops, food-halls, entertainment venues, guest-houses, zoo and parks and even its sports stadium and piggery are also required to function as separate accounting entities. The middle-schools that the enterprise has provided for the children of its workers must now charge fees leading an old friend who is a retired teacher to complain 'the dumber they are the more they must pay'. Another friend who is a parent was concerned about the volume of homework that her son had to do each night. She argued that this was because the teacher's bonus depended on how well the students in the class performed in school examinations. I am not sure that the dumber the child the more that has to be paid thesis is accurate in terms of what is happening, but like the concern over the amount of homework to be done by school students, it is a reflection of some the unhappiness expressed by the corporation's workers in the face of the ongoing process of enterprise property reform.[38]

Compromise and ongoing obligations

As I have argued in Chapter 2, the managers of the Second Automobile/Dongfeng corporation have also been obliged to undertake housing reform and this led to the corporation's managers being caught between the demands of government and those of their workers. They compromised. They subsidised the wages of those who had 'bought' housing while disposing of the corporation's housing stock in a manner that qualifies for a sale, but where the quality of housing continues to depend on the status of the worker and where the purchase price of the housing is subsidised to the point that it must be returned to the corporation when the worker leaves the corporation's employ. Though I understand that retrenched workers have not yet been required to leave their housing apartments, in this context the potential to be both unemployed and without a home is obvious. And, there are other problems. For example, retired workers keep their homes as a part of the obligation that the corporation has to them, but when sections of the Second Automobile/Dongfeng corporation have been carved off and made into separate accounting entities they have taken current workers without having to take over a corresponding responsibility for retired workers. In other words, they have taken workers who are currently productive and have not at the same time been responsible for providing for past workers. Moreover, because those who have 'bought' their housing requirements from the Second Automobile/Dongfeng group can have their apartments inherited by their children, there is an ongoing and almost open-ended need for the corporation to subsidise housing requirements. Surely this is an uncomfortable fit with the state edict that all state enterprises must now divest themselves of their housing and welfare 'burdens'.[39]

Separate accounting entities

The managers of the Second Automobile/Dongfeng corporation have already formed groups of their enterprises into separate accounting companies. There are the 'wing' factories such as the cap and soft-drink factories that I have already discussed. As I have noted, they, like the schools, the childcare centres, the shops and the corporation's food-halls, must now stand alone as separate accounting and legal entities. And, there are the companies that have been carved from the main automotive manufacturing capacity of the corporation. The enterprises that produce the Citroën sedan account as separate companies as do the enterprises participating in the Second

Automobile/ Dongfeng–Thomson International production of automotive thermostats. This process was made easier for the Second Automobile/ Dongfeng group because the corporation has been operating using an internally decentralised accounting system. It has been doing this since 1984. This system was intended to promote economic responsibility. Each of the branches within the Second Automobile/Dongfeng group have been required to fulfil their planned production quotas and each branch has been charged with accounting for their own funds. An internal bank has been established within the corporation. This mode of organisation means that each branch of the Second Automobile/ Dongfeng corporation banks with the Second Automobile/Dongfeng bank and this internal corporation bank, in turn, holds accounts directly with the People's Bank. Just a few branches and companies of the Second Automobile/Dongfeng corporation then also bank with China's state-owned Industrial and Commercial Bank. The People's Bank provides either funds or a credit note to the Second Automobile/ Dongfeng bank and the latter provides funds to the corporation branches and companies at the same rate of interest as that charged by the People's Bank. The Second Automobile/ Dongfeng bank controls the funds drawn from the People's Bank. It distributes the funds in accord with the proven performance ('efficiency') of the various branches and companies that make up the conglomerate and checks on matters such as the use of technology, technical improvement and on-the-job training for both enterprise managers and workers and the quality of products manufactured. The various corporation branches and companies include both automotive manufacturing entities and those companies that provide services for the corporation's staff and workers.

Branches, companies and restructured property rights

Amounts to be paid in workers' bonuses and into special funds such as the enterprise welfare fund are deducted from each branch of the Second Automobile/Dongfeng corporation and profits calculated. There have, of course, been problems with this form of economic division. For example, very soon after it was established it became clear that the different levels of technology available to different manufacturing branches were influencing their ability to fulfil their internally set production quotas. From the automotive workers' point of view, status is attached to working in those branches or companies that have the most advanced technological equipment. Those branches and companies returning the largest profit (in the case of branches this profit is still calculated on the basis of quantity of product manufactured) would also have the highest bonus payments and the largest welfare funds and so would provide better housing and welfare services for their workers.

From the point of view of restructuring property rights within the corporation the existing branches of the Second Automobile/ Dongfeng corporation formed 'natural' lines of division, particularly when service branches became stand alone companies. However, it is also the case that the companies that have been carved out of the corporation have not always followed these existing lines of separation. Other 'natural' lines of division arose when the Second Automobile/Dongfeng group embarked on projects involving the manufacture of Citroën sedans, Cummins engines, Thomson thermostats and Nissan automotive parts and also when smaller enterprises have been merged into the corporation.[40]

'Purchasing' smaller enterprises

It has been pointed out that when a large enterprise group merges smaller less economically able enterprises the managers of the enterprise group are in effect purchasing the smaller concern at no price. The Second Automobile/Dongfeng group has effected a substantial number of these 'purchases'. Obviously, economists and managers from the corporation prefer to merge enterprises that produce components that are vital to their production needs, but in the 1990s they are also under considerable pressure to merge enterprises that both central and local government agencies have targeted, often because they have administrative responsibility for the enterprise that is to be merged. This is in direct contrast to the situation in the 1980s when local provincial governments were holding on to factories and even continuing to demand taxation from factories that had joined the Second Automobile/Dongfeng group. The benefit gained by the Second Automobile/Dongfeng group from the current round of mergers, even when the supply of semi-finished materials is not an issue, is that it provides an almost painless avenue for expanding the group's productive capacity. Even after almost two decades of reform, this still serves to increase the status of the corporation, though this increased status is now only associated with the assets that will be transferred. It no longer includes the status accrued through an increase in the number of workers to be included in the corporation's kingdom. Today, the Second Automobile/Dongfeng corporation's managers are 'buying' the assets of the enterprise concerned and paying for them by taking responsibility for the work-force of the merged enterprise. However, often, the managers of corporations such as the Second Automobile/ Dongfeng group have been able to negotiate away a proportion of the smaller enterprise's work-force. In other words, they have been able to convince government administrators that the enterprise to be merged has been carrying 'surplus' workers. The latter are faced with unemployment or early retirement schemes and even periods of either minimally paid leave or unpaid leave. Middle-aged and relatively unskilled women in the smaller enterprise's work-force are again the most vulnerable. Minimal and sometimes even unpaid leave allows workers to continue to occupy their housing allocation and to receive medical care and any other available social services that had been provided by their enterprise. These workers are not given access to the services provided by the various branches and companies of the metropolitan Second Automobile/Dongfeng group. They will only have access to the services that have been provided by their cash-strapped enterprise.[41]

Shares and production suppliers, shares in foreign-invested corporations and share listings on foreign exchanges

Yet another form of ownership restructuring that is already well underway, is when large corporations such as the Second Automobile/ Dongfeng group have purchased shares in smaller enterprises that provide production in-puts. As I have argued, in these circumstances the managers of the Second Automobile/Dongfeng corporation have preferred to purchase at least a 50 per cent share in the enterprise concerned and, as in the case of the steel mill shares that they purchased they hope that their stake will either formally, or informally, result in their 'right' to influence the production run of the supplying enterprise.[42] However, this form of share purchase is not the highest, or even the second highest prize in the property reform stakes. The second highest prize is to be in a position to purchase shares in a corporation that has foreign investment. An example would be the Second Automobile/Dongfeng group's 35 per cent share in the Zhengzhou Light Truck plant that I have discussed in Chapters 1 and 3. The highest prize is to be permitted to list shares on an overseas stock exchange. Nine of China's largest state-owned enterprises were listed in the first series of mainland Chinese stocks to be traded on the Hong Kong stock exchange and then twenty-two large state-owned enterprises were listed in a second series. By the end of 1995 nineteen of the enterprises to be listed in both the first and second series were trading on the Hong Kong stock exchange. The Second Automobile/ Dongfeng stocks were in the second series of stocks listed.[43]

CHINA'S SECURITIES MARKETS

Shares, funding and expansion and the increasing importance of financial markets

To date, China's listed companies have felt free to use dividend shares to increase their capital. Dividend shares convert retained profit to stock that is distributed to investors on a proportional basis. Distribution is usually at a price lower than market price. The advantage for the share listing company or corporation is that funding is increased and once again expansion in productive capacity can proceed. This sets the scene for the use of new assets as the basis for the issue of further shares. The increased shareholdings of the investor are then to be listed as profit and subject to taxation.[44] It is then not surprising that Chinese state economists are arguing that while China has had markets for debt and equity for some time now, people do not either understand or use these markets correctly. The economists argue that there is a need to effect a change in the way that China's investors, particularly institutional investors, understand the role of securities generally (both shares and corporate bonds) and particularly the way that they understand the functioning of securities markets. The economists argue that the investors should begin by understanding that even though 'the stock market is something new for many comrades . . . many problems will crop up in the development of stock markets' and as monetisation and marketisation increase the role of financial markets will become increasingly important.[45]

With the banking system not yet committed for further development, the stock markets are the only formal markets for capital. Yet, wisely, Chinese economists are warning that the developing role of China's securities market should not be exaggerated. After all, at this stage in China's reform 'direct capital-gathering cannot supersede indirect capital-gathering'. It will 'not become society's dominant capital-gathering structure'. That role is to be left to the banking system. We are then left to note that at times 'indirect capital-gathering' has been very indirect. Enterprises issuing shares and enterprises and various government entities issuing bonds have gone about 'capital-gathering' in a number of ways.[46]

Exaggerating the effect of a securities market

An exaggeration of the effect that a securities market has in China seems to have occurred equally among those who disapprove of enterprise ownership reform and the current accelerated development of China's stock markets and among those who do approve of both ownership reform and the further development of the stock market. The latter group (those who do approve these current policy initiatives) argue that 'by setting up stock markets, we can improve fund-use efficiency'. They go on to argue that the further development of stock offerings should take place and that market listing capacity must be 'maximised'. However, they are seen to be guilty of exaggerating the role that can be played by China's securities market, at least in the near future. The other group (those who do not approve of further and faster development of China's securities market) counsel that the market will be subject to volatility and therefore will require direct government intervention. They argue that 'if the government fails to intervene, things will be terrible' and they suggest that the whole of the Chinese economy would be badly affected.[47] They are also wrong, because the direct government intervention in China's developing stock markets that they argue is essential, would ensure that market discipline is compromised.

Shares, money and stock markets

By the end of 1995 there were just over three hundred publicly listed companies on China's first level Shenzhen and Shanghai stock markets. Some two hundred billion yuan had been raised on the domestic A market, while an estimated $US6 billion of funding had been raised on the domestic B market. The latter is the category of shares in China's domestic holdings that is available for purchase by overseas investors. For the purposes of this calculation Hong Kong, Taiwan and Macao are counted in the overseas category. (Shares that are called H stocks are mainland China listings on the Hong Kong stock exchange.)[48]

Many observers, Western and Japanese economists among them, argue that China is not yet ready for a fully fledged stock market. They view China's prescribed banking system and relative lack of standardisation in terms of stock issue askance and go on to argue that 'China is not equipped to establish a stock market before the end of the 20th century'.[49] For their part, Chinese state planners and economists point out that not only do fully developed market economies require both a market for capital facilitated by an independent and profit oriented banking system, they also require securities markets, including fully fledged stock markets. Moreover, China's developing and 'multilevel' securities market 'has [already] raised a huge amount of capital' and this capital has been most important in terms of running and developing state-owned enterprises. Monies raised via the issue of bonds and shares are championed because they have gone a long way toward overcoming the heavy reliance that enterprises have had on the banking system. After all, the capital to debt ratio of China's state-owned enterprises has been over 80 per cent.

Can shares be an antidote for over-expenditure?

Chinese state economists have also noted that 'the state has long emphasized control of our investment scale year after year, [but] such control has never worked'. They then present the wide-scale use of share-based investment as an antidote to the centre's recurrent need to effect 'monetary tightening', though at this point in their argument it is worth pointing out that to date share issues have been used by state-owned enterprise managers as a means of off-setting Party/state tightening of the economy. As I have argued and as Chinese economists often note, share issue lies outside the direct monetary and administrative control of the centralised banking system. The Second Automobile/Dongfeng corporation and many others like it, have used share issues as a means of raising funds away from the direct purview of government monitored administrations, but the argument currently put forward by China's state economists in respect to the current ownership reform initiatives is that because 'investors [now] have to consider their stock options', they will be interested in production efficiency, the health of the market for the product manufactured and the business reputation of the enterprise or corporation that they are considering as an investment proposition. The opposite side of this coin is that enterprises that are considered to be inefficient with unmarketable products and a poor image will find it hard to find investors willing to purchase shares. This would leave them without capital, unable to operate and 'with no prospects'. The problem with this analysis is that it would need to be predicated on the debt burdens, welfare responsibilities, surplus workers and any technological backwardness in either machinery, technical skills, administrative expertise and market management having been overcome by the time that the enterprise or corporation issued shares. Nevertheless, in contrast to the manner in which state enterprise managers have previously viewed securities (both bonds and shares) the nexus between fund raising and ownership reform is now firmly in place as is the nexus between shareholding and property rights. As I note above, the latter include the right to buy and sell shares and enjoy dividends and the right to choose enterprise leaders. The catalogue of property rights is then to be combined with far greater standardisation of both share-holder entitlements and enterprise operations and it is claimed that the combination of these measures will bring ‘a qualitative change to China’s ownership relations’.[50]

Shaping China’s securities markets

By the beginning of 1995 a draft securities law had been made available. This law was intended to shape China’s multi-level securities markets. Legally registered company stocks would be listed for trading on securities exchanges. Now, securities companies would be allowed to operate only by facilitating ‘securities brokerages, consignment business, the sale of securities, the buying and selling of bonds, the storage and registration of securities and the sale on commission of those government bonds that the State Council designates as for sale on commission’. For their part, investors would be obliged to open securities trading accounts with securities companies or to entrust a securities company to open an account for them. While the securities companies themselves would be obliged to temporarily close trading if ‘a sudden occurrence’ was experienced.[51]

Those stocks that are ‘non-market company transferable stocks’ will not be listed on the more formal (first level) securities exchanges. They will be listed on exchanges described as ‘legally established non-centralised competitive price exchanges’ which are seen as second level securities markets. The draft securities law outlined a plan to regulate and standardise the business of these less formal exchanges and to develop them further. Unlike the major or first level securities exchanges, these exchanges do not have a brokerage system. Transactions are made at the counter, usually at negotiated prices. This is deemed to be a more regulated approach to the local exchanges that began operating in 1991 and it is an attempt to avoid the ‘rampant speculation’ that has taken place in the past. There are also plans to strengthen the laws governing securities exchange and to introduce arbitration procedures in order to mediate ‘the ever-increasing securities disputes’. The draft law also carries strict rules in relation to insider trading. People are also to be prohibited ‘from fabricating and disseminating rumours or false information’.[52]

Educating the public

The need to educate people in what is required by market exchange of securities is a recurrent theme in Chinese discussions of both the changing ownership structure of the state industrial enterprises and the further development of securities exchange. Arguments begin by noting that 'general knowledge and a strong concept of a modern market economy is very important' and then they reiterate this point a number of times in the course of their wider discussion. Those dealing in stocks are warned that they must recognise that in the stock market the law of demand and supply dominates. Moreover, the Chinese market has shown indications of being a weak market. The indicators of a weak market are given as one where shares traded are below what is considered to be their normal price and the volume level of shares traded is depressed for a sustained period of time. Indeed trading may become all but inactive. An added problem is the 'rampant speculation' that has been evident on China's stock markets. This is argued to have resulted in market instability. Sharp rises have been followed by sharp falls and it is believed that without sufficient funds to boost the market when 'this kind of sharp fall' is experienced further market weakness will result.[53]

Investor confidence

Drawing on a study that they conducted in 1994, state economists have noted that at times both China's primary domestic stock markets were trading at a lower level than would be expected. They claimed that the Shanghai market should be around seven to eight hundred points and the Shenzhen market around two hundred and twenty to two hundred and fifty points. In July 1994 the Shanghai market index dropped to around four hundred and twenty points, while the Shenzhen market index was at the low ebb of one hundred and ten points. The volume of transactions on both markets dwindled. The economists also warned that the question of whether a market is normal or weak cannot be answered simply by examining share prices. After all, some enterprises may have set the price of their shares too high at the point of issue. It seems that some premiums were set 'so out of line' that they were bound to fall on the primary stock markets and they 'put pressure on the secondary market'. Prices, even in the secondary market, then fall below the price set when the shares were issued. In this case the market concerned is not weak, though obviously, any drop in expected share prices has a bad effect on investors. In short, 'their confidence is badly shaken'.[54]

Bank commercialisation

Another area where it is claimed that there is a pressing need for investor and even general public education in relation to stock market development is in the area of bank commercialisation. It is argued that because there is little public understanding, 'the objectives of bank reform through commercialization remain fuzzy'. The public, it is argued, must recognise that a 'modern joint stock system for a commercial bank is coupled to a market economy'. It must serve as the goal for China's banks. Because the 'banks do not practice the shareholding system, responsibilities, rights and profits bear no relationship to one another . . . [and this] has a disruptive effect on the entire economy and society'. Shareholding is to be seen as the only way to effect a measure of financial autonomy and control over personnel in China's banks. However, it is argued that it would not be advisable to adopt it immediately. Among the plethora of problems impeding this avenue of reform, pricing continues to be irrational and so it is currently impossible to put the right price on the assets held by the state-owned specialised and commercial banks and above all, the People's Bank 'is incapable of deploying economic tools to control the total money supply, total credit, and the direction of investment'. After all, 'there is still an acute desire for investment on the part of production enterprises'.[55]

The continuing need to effect macro-economic control

I doubt that the Chinese public's failure to understand the eventual need for China to have commercial shareholding banks operating in accord with market indices is currently impeding banking reform. It is clear that the reason that a capital market facilitated by the banking system has not yet been introduced has much more to do with the reasons listed above. As I have been arguing, it is because the People's Bank would be unable to affect macro-economic control in the current micro-economic climate and because unwanted political consequences must be expected if the Party/state is unable to control the interests of local agents who continue to display 'an acute desire for investment'. On the other hand, investors' lack of understanding in relation to share markets may well impede the process of restructuring the ownership profile of China's state enterprises. All investors and potential investors need to understand that enterprises that they invest in may effect losses and that stock market trading can be weak. They must be made aware that shares will differ from bonds. Monies that have been invested can be lost. They also must expect to be able to conduct share transactions in the context of standardised and impersonal rules and regulations. If reform is to be advanced and a 'real' capital market established in the province of 'direct capital-gathering' effected by stock market exchange (rather than the 'indirect capital gathering' undertaken by the banking system), the shares that are to be issued by enterprises that have been subject to ownership restructuring must not be subject to negotiation and manipulation. Moreover, when prices on stock markets plunge, investors, including institutional investors, must not expect that government 'rescue' will be at hand.

CONCLUSION

Restructuring the ownership profile of China's state enterprises will realise its potential to press the process of reform forward and so will keep the leadership élite's reform credentials intact. In other words, it will buttress their ability to continue to promote the process of modernisation: a concept that is often reduced to the continued healthy rate of industrial growth and an ever-increasing level of consumption for China's urban workers. However, it will also result in 'a certain degree of shock in society' and obviously this will need to be tempered by a Party/state élite who will need to be careful when considering the speed at which the ownership restructuring of China's most important industrial sector is implemented. On the other hand, as I have argued, appearing to be either tentative or pusillanimous would not advance their cause. It would be disastrous.

China's Party élite do recognise that the restructuring of state enterprise ownership must not exceed the people's tolerance. They know that it must not proceed to the point where the authority of their rule is undermined. Ownership reform means a loss of jobs, privilege and income and so as Kornai has argued and as the Chinese leadership has recognised, an aggressive approach to this reform must be avoided. Not surprisingly, this politically and economically ill-advised method has been spurned, but the question of the timing and extent of the people's tolerance toward the fall-out from ownership reform remains. It is coupled with the need to build a constituency for ownership reform outside progressive members of the Party/state élite. This wider public constituency must be willing to accept the considerable changes that restructuring the ownership of state enterprises will bring.[56]

China's Party/state leaders also recognise that they must successfully manage the opposition of interests that reform has promoted between themselves and local agents and this is why they have been most willing to believe that 'the only way to break out of the imbroglio of price, wage, capital investment, and tax reforms is to change the ownership of state industry'. Moreover, the Central and Eastern European experience has suggested that 'ideological resistance to ownership reform under socialism may not be insuperable',[57] and some commentators go as far as arguing that the conversion of China's state-owned enterprises into limited liability shareholding companies and joint stock corporations may well deflect blame away from those who represent the Party/state and particularly from the Party leadership élite. Either enterprise shareholders or the managers that they appoint would be the targets of blame. Whether or not this is a likely outcome of ownership restructuring, Kornai's advice to avoid 'ownership reform by a cavalry attack' must be heeded by a leadership who are, above all, interested in maintaining their authoritative rule. The argument of those among the ranks of China's cautious reformers who advise that a solution to both the micro-economic chaos that reigns over the accounts of the state-owned enterprises and the 'jobs problem' is a prerequisite for the formulation of any socio-economic development strategy cannot be ignored. Their caution is well placed.

Conclusion

> Little direct evidence is available on the transition from a central planned communist regime to a . . . market-oriented regime. The clarity that does exist relates to the end points of the transitional process. . . . Unfortunately the ideal path from 'here' to 'there' is less obvious.[1]

The political authority of the China's Party/state élite is built on both old and new foundations. They continue to claim that China is in 'the primary stage of socialism' and that during this stage the people are not sufficiently aware of their 'real' needs and interests and so they, the Party leaders, must fulfil a paternal role. They must act on behalf of the people. In this context their political authority continues to be based on a platform of superior knowledge that masquerades as Marxism-Leninism adapted to China's needs. Yet, the post-reform relationship between the Party/state élite and the Chinese people increasingly resembles that of a leadership who must accommodate the subjectively expressed expectations of their political constituency. And, even if we leave aside the considerable tension between the paternalism of a leadership élite who present themselves as the guardians and diviners of the interests of the Chinese people and their growing need to satisfy the subjectively determined interests of an increasingly confident constituency, there are further problems.

The expectations of China's urban residents are also both old and new and they are often contradictory. Local government administrators, the managers of China's state-owned enterprises and China's industrial workers all value the opportunities that the process of reform has delivered. They have come to expect the increased level of bargaining, negotiation and individual decision-making that reform has promoted and they have grown used to an ever-increasing level of consumption and improved living standards. The latter was the original promise of Deng Xiaoping's reforms. Yet, at the same time, the members of each of these groups continue to value the positions and security that China's centralised pre-reform administration had afforded them.

ENTERPRISE WORKERS: INCREASED CONSUMPTION AND GREATER UNCERTAINTY

The process of reform initiated by the Deng Xiaoping leadership has certainly increased the level of consumption enjoyed by urban industrial workers. Friends that I visit who work for the large and successful Second Automobile/Dongfeng group have microwaves, range hoods over their stoves, showers, central heating, housing units comparable with many that you would find in a suburb of a Western industrial city, and coloured television sets, refrigerators and washing-machines have been a part of a young couple's essential needs for a decade or more. Mobile telephones are popular and now Party/state leaders are dangling the prospect of household car ownership in front of the more affluent of China's workers. The reform process has, as Deng Xiaoping claimed it would, 'met the [consumption] needs of the broad masses', but this consumerism has come at a price. The workers who now enjoy a much higher standard of living and the attendant consumer durables no longer enjoy the cooperative 'familyism' that previously dominated enterprise manager/worker relations. During the 1980s the 'web of interests' that Walder identified (and lamented) continued to reside within China's state-owned enterprises. It provided urban residents with an array of wage payments, relatively well-heeled housing, health, education and a range of other welfare provisions and, as I have argued, it extended even as industrial reform policy was implemented. Indeed, it served to promote the increased living standards enjoyed by urban workers. Enterprise managers used the increased negotiating and bargaining power that reform had afforded them as 'a rich source of illicit funds for use as bonuses' and later for funding increased worker services, improved housing and even gifts. However, by the latter half of the 1980s their concern to care for 'their' workers had come to reside incongruously alongside an ever more clearly delineated opposition of interests between managers and workers. Moreover, it was soon clear that the initial coexistence of a web of factory manager/worker interests and a growing tension between managers' and workers' interests was no more than a temporary phenomenon. The long established manager/worker cooperation (even collusion) which ensured workers' employment security and increasing consumption was first eroded and then eclipsed by the aggressive nature of the developing manager/worker tension. A process was in hand whereby workers' consumer appetites were being sated, but it was at the expense of their cooperative labour relations.[2]

Today, we can see that the introduction of labour contracting to China's state-owned enterprises in 1986 began the erosion of state workers' employment security. It was the first step in both eroding workers' 'right' to life-time tenure of their employment and the development of a market for labour time. At the same time, it paved the way for the current push to divest state-owned enterprises of their welfare responsibilities. The latter has now been firmly attached to the process of ownership restructuring formally ratified by the Fifteenth Party Congress. This reform initiative provides a deadline for the state-owned enterprise managers to divest themselves of both their surplus workers and their welfare responsibilities. Even conservative estimates note that in many of China's large state-owned enterprises surplus personnel account for about 30 per cent of the work-force. At the same time, in some of the older state-owned enterprises surplus workers combined with retired employees are estimated to account for almost 50 per cent of the work-force. Both the surplus workers and the retirees are in receipt of money income and welfare services. The argument is that the clarity of property rights delivered by ownership reform will focus attention on the ratio of investment to profit. After all, there will be clearly identifiable enterprise owners who will benefit from profit earnt, but who will be responsible for losses? In this scenario surplus personnel will be dismissed.[3]

Ownership reform will obviously mean that urban unemployment will increase, largely because those who are now among the hidden or stealthily unemployed will become the openly unemployed. For those workers who stay in the employ of a state-owned enterprise it is intended that their housing will be purchased in the market-place and their welfare needs will now be provided by community based shareholding companies. In time, there will be market distribution of social services. This situation is already apparent in education. Parents are now paying for their children's education, rather than having access to education on the basis of their employment. Walking along a side-street in Guangzhou one winter's morning recently I came across a music school that apparently provided a Yamaha piano for each student. The school was obviously for the children of China's 'new rich'. Enterprise and local government distribution of welfare resources was never equal. Workers of large state-owned enterprises like those that constitute the Second Automobile/Dongfeng corporation have been the aristocracy of China's work-force, but the development of a market for labour time combined with market distribution of social services and welfare provisions will obviously further promote, rather than lessen, distributive inequality. The question then is – will China's urban workers continue to support a leadership that must engage in further reform in the name of promoting the goal of 'a socialist market economy'? Reform must provide the growth rate that will support the increased consumerism that they have come to expect, but it is being implemented at the cost of the employment security and distributive provisions that have long formed the basis of the unwritten, but firmly entrenched, 'social contract' that they have had with their enterprise managers and that they continue to expect to have with their leaders.[4]

ENTERPRISE MANAGERS: SOFT BUDGETS AND OWNERSHIP REFORM

Having decided to forgo, or more correctly to delay, banking reform in the name of macro-economic control and attendant social stability, China's Party/state leaders have presented ownership reform as proof of their ongoing reform credentials and as a panacea for micro-economic chaos. They have promoted it as an answer to the problems of enterprise debts, the slow repayment and enterprise defaults on bank loans, stock-piled goods resulting from extended productive capacity and inappropriate production decisions, failure to meet taxation commitments and high welfare costs and 'surplus' workers. Unlike the situation in the latter half of the 1980s when stock is sues were primarily a means of raising enterprise funds, today share issues are intended to raise enterprise funds while realising their potential for disciplining the economic decision-making of enterprise managers. Indeed, members of the leadership élite have touted ownership reform as a means of managing the opposition of interests between themselves and local agents through the effective imposition of hard budget constraint.

When ownership reform ushers in widespread share-holding and joint stock ownership as a replacement for government ownership of China's state industrial enterprises (the former presented by Party/state administrators as a form of collective ownership by the people and the latter as government ownership on behalf of the people) managers will be accountable to the shareholders who appoint them. It is intended that this investor interest will ensure the hard budget constraint is effected. However, at the point of share issue, the managers' economic decision-making may not undergo the sudden conversion to Westernstyle economic rationalism and the punctilious observance of hard budget constraint that China's Party/state élite are hoping for.

Even as Party/state leaders formally announce their intention to restructure the ownership of the state enterprises they are finding it necessary to draft and adopt rules and regulations that they intend will proscribe the economic decision-making of enterprise managers. For example, once again Party/state administrators are attempting to limit the investment in fixed assets initiated by enterprise managers. Again we are back to the administrative, rather than the market, disciplining of local decision-making. Even with the capital markets promoted by enterprise shareholding, complete with the exhortation that 'comrades' must now learn how stock markets operate, while the banking system remains tied to the Ministry of Finance it is difficult to see that hard budget constraint will be practised. Enterprise managers will continue to negotiate and manipulate policy. After ownership reform the difference will be that they no longer do this, as they did in the 1980s, for their own and their workers' particular advantage. They will do it for their own and their shareholding constituents' particular advantage. And, at the same time, local government administrators will continue to participate in what some have aptly called 'the national scramble'. In other words, they will also continue to negotiate and manipulate centrally set policy in their own interests.[5]

As has been pointed out, 'the key to exercising macro-economic control [even over share issues and the stock markets] lies in appropriate regulation'. This regulation will have to be non-negotiable and must be extended to the point where it is effective in overcoming problems such as enterprise managers using monies raised from stock issues to once again extend the productive capacity of their enterprises, rather than paying debts, including bank loans and taxation commitments. Already, having extended the enterprise asset base, enterprise managers have issued more shares and then used monies provided by the share issue to pay dividends to existing investors. Practices such as this serve to underline the point that even after state enterprises have been converted to shareholding and joint stock companies and are officially beholden to the investors who appoint them, enterprise managers are, as I have argued, unlikely to be willing to give away the bargaining and negotiating power that reform has already bestowed on them. And, there is the question of whether it will be possible to harden the budget constraint of the enterprises without closing the life-line that enterprise managers have used to continually draw on the centralised banking system for circulating and investment funds, even when they are already running in the red. Again, a market for capital facilitated by the banking system is the only convincing solution to this problem, but this would mean that the enterprises would close if they consistently failed to make a profit. They would close even if, as in the case of the enterprises belonging to the Second Automobile/Dongfeng corporation, they had a past history of considerable success, are currently categorised as enterprises hampered by the lack of capital injection and are on the leadership's list of priority industries. Any exceptions would open the door to negotiation and manipulation of policy and so would undermine the hardening of budget constraint. However, without financial help, the shareholders and the dismissed workers of enterprises that were forced to close would be alienated. Both groups continue to see themselves as the subjects of the authoritarian and paternalistic Party/state while, at the same time, they are expressing interests and concerns that reflect their position as constituents of a 'modern' reforming society.

COURTING POLITICAL STABILITY

In order to stay in power, China's Party/state leadership élite must be seen to promote their publicly articulated goal of developing a market integrated economy, but they must at the same time court the political stability and economic order that buttress their rule.

The process of reform requires that economic decision-making be decentralised and yet even after almost two decades of reform, the market discipline necessary for economic decision-making has not matured. It is still unable to discipline the demands of local agents and the leadership élite have decided that they must continue to use the banking system as their most important macro-economic tool. They are now looking to ownership reform as a way forward. The question then is – will restructuring the ownership profile of China's state-owned enterprises impose hard budget constraint on enterprise managers' decision-making? As I have noted, I think that this is unlikely in the absence of banking reform. What is more, ownership reform, like the increased standard of living promoted by reform, comes with a price. It has the potential to promote further disaffection among China's urban work-force.

In the 1990s, it is the opposition of interests between enterprise managers and workers that in its most explicit and aggressive form results in the worker unemployment that, in spite of the rising levels of consumption enjoyed by many urban workers, has the potential to lead to overt social discontent. This is why China's leaders must slow the process of ownership reform while they embark on the difficult task of building a wider constituency for this latest reform initiative. It is not sufficient to find that this reform is accepted within the ranks of the Party/state leadership élite who are now willing to trample the Marxist holy ground of both cooperative labour relations and community ownership. They must remember that today their authority is predicated on both their ersatz Marxist credentials *and* their ability to satisfy the reform fed expectations of their constituents.

Notes

INTRODUCTION

1 Deng Xiaoping *The Selected Works of Deng Xiaoping*, vol. 3, Beijing: Foreign Language Press. Selections reproduced in *Renmin ribao* (5/11/93) and *Xinhua* (9/11/93) and translated into English by *Foreign Broadcast Information Service* (*FBIS*) 18/11/93 and 5/1/94.
2 The Fifteenth Party Congress was convened in September 1997.
3 Janos Kornai argues that,

> expanding your budget means expanding your scope of power. The larger and more technically equipped you become, the more power, the more prestige, and perhaps the more salary you acquire. Now when you aggregate this behaviour and combine it with the soft budget constraint, then you have a society with what I call investment hunger.

He uses his concept of a 'soft budget constraint' to describe the situation where 'a budget does not really bind decision-makers'. Cost overruns are met by a paternalistic state (see Kornai *Contradictions and Dilemmas*, 1986: 33–51).
4 See Andrew Walder, 'Wage Reform and the Web of Factory Interests', 1987 and comment by Yimin Lin, 'Between Government and Labor: Managerial Decision-making in Chinese Industry', 1992: 381–2.
5 For an excellent account of both the possible intention behind Deng Xiaoping's (or his children's) support for the resumption of economic reform and of the tension within China's leadership élite during the months before the Fourteenth Party Congress see Richard Baum, *Burying Mao*, 1994: 341–69.

1 THE NATIONAL INTEREST VERSUS PARTICULAR INTERESTS

1 Gordon White, *Riding the Tiger*, 1993: 129.

2 Some even go as far as interpreting the overtly tense relationship between centre and regions as a symptom of China's political disintegration. However, others have very sensibly argued that the relationship between the Party/state centre and the regions is 'more usefully interpreted in terms of negotiation rather than in terms of any necessary conflict leading to political disintegration' (see David Goodman, 'The Politics of Regionalism', in D. Goodman and G. Segal, *China Deconstructs*, 1994: 4 and 15–16; and David Goodman, 'China in Reform: The View from the Provinces', 1997: 4–6).
3 See Hannan (1995b) 'Reforming China's State Enterprises, 1984–93', *The Journal of Communist Studies and Transition Politics*, 11 (1), March.
4 Interview with Janos Kornai titled 'Hungary's Reform: Halfway to the Market' published in *Challenge*, May–June 1985: 30.
5 In China the cost overrun feature of this form of economic arrangement was first met from funds distributed directly by government, but later in the reform process it was facilitated primarily by negotiated bank refinancing. It is clear in this context that the hard budget constraint of market discipline effected in Western capitalist economies and advocated in the ideology of neo-classical economics is far from being realised.
6 It is then apparent that while the soft budget constraint has been a feature of centrally organised economies (in both the former Soviet Union, the nations of central and eastern Europe and China), it is also a central feature of reforming centralised economies (see Yimin Lin 1992: 382). For a very well informed account of the 'separate kitchens' issue see Shirk, *The Political Logic of Economic Reform in China*, 1993: 171–3. See also Stephen Herschler, 'The 1994 Tax Reforms: The Centre Strikes Back', *China Economic Review*, 6 (2), 1995: 239.
7 K.C. Yeh, 'Macroeconomic Issues in China in the 1990s', *The China Quarterly*, 131, September 1992: 534.
8 See You Ji, 'Dismantling Party/State Controls in China's State Enterprises', unpublished Ph.D. thesis submitted to The Australian National University, September 1993. As Yimin Lin has pointed out, the Factory Director Responsibility system also linked enterprise profitability to the managers' own economic interests. It quickly became clear that 'if the production plan was fulfilled and operations outside the plan were profitable' workers' bonuses would increase accordingly. The managers were, of course, seeking labour cooperation. See Yimin Lin, 1992: 394.
9 When the Enterprise Law was introduced in 1988, its political sponsor, China's then Party General Secretary – Zhao Ziyang, had intended that it would strengthen the Party's leadership role by conserving Party energies for policy decision-making rather than using them on the vagaries of hands-on day to day activities such as those performed by enterprise Party Committees and that it would also promote the separation of enterprise decision-making from government decision-making. In the immediate wake of the 1989 Tiananmen Incident Zhao was discredited and criticised for promoting policy that undermined the role of the Party and the Enterprise Law was apparently diluted. His Party-role recommendations were formally ignored and it was presented as primarily a law that underwrote the separation of enterprise management from government decision-making. It was not until after the 1992 return to

progressive reform policy that the decline that was already taking place in the decision-making role of the enterprise Party committees was acknowledged. As an added matter of interest, Yimin Lin has argued that the demise of the Party committees also served to bring the relationship between management and labour to the fore (Yimin Lin 1993: 397).

10 You Ji, 1993, see also Bei Duoguang, Arden Koontz, Lewis Xiangqian Lu, 'The Emerging Securities Market in the PRC', *China Economic Review*, 3 (2), 1992: 156. Another argument in relation to the behaviour of local administrators notes that as the ideological commitment has waned and as, at the same time, the income position of Party cadres has been somewhat diminished during the process of reform, there has been an increased 'money fetishism'. In other words, there has been an increase in seeking personal gain, rather than in commitment to the reform 'revolution'. This is behaviour that can obviously either promote or undermine the unity of interest between local administrators and enterprise managers and in the latter case it is by no means the only incidence of a tension of interest in this relationship. There are numerous well documented cases of local government administrators using their administrative authority to ensure that taxation revenues and fees are paid and even to extract substantial fees from enterprise management, using dubious pretexts. In terms of taxation and fee payment by enterprise managers to local administrators the enterprise's relationship to the state is mimicked when the same opposition of interests in relation to these payments exists between the state-owned enterprise and local administrative agencies. The same soft budget bargaining and manipulation between the two parties takes place. In the end, we should recognise both the unity of interest that has been promoted between local administrators and state enterprise managers and is manifest in their dealings with the state *and* the difference of interest that is manifest between these two groups when they are obliged to negotiate with each other.

11 See Susan Shirk, *The Political Logic of Economic Reform in China*, 1993: 171.

12 These funds were often used either to further expand enterprise production capacity, or to provide 'extra' compensation for enterprise workers. See Hannan, 'The Left Hand Doesn't Know What the Right Hand Is Doing: Industrial Reform in China', 1995a: 137.

13 By the latter half of the 1980s China's economically advantaged state-owned enterprises were exercising their ability to pay above the government set price for scarce resources; to use their status to bargain for scarce resources and to cultivate reciprocal favours and advantages; to effect a strong and persuasive bargaining position in relation to administrative authorities at all levels, including in terms of the banking system; to provide their own infrastructural resources, i.e., their own power generation plants; and to attract scarce technically trained workers.

14 Dorothy Solinger chooses to use the term 'relational contracting'. She notes that by contrast with impersonal market based contracting, relational contracting is 'non-standardised' and 'recurring'. She approvingly quotes Victor Goldberg's argument that under relational

contracting 'much economic activity takes place within long-term, complex, perhaps multiparty contractual (contract like) relationships . . . [where] behaviour is, in varying degrees, sheltered from market forces'. See Victor Goldberg, 'Relational Exchange: Economics and Complex Contracts', *American Behavioural Scientist*, 23 (3), 1980: 338; and Dorothy Solinger, *China's Transition From Socialism*, 1993: 109.

15 See Kate Hannan (1991) 'Economic Reform and the Fixed Asset Problem', *Access China*, 1, March. Material also drawn from interviews with economists from the Second Automobile/Dongfeng group held in 1988.

16 *Xinhua* 26/8/88, *FBIS* 30/8/88. This quote has also been used by Solinger. She has also argued that raising funds for state enterprises via shareholding was seen as preferable to enterprise mergers and closures, because the latter would upset workers. She quotes the observation made in the Chinese press in 1988 that 'Ideologically, only when we admit that some enterprises will "survive" and others "die" or some enterprises will develop and others perish can we support superior enterprises in "swallowing up" inferior ones'. She then goes on to claim that 'permitting firms with surplus funds to buy into other firms is inherently less threatening to employees than a merger would be'. She argues that share issues would therefore be expected to protect the jobs of staff and workers in the inferior enterprises. See Solinger, 1993: 134–5.

17 Solinger also draws attention to this point. See 1993: 135.

18 Bei *et. al*. 1992: 159.

19 See Solinger 1993: 134.

20 Solinger notes that 'this practice, in effect, serves to reinstate the old management system, despite the fact that the firm is now drawing investment funds from new sources', Solinger 1993: 136.

21 Bei *et al*. have pointed out that China's securities market has gone through at least three identifiable periods: the July 1981 to April 1988 'black market' period when black marketeers were in a position 'to buy treasury notes at deeply discounted prices'; April 1988 to October 1990 when a 'grey market' operated during which the government first allowed a trade in treasury notes and the period in which, in 1985 and 1986, treasury notes were first formally designated as tradable bonds; and, the October 1990 to the present white market period. During the latter stage the secondary share market has been subject to a far greater degree of institutionalisation and uniformity than during the previous two periods (1992: 158–60).

22 See *Zhongguo tongxun she*, Hong Kong published 8/12/92, *FBIS* 10/12/92; see also *Zhengming* no. 179, Hong Kong published September 1992, *FBIS* 1/9/92. It has been estimated that as many as 400,000 people (one-fifth of Shenzhen's population) lined up overnight to participate in a lottery which distributed rights to purchase new shares. This rationing method was greeted with rioting when it was understood that corruption and connections had undermined the rationing process (see Bei *et al*. 1992).

23 The use of share issue by enterprises had been posited and even begun, as early in the reform process as 1982. But it did not become a part of enterprise policy until the financial crisis that loomed in the latter half of the 1980s. By this time government sources were noting that bank savings deposited by individuals had expanded considerably and again, in the early 1990s as the noose of economic rectification/contraction took effect, they

were arguing that ‘after 12 years of reform, the distribution pattern of the national income has changed, and the people’s incomes have increased (the proportion of income received [in money form] by individuals increased from 49.3 percent [of total real wage] in 1978 to 61.3 percent in 1990)’, *Renmin ribao* 23/6/92, *FBIS* 2/7/92. Using 1990 statistics it was estimated that even after some years of stocks being available, compared with the 800 billion yuan in savings deposits only 18.7 billion had been invested in tradable securities (see Bei *et al*. 1992: 151).

24 From interviews with members of the management of the Second Automobile/Dongfeng group held in 1988, 1989, 1991 and 1992.

25 Yimin Lin 1992: 388.

26 See Yimin Lin 1992: 391.

27 The kingdom building practices of enterprise managers would not have been possible without local government assistance and in this context it has been suggested that ‘there are basically two competing categories of explanations’ concerning the question of why local bureaucrats seek to negotiate with state administrators and why they have sought to manipulate central government directives. But both of the categories suggested in relation to the behaviour of local administrators have been predicated on the assumption that local bureaucratic behaviour is informed by the bid to maximise revenue. It is argued that they do this to (i) please their superiors or (ii) to increase their autonomy *vis-à-vis* their superiors. But, I believe that there are other reasons. These are predicated on local administrators’ bids (i) to increase the province of their influence and (ii) to be seen to have been successful in providing for those who reside within their province. In other words, local administrators have protected and promoted their subordinate enterprises even to the point of promoting an opposition of interest between themselves and the Party/state. They have negotiated with state administrations and manipulated central government policy in order to extend and provision their kingdom to the best of their ability. See Huang Yasheng, ‘Web of Interests and Patterns of Behaviour of Chinese Local Economic Bureaucracies and Enterprises during Reforms’, *The China Quarterly*, 123, September 1990: 439–53.

28 Interviews conducted at the Second Automobile/Dongfeng corporation headquarters in Shi-yan in 1985–6 and 1987. See also William Byrd (1992), ‘The Second Motor Vehicle Manufacturing Plant’, in William Byrd (ed.), *Chinese Industrial Firms Under Reform* and see Shirk 1993: 285. Shirk also underlines the observation that the managers of the very large advantaged state-owned enterprises wield considerable ‘political clout’.

29 This was, as would be expected, particularly the case when it came to managers of not just advantaged, but ‘giant’ enterprises such as the Anshan Iron and Steel Company. In 1986 the Second Automobile/ Dongfeng group had been ranked number eight calculated in terms of the output value of China’s top twenty enterprises. The Anshan Iron and Steel Company has for a long time been ranked at number one.

30 See *Renmin ribao* 21/10/91, *FBIS* 7/11/91.

31 In reply to repeated requests from the Second Automobile/Dongfeng managers the State Planning Commission allowed the Second Automobile works a separate line item in the state plan. This meant that the Automobile Corporation was no longer an intermediary in the state/corporation

planning mechanism. Then, in 1986 the works and the Dongfeng corporation were each granted independent status under the state plan.

32 Argument taken from interviews held in 1987, 1988 and early 1996.

33 See *Xinhua*, in English, 2/1/95.

34 See *Xinhua*, in English, 2/1/95 and interviews with managers and economists from the Second Automobile/Dongfeng group. See also Xiaohua Yang, *Globalization of the Automobile Industry*, 1995: 163.

35 I understand that the Second Automobile/Dongfeng corporation–Nissan Company relationship has now reached the point where it is likely to become a joint venture agreement. The managers of the Second Automobile/Dongfeng conglomerate are interested in bus axles because the group manufactures buses at a plant in Huizhou city in Guangdong Province.

36 Material drawn from interviews held in 1985 and 1986. See also Xiaohua Yang, 1995: 138.

37 Prices quoted from notes taken in interviews with Second Automobile/Dongfeng managers in 1988 and 1991. Other comment taken from interviews conducted between 1987 and 1991.

38 In September 1988 a friend at the Second Automobile/Dongfeng corporation invited me to his apartment in order to read the contract that was to be signed by the Second Automobile/Dongfeng management and representatives of the French government. I considered it bad form to Xerox these documents, but the terms and conditions contained in them made very interesting reading.

39 Material drawn from interviews with economists from the Second Automobile/Dongfeng group that took place in 1988.

40 See *Xinhua*, in English, 7/3/95.

41 The result was that, in a period of less than two years (from the end of 1988 to mid 1990), the total number of private enterprises alone dropped from 14.5 million to 12.4 million. *China Daily*, in English, 17/8/90. As Marie-Claire Bergère (1992) points out on page 143 of her article titled 'Tiananmen 1989: Background and Consequences', at this time enterprises in the collective and private sectors were subject to higher rates of taxation and restrictions and rationing of raw materials and energy supplies. Thomas Gold also noted this outcome of the austerity period and having argued that the private sector was being substantially augmented by 'moonlighting fever', whereby 'entrepreneurs, numerous intellectuals, performers and ordinary workers' were increasingly engaged in 'legal but unregistered and untaxed economic activity', he observed that 'China's entrepreneurial explosion came to a sudden halt . . . in the aftermath of the June 4 assault on Tiananmen; overall economic retrenchment had brought about a substantial shrinkage of the private economy to 12.3 million units'. Thomas Gold, 'Urban Private Business and China's Reforms', 1991: 91.

42 *Xinhua*, in English, 26/8/91.

43 Subsidies paid by the government to large state-owned enterprises for losses amounted to 59.9 billion yuan in 1989 and 58.8 billion yuan in 1990. That was 20 per cent of all state revenues. See *Renmin ribao* 23/9/91, *FBIS* 30/9/91. And it was not all. At the same time the state was paying subsidies to cover losses caused by price increases. These totalled 37.9 billion yuan in 1990 alone. See *Beijing Review*, 6–12 January 1992.

44 Interview at the Second Automobile/Dongfeng group headquarters in Shiyan city in early 1991.

45 *Renmin ribao* 23/9/91. At this time, some of the large advantaged enterprises such as the Baoshan Iron and Steel Complex began to require enterprises with a poor credit history to settle accounts before receiving goods. See ibid. Also at this time, it was noted that in the case of the Jiujiang Power Plant, 430 million yuan was provided by the central government for a project where the actual cost was expected to be 639 million yuan.

46 Where government financial responsibilities have been 'off-loaded' on to the banking system it has been a direct consequence of the soft budget constraint experienced at the level of state-enterprises, while hard budget constraint applied at central government level. By mid 1992, the domestic deficit situation was being openly discussed by Chinese planners and economists and by September it was noted that the proportion of enterprises listed in the state budget as operating 'in the red' had reached 32 per cent, 'with the volume of deficits . . . [reaching] 21 billion yuan, up 3.3 percent over the corresponding 1991 period' (see *Xinhua* 18/9/92, *FBIS* 7/7/92). Moreover, concern over the increasing deficit had been brought out into the open and had been discussed in conjunction with increasing concern over the 'hidden' deficit. For example in June 1992 it was reported that 'the 20.2 billion-yuan deficit was what was shown in China's financial books . . . [but] the financial deficit should include income derived through loans, government debts to banks, and enterprises' potential losses' (see *Zhongguo xinwen she* 29/6/92, *FBIS* 7/7/92).

47 *Zhongguo xinwen she* 29/6/92.

48 See Shea Jia-Dong and Yen Tzung-Ta, 'Comparative Experience of Financial Reform in Taiwan and Korea: Implications for Mainland China', 1992: 241. See also Liu Funian, 'Financial Reform: A Prerequisite for Development', 1990: 126.

49 See *Renmin ribao* 25/1/95, *FBIS* 1/2/95. For their part Second Automobile/Dongfeng corporation economists argued that if all their shares were issued on China's domestic market, they would swamp and so 'distort' the market.

50 This goal had been formally agreed upon at the Fourteenth Party Congress held in October 1992. For comment on the politicking that preceded this Congress, see Baum, *Burying Mao*, 1994: 341–56.

51 *Xinhua* 15/7/86, *FBIS* 17/7/86.

52 *China Daily*, in English, 17/7/92 and *Xinhua*, in English, 19/11/92. In 1991 China's formal national domestic deficit was listed as 20.2 billion. At that time it was noted that 'China's deficit had remained at an annual 9 billion yuan or so, but in the last three years [1988–1991] it has increased to between 12 billion and 20 billion yuan' (see *Zhongguo xinwen she* 29/6/92).

53 It was argued that:

> The year 1988 saw a bout of inflation. At that time, in order to stabilize the currency, the People's Bank of China exercised management of credit limits of specialized banks and strictly curtailed the scope of credit, besides raising the reserve ratio. This

measure, supported by other relevant measures, quickly curbed inflation. By 1990 the inflation rate, which had been 18.5 percent in 1988, had dropped to 2.1 percent.

(see *Renmin ribao* 26/11/92, *FBIS* 15/12/92)

54 *China Daily*, in English, 17/7/92. Post-reform credit limits within the banking system were first introduced in 1985

(see *Renmin ribao* 26/11/92).

55 *Renmin ribao* 26/11/92. See also Liu Funian 1990: 126.

56 This situation undermines the confidence behind statements such as:

> when credit lending grows too fast, a mandatory ceiling – the major credit indicator – will be imposed for lending in order to keep credit activities from running out of control . . . . Specialized banks and regions should loan within the ceiling as regulated by the central bank, and can on no account overshoot it without approval.
>
> (Beijing Institute of International Finance, *The Banking System of China*, 1993: 21)

57 See *Xinhua* 25/7/92, *FBIS* 27/7/92. The name is 'Regulation on Transforming the Management Mechanisms of State-Owned Industrial Enterprises'.

58 *Jingji yanjiu*, 10, 20/10/95, *FBIS* 15/2/96.

59 I have argued that the 1989–92 period of rectification ended because the economic problems it generated could no longer be tolerated. By way of contrast Baum has noted that Hong Kong sources have argued that

> Given the strong expectation that the original verdict on the Beijing massacre would eventually be reversed, his [Deng Xiaoping's] children greatly feared that in the absence of any dramatic new evidence confirming the brilliance of their father's economic theories and strategies, his reputation might suffer grievous, possibly irreparable, posthumous damage – as Mao's reputation had done.

Baum believes this offers a reason for why Deng was so vigorous in supporting the return to progressive economic policy (see Baum, *Burying Mao*, 1994: 341). It is also worth noting the point made by Athar Hussain that

> the problems facing the Chinese economy cannot be solved by reverting to the command economy, though the government has periodically resorted to administrative controls to keep them in check. The [economic] reforms have weakened the structure of

the command economy and the planning machinery to a degree where a reversal is no longer possible.

(see Athar Hussain, 'The Chinese Economic Reforms: an Assessment', 1994: 25)

2 MANAGERS' INTERESTS VERSUS WORKERS' INTERESTS

1 See selections from *Gongren ribao* 9, 13, 23 and 27 January 1995, *FBIS* 29/3/95.

2 Under the terms of the wage trial conducted at the Second Automobile/Dongfeng conglomerate in 1985, managers had been given a total wage package. Though strict guide-lines related to workers' wages were to be followed, the greater autonomy afforded by this and other trials was greatly appreciated by management. Conversely any attempt at heavy handed administration of enterprise affairs met with very strong management resistance.

3 Prior to 1986 the introduction of a system of labour contracting had been discussed and trialled by the leadership élite for some considerable period of time. Progressive members of the Party élite argued that a system of labour contracting would break 'the iron rice bowl' by not only bringing a clearer definition of managers' and workers' responsibilities, but also by promoting an equality between these two contracting parties. The contract system had first been discussed within the ranks of the Party/state élite during the 1980–2 debates on reform priorities, particularly in relation to labour reform. Subsequently labour contracting was trialled in a number of selected enterprises. Local trials of the labour contract system continued throughout 1983 and 1984 and a national conference was held in November 1984 to review progress. This meeting concluded that the reform should continue to be trialled, but should 'not be extended for the time being (beyond the narrow target group of new workers)'. Nevertheless, in spite of the considerable disagreement at all levels of government over the policy and what were agreed to be 'disappointing' results in popularising the policy, by mid 1986, in the context of another review of the policy by the Ministry of Labour and Personnel, it was decided that the time had come for widespread implementation (see Gordon White, 'The Politics of Economic Reform in Chinese Industry: The Introduction of the Labour Contract System', *The China Quarterly*, III, September 1987: 375–6 and 378–80).

4 In the late 1970s, when the Chinese leadership was convinced of the need to protect its industries against a possible Soviet invasion, the Second Automobile work's factories were, as I have noted, situated in a remote and closed area among military installations.

Shirk, among a number of other commentators has noted enterprise managers' interest in ensuring good worker conditions. She follows Walder in arguing that 'managers themselves had an interest in keeping their workers contented and therefore tended to hand out bonuses indiscriminately'. Shirk 1993: 45.

5 Material taken from interviews conducted with Second Automobile/Dongfeng corporation staff in 1987 and 1991. As I have noted, there had been proposals among progressive members of the Chinese leadership to

institute a labour contract system. They anticipated opposition, but were still able to arrange for the system to be trialled. Moreover, the managers of the Second Automobile/Dongfeng group were by no means the only state enterprise managers to oppose (or at least dilute) the system by using long-term contracts for the workers that they now employed (see White, 'The Politics of Economic Reform in Chinese Industry: The Introduction of the Labour Contract System', 1987: 385). White has also pointed out that 'there is considerable evidence that a good deal of . . . resistance to labour reform came from officials in local labour bureaux' (Gordon White, *Riding the Tiger*, 1993: 142).

6 Cited by Minghua Zhao and Theo Nichols in 'Management Control of Labor in State-owned Enterprises: Cases From the Textile Industry', *The China Journal*, 36, July 1996: 15.

7 White has also reported on this plastics plant. He first noted that 'viewing the experience of the 1980s as a whole, it is clear that labour reforms ran into a lot of trouble and did not get very far' and then he cited the plant as one where working hours were 'only two and a half hours a day when the plant was working at full capacity'. He also noted that even in a watered down form, even labour contracting (in contrast to the stringent and pressing labour requirements of Taylorism) was 'highly unpopular' among state enterprise workers. White, *Riding the Tiger*, 1993: 140–41.

8 Yimin Lin has pointed out that at this point in the reform process 'obtrusive [worker] control mostly turned out to be counter-productive and tended to increase manager-worker frictions' (see Yimin Lin 1992: 395).

9 Gordon White, 'State and Market in China's Labour Reforms', *The Journal of Development Studies*, 24 (4), July 1988: 183–5. It has been estimated that by the end of 1987, about 78 per cent of cities in 22 provinces had established labour offices that would process unemployment benefits. See Yimin Lin, 1992: 398. A usual arrangement was that when a worker was unemployed he would receive 50–75 per cent of their former *basic* monthly wage. Workers were required to pay no more than 3 per cent of their standard wage in to the unemployment fund, while the enterprise was required to pay no more than 15 per cent of the total wages paid to the enterprise's contracted workers. Also see White, *Riding the Tiger*, 1993: 142–3 and see Kate Hannan, *China, Modernisation and the Goal of Prosperity*, 1995: 171. It has been estimated that by 1988 enterprise investment in housing was two times higher than in 1981 (see Yimin Lin, 1992: 391).

10 The expectation of life-time employment had been inherited from the previous centralised organisation of the Chinese economy (Walder 1987).

11 The progressive programme that Zhao Ziyang championed at the Thirteenth Party Congress was predicated on his belief that 'all' existing economic problems will be 'resolved with the deepening of economic system reform'. By the spring of 1988 a number of the progressive reforms were being implemented. They included the further development of ownership reform by promoting the enterprise shareholding system; the publicisation of the need to further develop a labour market and the attendant need for further social service reform; a renewed push to separate government administration from enterprise management, now under the auspices of the 1988 Enterprise Law; measures to establish a free market in agricultural land-use rights; and the proposal to accelerate the development of China's east coast, using foreign

investment combined with the low-cost labour time of China's workers to boost manufacture for export. Zhao also promoted his ill-fated proposal to separate Party decision-making from the day to day responsibilities of government administration and, at the same time, his name became welded to the politically inopportune and economically inept price reform measures adopted by the Party leadership in July 1988. See Office of the Research Group on Economic System Reform under the State Council 'Preliminary Plan for Deepening Economic System Reform in 1988 (Draft for Solicitation of Opinions)'; supplement to *Jihua jingji yanjiu*, 5, November 1987; reproduced in translation in *Chinese Law and Government*, Summer, 25 (3), 1992: 76–95. The management of the Second Automobile/Dongfeng corporation favoured the progressive measures promoted by Zhao Ziyang. They particularly applauded the greater autonomy of decision-making for enterprise management that he had promoted and they approved his reinterpretation of public ownership in a manner that effectively sanctioned fundamental state-enterprise ownership reform and the greater flexibility that the new labour contract provisions could provide. Rather than being concerned with the 'deep ideological issues rooted in Marxist definitions of "socialist" and "capitalist" modes of production' and the 'challenge to the traditional socialist political commitment to full employment and job security', they saw that Zhao's reforms, including the labour contract system that he had now included in his platform, would provide them with a clearer definition of their province of interest and they welcomed policies that Zhao Ziyang's support of the Enterprise [Reform] Law would afford their decision-making priorities. However, it was not long before enterprise managers used the considerable economic chaos that preceded the social unrest of 1989 to their own advantage. Then, in the period following the 1989 Tiananmen Incident, these managers were presented with policies consistent with the conservative reformers' bid to effect 'economic rectification'. At this point they were clearly resentful. Material from interviews at the Second Automobile/Dongfeng headquarters in Shi-yan city. They were held in 1988, 1989 and 1991.

12 At this time progressive reform policy was being resisted by Chen Yun, Bo Yibo, Peng Zhen and Wang Zhen who are cited as the line-up of conservative grouping within the Party leadership élite. See White, *Riding the Tiger*, 1993: 61. The line-up of Chen Yun, Peng Zhen, Deng Liqun and Hu Qiaomu have also been cited as the conservatives of the 1980s. See David Kelly (1991) 'Chinese Marxism Since Tiananmen Between Evaporation and Dismemberment'. For her part Solinger has preferred to argue that: 'rather than subscribing to the more simplified characterization of the present leadership as a "pragmatic" [or progressive] faction that has already bested its rivals [the conservatives] . . . [there were] at least three broad lines of fissure within the [China's] policy-making élite'. Solinger identifies these three groups as the 'adjusters, the reformers and the conservatives'. Those 'associated with (and indeed, perhaps the head of) each are [in order] Chen Yun, Zhao Ziyang and Yu Qiuli' (see Solinger 1993). Shirk too offers a line-up of leaders. She cites Deng Xiaoping, Hu Yaobang and Zhao Zhiyang as the progressive reformers and then prefers to discuss Chen Yun and Yao Yilin as the Party veterans with little to lose in the leadership stakes. She then argued that their protégé is the conservative Li Peng (see Shirk 1993: 191).

13 See White, 'The Politics of Economic Reform in Chinese Industry: The Introduction of the Labour Contract System', 1987: 380. The phrase 'a web of interests' was used by Walder to describe a calculated strategy by enterprise work-forces (managers and labourers) that operated as a unit in their quest for the best possible outcome from their negotiations with the government. It is a situation that I am arguing is now clearly obsolete (see Walder 1987). Lin has argued that it is not sufficient to characterise factory managers as 'responding to pressures from workers without much reservation'. He prefers to argue that in the post-reform environment of the 1980s factory managers were keen to maximise their own share of bonus payments and so, while not subject to hard budget constraint, did have an interest in worker productivity. He calls for 'a fuller examination of managers' agendas, especially their attempts [during the 1980s] to play the economic game to their own advantage' (see Yimin Lin 1992: 394). For a discussion of the ideological and 'practical' concerns surrounding the introduction of the 1986 labour contract reform see White (1987) 'The Politics of Economic Reform in Chinese Industry: The Introduction of the Labour Contract System'.

14 Even though the contracting of labour was initially only applied to workers who began employment with a particular enterprise, it was 'highly unpopular' (see White, *Riding the Tiger*, 1993: 141 and 209–12).

15 Some have dated the labour contract reform from 1983 when trials in this policy were introduced (see Walder 1987). For comment on housing reform see Chingboon Lee, 'China's Transition Towards The Market: "Socialization" of the Safety Net', *China Economic Review*, 4 (2), 1993 and Peter Non-Shong Lee (ed.), 'Housing Reform Under Deng Xiaoping', *Chinese Law and Government*, 26 (1), January–February 1993: 3.

16 In December 1987 Zhao Ziyang presided over a meeting of the Central Financial and Economic Leading Group that received a report from the Leading Group for Housing Reform of the State Council and he had supported the January 1988 conference on housing reform where 'The Proposal for the Step-by-Step Implementation of Nationwide Urban Housing Reform' had been approved. This programme was enacted in February 1988.

17 See Peter Non-Shong Lee, 1993: 3–11 and 37–9 and Joseph Chai, 'Consumption and Living Standards in China', *The China Quarterly*, 131, September 1992: 731.

18 See Hannan, *China, Modernisation and the Goal of Prosperity*, 1995: 176–8. It is also clear that the Hubei provincial government was willing to adopt other innovative reform policies at an early date. For example, as Solinger notes, in the provincial capital of Wuhan the use of wholesale centres and trading companies began 'immediately' after this reform initiative was put into place in 1984. In 1987 Wuhan was 'one of only four Chinese cities to have pushed enterprises into bankruptcy' and in what Solinger describes as 'another ground-breaking effort', Wuhan was involved in promoting enterprise mergers. The latter in combination with the housing reform initiatives that I have discussed and with what amounted to a pilot programme for enterprise share issues (see Dorothy Solinger (1996) 'Despite Decentralization: Disadvantages, Dependence and Ongoing Central Power in the Inland – the Case of Wuhan', *The China Quarterly*, 145, March).

19 See Chingboon Lee 1993: 170, *Zhongguo xinwen she*, in English, 25/3/96 and *Xinhua*, in English, 19/3/96. For their part Hubei provincial government administrators have now chosen to make the purchase of housing a price of provisional residential status for economically able rural migrants wanting some permanency in the provincial capital Wuhan. In order to qualify for a so-called 'blue chop' (a blue provisional resident's stamp) the migrant must purchase one of the housing units recently built by the provincial government. At present these units are hanging in the market and have tied up funds that administrators feel could be better deployed. The so-called 'market' price of this housing has not been subsidised by the provincial government. It is also worth noting that housing reform is certainly not the only area of the Chinese economy where the World Bank has been active. For example, in 1993 the World Bank issued reports that advised that 'an average annual growth rate of about 8 to 9 per cent may cause overheating and inflation' in the Chinese economy and in February 1996 the Bank extended loans of $US19 million for the technical renovation of three non-state enterprises. In this case the monies were to be forwarded and administered using China's state-owned Bank of Communications (see *Yangcheng wanbao* 7/7/93, *FBIS* 4/8/93 and *Xinhua*, in English, 8/2/96).

20 Interviews conducted at the Second Automobile/Dongfeng headquarters in Shi-yan city in 1991 and 1992.

21 If you are a lecturer at the Second Automobile/Dongfeng corporation's 'workers' university' (a tertiary studies college that is now called the Hubei Automotive Industries Institute) you are entitled to housing covering 42 square metres (not including kitchen and bathroom); if you are an Associate Professor at the college you are entitled to 60 square metres of living space (not including kitchen and bathroom).

22 Interview in February 1996 with a member of the staff of the Second Automobile/Dongfeng corporation tertiary institute.

23 *ibid*.

24 This is to be done on the basis of home purchasers being able 'to obtain a mortgage loan of up to 70 percent repayable over a maximum term of 10 years provided there is guaranteed security'. China's Industrial and Commercial Bank has now completed what are described as the initial preparations for underwriting a loan from the World Bank 'for housing and social system reform' (see *Xinhua*, in English, 19/3/96 and *Xinhua*, in English, 25/3/96).

25 See Azizur Rahman Khan, Keith Griffin, Carl Riskin and Zhao Renwei, 'Sources of Income Inequality in Post-reform China', *China Economic Review*, 4 (1), 1993.

26 *Xinhua* 10/3/95.

27 *Renmin ribao* 13/11/92, *FBIS* 3/12/92.

28 *Xinhua*, in English, 29/1/95, *Xinhua*, in English, 22/3/96. *Jingjixue dongtai*, 10, 18/10/94, *FBIS* 12/1/95.

29 *Xinhua* 10/3/95, *FBIS* 15/3/96, *Zhongguo gaige*, 10, 13/10/94, *FBIS* 13/1/95 and *Guanli shijie*, 1, 24/1/96, *FBIS*, 28/3/96.

30 *Zhongguo gaige*, 10, 13/10/94.

31 *ibid*. and *Xinhua*, 10/3/95.

32 *ibid*.

33 In this context government sources have again pointed out that they 'should take into account what the state, the enterprises, and the individuals can tolerate' (*Xinhua* 10/3/95).

34 *ibid*.

35 *Xinhua*, in English, 12/5/95. *China Daily*, in English, 2/1/95, *China Daily*, in English, 24/1/96. See also Anita Chan, 'The Emerging Patterns of Industrial Relations in China and the Rise of Two New Labor Movements', *China Information*, IX (4), Spring 1995: 47. Chan has also pointed out that 'given the poor working conditions and lack of any genuine representation' in China's foreign-funded enterprises, 'strikes and go-slows are becoming a commonplace phenomenon in Special Economic Zones'. She gives the example presented in a 1995 *Renmin ribao* editorial that noted that there have been 1,100 cases of 'collective labor disputes' officially recorded in Shenzhen alone over the space of the previous two years (Chan 1995: 50). It is also worth noting that by mid 1995 as many as 91,000 of China's industrial workers were employed by foreign-funded enterprises and that these enterprises produced an estimated 12.2 per cent of total industrial output value. *Zhongguo xinwen she*, in English, 26/7/95.

36 *Xinhua*, in English, 12/5/95. By 1995 there were said to be more than 3,000 labour arbitration committees operating in China's state-owned and foreign-funded enterprises. These committees were employing an estimated 12,000 arbitrators.

37 The January 1995 Labour Law was put in place immediately following a set of Ministry of Labour Regulations 'guaranteeing workers' rights for compensation' if wages are left unpaid, including overtime; if workers have been unjustly sacked; have been subject to faulty safety standards; or have not been awarded their full entitlements in terms of sickness, maternity or holiday leave. *Xinhua* 19/7/93, *FBIS* 2/8/93, *China Daily*, in English, 2/1/95 and *China Daily*, in English, 3/1/95.

38 *China Daily*, in English, 3/1/95.

39 *China Daily*, in English, 24/1/96. A year after the introduction of the 1995 Labour Law, it was reported that the labour supervisory committees that had been established to oversee employer treatment of employees had recovered a total of Rmb. (renminbi) 340 million that had been embezzled and had also 'urged employers to make up a deficiency of Rmb. 288.5 million in social insurance premiums'. Wages arrears of some Rmb. 300 million had also been recovered (see *Zhongguo xinwen she*, in English, 2/2/96).

40 *Renmin ribao*, overseas edition, 28/12/95, *FBIS* 6/2/96 and *Jingji cankao bao* 3/5/96, *FBIS* 2/7/96.

41 *Zhongguo xinwen she*, in English, 17/2/96.

42 *Renmin ribao* 20/12/95, *FBIS* 9/2/96.

43 *Renmin ribao* 23/3/95, *FBIS* 1/6/95.

44 *China Daily*, in English, 3/1/95 and 24/1/96. The Hong Kong published *Lien ho pao* (8/5/95) reported that when their staff interviewed workers who had been on strike and who had demonstrated in the streets in Liaoning and Sichuan during 1995, the workers said that they were worried about 'being able to get food for survival'. In these areas it seems that enterprises were not only dismissing workers, but were also not paying workers on time. Workers were finding themselves 'living in difficult conditions'. There

was obvious government concern 'to prevent workers' discontent and to prevent the appearance of more serious labor unrest', but 'resentment' had obviously not been avoided (see *FBIS* 8/5/95).

45 See *Xinhua*, in English, 3/5/93, *Zhongguo xinwen she* 22/3/94, *FBIS* 1/4/94 and *China Daily*, in English, 18/1/95. As early as 1986, Jiang Yiwei, former director of the Chinese Academy of Social Sciences (CASS) Institute of Industrial Economics, was warning that adoption of the labour contract system 'would intensify an already significant shift of power within the enterprises in favour of managers, with the consequence that workers would become "hired labourers" rather than masters of the enterprise' (White, *Riding the Tiger*, 1993: 139). Under the present 'brand new' labour relations this situation is all the more apparent (see also *Zhongguo xinwen she* 22/3/94, *FBIS* 1/4/94).

46 See *Guanli shijie* 24/1/96, *FBIS* 2/7/96 and *Jingji yanjiu*, 10, 20/10/95, *FBIS* 15/2/96.

47 *ibid*. In 1995 figures government sources estimate that 44.5 per cent of China's state-owned enterprises show losses. *Xinhua* 27/1/95, *FBIS* 3/2/95. See also *Renmin ribao* 20/12/95, *FBIS* 9/2/96.

48 *China Daily*, in English, 26/4/95.

49 *Renmin ribao* 23/3/95, *FBIS* 1/6/95.

50 See *Jingji cankao bao* 19/6/95, *FBIS* 26/7/95. The rate of rural unemployment is significantly higher than urban unemployment and to add to China's unemployment woes, in rural areas it is believed that the number of those out of work will also increase steadily. Indeed, it has been predicted that the total number of rural labourers available for employment 'may surpass 600 million by the year 2000' (*Renmin ribao* 23/3/95). See also *China Daily*, in English, 15/2/96 and *Zhongguo shuiwu bao* 12/11/94, *FBIS* 23/1/95. Other reports argue that out of the current 450 million strong rural work-force (a work-force that currently represents 74 per cent of all China's workers) only 150 million can be accommodated in agricultural production. The remainder must be supported by wage labouring positions (see *Guanli shijie* 24/1/96).

51 *Xinhua*, in English, 17/5/95. It also should be noted that other sources expect a growth rate of 11.7 per cent with a growth in domestic product of no less than 8 per cent per year (see *Guanli shijie* 24/1/96).

3 BANKING, PRICE AND TAXATION REFORM

1 Keun Lee, *Chinese Firms and the State in Transition*, 1991: 13.

2 When we discuss China's programme for industrial reform, the question of how to balance China's 1990s push to develop a market integrated economy that would effectively discipline the investment hunger exhibited by local agents with the Chinese leadership's need for 'political stability and unity' is probably the most interesting question of the moment. It is a balancing act that clearly demonstrates the tensions and contradictions embedded in China's programme for industrial reform. A number of commentators went as far as stating, 'No stability, no nothing. Without a stable social environment, nothing can be accomplished. Stability is the social foundation for implementing reform' (*Jingji cankao bao* 5/1/94, *FBIS* 12/1/94).

3 Some scholars have also argued that the distribution of fiscal resources is one of the indicators of the state of inter-governmental relations (see Dali Yang, 'Reform and the Restructuring of Central-local Relations', in D. Goodman and G. Segal (eds), *China Deconstructs*, 1994: 73).

4 See Li Yunqi (1991) 'Changes in China's Monetary Policy', *Asian Survey*, XXXI (5), May. A jaundiced economic commentator went as far as arguing that 'our banking system is a system allowing everyone to eat from the big common pot. A main symptom of this system is that bank loans are not treated as commodities that can be sold and bought, but are distributed and given away as gifts. If you do not take the loan, you will lose the gift. If you take it, you have no repayment obligation', *Caijing wenti yanjiu*, 10, 15/10/94, *FBIS 6/1/95*.

5 A representative of the Moodys rating agency is reported to have commented that not only are debts to the client banks not likely to be written off, but that to write off the client banks' debts to the People's Bank would involve 'huge sums' that are unlikely to be found for this purpose. Moreover, the agency 'doubted whether Beijing would implement' enterprise bankruptcy reform in the near future, 'because of the severe social consequences, such as supporting unemployed state workers without the safety net of a proper social welfare system' (see the Hong Kong published *South China Morning Post*, in English, 10/2/95). By May 1994, the people's courts had received only 1,577 bankruptcy applications. Of these, only 526 were state-owned enterprises (see *Zhongguo gaige*, 2, 13/2/95, *FBIS* 3/4/95).

6 It has been pointed out that the four client specialised and commercial banks have been submitting an amount to the treasury that is equivalent to an estimated 68 per cent of the bad debt reserve fund since 1988. Then it has been argued that the treasury should return these monies back to the banks to be used alongside the portion of reserve funds retained by the banks themselves to write off bad loans. Alternately a rule should be adopted that would require the banks to set aside a portion of their after-tax profits to finance loan write-offs. A percentage of bad debt loans could then be written off each year. *Guanli shijie*, 6, 24/11/94, *FBIS* 23/3/95. Another problem in relation to the specialised banks was that after the 1992 return to progressive economic policy they were permitted to participate directly in speculation in the Chinese economy. With the return to progressive economic measures they were allowed to establish property development subsidiaries. Banks were permitted to own these subsidiary 'companies' wholly and to fund them from the bank's credit or reserve fund, though it was required that these companies would stand as independent legal entities and that they would operate and account as independent administrations. Another group of these subsidiary companies was permitted to enter into 'joint ventures' with local government and construction enterprises. They acquired land and constructed housing. Others in this raft of companies were established as joint stock companies with each interested party group holding a relevant number of shares and supposedly each group accepting responsibility for any losses incurred. It is a policy measure that would obviously support the push to effect housing reform, but it also fuelled the real estate boom that, in turn, stressed China's immature urban and environmental planning mechanisms and, much to

the central government's consternation, devoured productive agricultural land. And at the same time, the stage was set for direct bank funding to find its way into property ventures. It is obvious that these bank property companies would have considerable leverage in terms of accessing credit. In other words, we would expect them to have *a very soft* budget constraint (see Beijing Institute of International Finance 1993: 230–31). The number of bankruptcies for the six years following the 1988 adoption of the bankruptcy law were as follows. In the first five months after the law was adopted there were eighty-nine bankruptcies, in 1990 there were thirty-two cases of enterprise bankruptcy, 117 bankruptcies in 1991, 420 cases in 1992 and 710 in 1993 (*Zhongguo xinwen she*, in English, 20/13/95).

7 See Shirk 1993 and Beijing Institute of International Finance 1993: 19.

8 See Marc Blecher (1991) 'Sounds of Silence and Distant Thunder', and Liu 1990: 126.

9 *Zhongguo xinwen she* 11/7/93 and *Zhongguo xinwen she* 12/7/93, *FBIS* 27/7/93. *Jinrong shibao* 22/3/96, *FBIS* 2/7/96.

10 *ibid*.

11 Joseph Stiglitz, 'The Design of Financial Systems for the Newly Emerging Democracies of Eastern Europe', 1992: 174–5. Stiglitz suggests that the way to overcome the problem of the risk involved in using mechanisms other than crude monetary control measures is to create a situation where,

> the Central Bank would control the quantity of credit, either auctioning off the right to issue loans or granting the rights to various banks with the proviso that banks could trade the rights among themselves. [He argues that] Such marketable quantity constraints combine the certainty of quantity targets with the allocational efficiency of market mechanisms.
>
> (1992: 176)

12 Barter trade was not at all new to China. It went well back into the history of trading. What was new was the post-reform prevalence of this method of trading: a method that lay outside the purview of state authorities. Throughout the 1980s this form of trade had been recognised as being responsible for diverting supplies away from projects and priorities set down by the state. In spite of the promotion of lateral economic ties in the post-reform period, decentralisation of decision-making had often stood in the way of the free lateral flow of supplies and commodities (see Solinger, *China's Transition From Socialism*, 1993: 162). The use of debt-chains in order to informally access credit was also a common practice in Eastern European reform economies before the considerable changes wrought by events of 1989 (see Christopher Clague, 'The Journey to a Market Economy', 1992: 12; see also Peter Bernholz, 'The Importance of Reorganizing Money, Credit and Banking When Decentralizing Economic Decisionmaking', 1990: 107–114; and Liu 1990: 125–7).

13 In 1991 China's formal national domestic deficit was listed as 20.2 billion yuan. At that time it was noted that 'China's deficit had remained at an annual 9 billion yuan or so, but in the last three years [1988–91] it has

increased to between 12 billion and 20 billion yuan' (see *Zhongguo xinwen she* 29/6/92, *FBIS* 7/7/92; see also *Zhongguo xinwen she* 29/6/92).

14 *ibid*.

15 In the 1984 push to further the process of economic reform through decentralising decision-making the People's Bank had been instructed to institute a reserve deposit rate for its client specialised banks. However, in spite of that policy (intended to promote increased autonomy of client bank decision-making supported by the safety net of a reserve deposit rate) throughout 1985 and 1986 centralised and vertically-organised control of credit continued to hold sway. Even though, as I have noted above, from 1985 the client banks were permitted to borrow from each other, the People's Bank continued to be held responsible for the direct provision of capital to its client banks. The result was that 'in these circumstances, the deposit reserve rate had not played a significant role'. Subsequently (in October 1987), in the face of a reserve rate which amounted to only 6.4 per cent of deposits (in 1985 it had been 11.6 per cent), it was announced that 'the People's Bank would stop taking care of the special banks' capital' (see also *Xinhua* 9/2/87, *FBIS* 12/2/87).

16 See Barry Naughton, 'Macro-economic Management and System Reform in China', 1990: 67.

17 *Renmin ribao* 9/11/84, *FBIS* 15/11/84.

18 The task of drafting the banking law was first undertaken in 1979. It was considered again ten years later – in 1989, again in 1992 and in 1994 (*Renmin ribao, overseas edition* 16/3/95, *FBIS* 25/4/95 and *Renmin ribao*, 16/3/95).

19 See *Zhongguo xinwen she* 14/7/93, *FBIS* 27/7/93, *Xinhua* 21/1/96, *FBIS* 23/1/96 and Hong Kong published *Ming Pao* 28/6/96, *FBIS* 22/7/6. See also Ronald McKinnon, 'Taxation, Money, and Credit in a Liberalizing Socialist Economy', 1992: 114.

20 The recently founded commercial banks are the only banks exempt from banking with the People's Bank of China. These banks are not funded from the public purse, indeed many of them are foreign funded.

21 *Xinhua* 23/7/96, *FBIS* 25/7/96. 'Price-scissors' is a term taken from Lenin that has been used to describe the disguised taxation borne by the agricultural sector in order to fund the process of urban industrialisation.

22 *Jingji ribao* 25/11/94, *FBIS* 1/2/95. See also *Renmin ribao* 5/1/95, *FBIS* 31/1/95.

23 *Renmin ribao* 26/6/96, *FBIS* 30/7/96.

24 See *ibid*., *China Daily*, in English, 29/7/96 and *China Daily (Business Weekly)*, in English, 15–21 January 1995.

25 *Guanli shijie*, 1, 24/1/96, *FBIS* 3/7/96. This journal (named *Management World* in English) has reported on the substance of a report by the Labour Ministry's Science Institute Task Force.

26 The People's Bank now provides funds or credit directly to the Second Automobile/Dongfeng group's own bank and the group has a number of accounts at branches of the Industrial and Commercial Bank. Interview with Second Automobile/Dongfeng group economists in February 1996.

27 *Xinhua*, in English, 24/7/96.

28 *Jingji cankao bao* 3/5/96.

29 The example given is the use by the German company Mercedes Benz of Indonesia, Brazil and India for production 'because off-shore production costs are 12 to 18 percent lower than their domestic counterparts' (*Jingji cankao bao* 3/5/96). When interviewing economists from the Second Automobile/Dongfeng group in 1991 I learnt that prior to the proposed Hyundai negotiations for automotive parts manufacture, the group had attempted to establish a parts manufacturing plant in the new Pudong development zone through negotiation with the very large Chinese Baoshan conglomerate and a Canadian manufacturer.

30 From interviews conducted with the leader of The Research Institute of the Second Automobile/Dongfeng corporation and the senior economist from the Research Institute in February 1996 (see also *Xinhua*, in English, 15/2/96).

31 From interviews conducted in February 1996. We discussed the Second Automobile/Dongfeng corporation's financial fortunes during 1995 and the corporation managers' attitude to current economic reform policy.

32 Material drawn from interviews conducted in 1994 and early 1996 and from *China Daily* (*Business Weekly*), in English, 10–16 April 1994. See also *China Daily*, in English, 10/1/95 and see Xiaohua Yang 1995: 135.

33 Material drawn from interviews conducted with Second Automobile/ Dongfeng management economists in 1991.

34 Shirk 1993: 285. See also Peter Non-Shong Lee 1993: 34–5 and 52.

35 *ibid*.

36 Comment based on interview material. At times when controversial policy has been challenged there has been a steady (almost unrelenting) flow of senior managers from the corporation's base in Shi-yan in north-eastern Hubei province to Beijing to visit state ministry officials. See also Shirk 1993: 286. Shirk describes the formation of the Golden Triangle Entrepreneurs' Club. In 1988 members of this élite group of managers from China's largest and most advantaged state-owned enterprises met in Shanghai and then published their manifesto in *Renmin ribao*.

> The manifesto asserted in sharp language that the respect, authority, and rewards given to enterprise managers were not commensurate with the economic and political risks they faced. They argued that contracting systems were the best way to give the managers their due and to invigorate large enterprises and that the managers needed an independent association of entrepreneurs to give them a political voice in policy-making.
>
> (Shirk 1993: 287)

37 Shirk gleaned the figure of 70 per cent enterprise evasion of tax payments from her interview material (see Shirk 1993: 282–5). See also Peter Non-Shong Lee 1993: 51. Other comments are drawn from my own interviews held with economists from the Second Automobile/Dongfeng group in Shi-yan in 1988 and 1989. At the time the tax-for-profit system was implemented the group's responsibility for producing one-third of their output for sale to the state at fixed prices was matched by the state's

coopting of the raw materials required for this part of production at fixed rate prices. Nevertheless, the management of the group felt that their potential for profit creation had been restricted.

38 See Peter Non-Shong Lee 1993: 55.

39 Material taken from interviews held in February 1996. See also *Jingji cankao bao* 19/3/96, *FBIS* 2/7/96. For an outline of the Enterprise Income Tax Interim Regulations see *Jingji yanjiu*, 11, 20/11/94, *FBIS* 30/1/95.

40 Du Mengkun, 'Government Budgets', 1992: 47. See also Shirk 1993: 283. In the early years of the 1980s Chinese economists had argued that price reform would go a very long way toward effecting a market integrated economy. Today, almost two decades after the introduction of reform policy, arguments presented recognise the degree of complexity involved in the process of reforming a centrally planned economy. Discussion focusing on price reform is now often limited to the question of whether the process of reform in China has matured sufficiently to make it possible to expunge the so-called double-track pricing system that grew up during the 1980s.

41 Ironically, it was Zhao Ziyang's political concern that meant that, though he believed price reform to be essential to the development of market reform, he supported the development of the two-track pricing system during the 1980s. Shirk has argued that,

> his [Zhao's] willingness to expend political capital on price reform was questionable from the beginning, and his decision to create a two-track system by allowing enterprises to sell above-quota output at market prices was a pragmatic strategy designed to avoid bureaucratic conflict.
>
> (Shirk 1993)

42 Du Mengkun 1992: 128–9.

43 *Zhongguo xinwen she* 12/1/95, *FBIS* 25/1/95 and *Jinrong shibao* 6/12/94, *FBIS* 23/1/95.

44 *ibid*. See also K.C. Yeh, 'Macroeconomic Issues in China in the 1990s', *The China Quarterly*, 131, September 1992: 533–42.

45 See Yeh 1992.

46 By 1993, the majority of Chinese economists, like their Western counterparts, had identified specific inflation cycles. They saw the first cycle as the 'planning error type'. This was the 1978–82 cycle which they argued was 'induced by investment expansion without a corresponding expansion of consumption'. In that respect, it was seen as different from the subsequent two cycles: 1983–6 and 1987–91. In assessing the 1983–6 cycle some Chinese economists noted that 'during 1983 and 1984 the proportion of profits to be retained by enterprises was increased and funds at the disposal of enterprises showed a marked growth'. The result was 'the rapid expansion of "self-determined investment" by the grass-roots units'. They noted that, in 1984, 'autonomy in respect of bank credit was increased', together with further expansion of enterprise autonomy and experiments in wage reform and went on to say that 'in the fourth quarter

of 1985, the total volume of wages of state-owned enterprises grew 46 percent over the same period the previous year'. At that time, the growth in 'extra-budgetary investment' was at its greatest. Then, in the 'brief readjustment of 1985 and 1986, some of the autonomy handed down was taken back'. A 'bonus tax' and controls over investment were implemented. But greater autonomy, particularly in the case of local government and the 'official profiteering', which was now accompanying the dual-track pricing system was soon established. In 1988, there was 'panic purchasing' in response to a rising rate of inflation. And, another problem which became increasingly prominent after 1987 was 'structural deterioration'. State economists noted that the speed of development of the processing industry greatly exceeded the speed of development of basic industries. There was overheating and retrenchment (economic contraction) followed. This was recognised to be the result of government policy. After all, 'retrenchment cannot be manifested as a process which spontaneously occurs from bottom to top', *Jingji guanli*, 10, 20/10/93. *FBIS* 9/12/93. See also Hong Kong *Agence France-Presse*, in English, 22/5/95, *Jiefang ribao* 28/10/92, *FBIS* 10/11/92, Peter Non-Shong Lee 1993: 11, and *China Daily*, in English, 25/1/95.

47 *Jiefang ribao* 28/10/92.

48 *ibid*.

49 *Guangming ribao* 17/1/92, *FBIS* 3/3/92, Du Mengkun 1992: 128–35.

50 Interview with Finance Minister (Liu Zhongli); see *Xinhua* 18/9/92, *FBIS* 21/9/92.

51 McKinnon 1992: 117.

52 McKinnon 1992: 117, 113–15.

53 McKinnon 1992: 116. An article published in January 1995 proclaimed that a survey conducted using some 10,000 enterprises of all types found that 'more than 50 percent of enterprises nationwide were in the red at the beginning of last year [1993]. By the end of 1994, however, the figure had dropped to 34 percent' (see *China Daily*, in English, 26/1/95). Another 1995 editorial (also published in January) noted that since a new accounting system had been put in place 'money-losing enterprises accounted for 44.5 percent of the budgeted [state-owned] enterprises by late September 1994'. Their total losses were estimated to amount to 29.2 billion yuan (see *Renmin ribao* 4/1/95, *FBIS* 3/2/95). And yet another January article noted that banks had been urged to extend credit to the state-owned enterprises in order to keep them afloat, but the result was that when 'hidden losses' were taken into account as many as 60 per cent were operating in the red (see *China Daily*, in English, 9/1/95).

54 The need for taxation reform had been very clearly recognised in Jiang Zemin's Work Report to the Fourteenth Party Congress where he stated that there was a pressing need for the creation of a rational system of taxation, particularly in terms of the division between the central government and the localities (see Tony Saich, 'The Fourteenth Party Congress: A Programme for Authoritarian Rule', *The China Quarterly*, 132, December 1992a: 1145).

55 This was contrasted with the US situation where, in the period 1972 to 1989, federal government revenue had risen from 19.1 per cent of gross national product to 23 per cent (*Xinhua*, in English, 30/7/93 and *Caijing wenti yanjiu*, 2, 5/2/95, *FBIS* 4/5/95).

56 China's dropping proportion of government revenue in relation to gross domestic product has been compared with the situation in other non-reforming economies. Chinese sources have noted that in the developed market economies during the decade 1979 to 1989 the percentage of government financial revenue to gross domestic product did not drop. It is believed to have risen from 42.8 to 48.7 per cent. In China, during the same decade, it dropped from 26.2 per cent to 17.5 per cent and by 1993 it had dropped to 13.9 per cent (*Caijing wenti yanjui*, 2, 5/2/95).

57 See McKinnon 1992: 113–14.

58 *Jingji guanli*, 11, 5/11/93, *FBIS* 6/1/94, *Renmin ribao* 9/1/94, *FBIS* 21/1/94. It was at the November 1993 Third Plenum of the Fourteenth Party Central Committee that it was decided that a new taxation system should be adopted specifically to give 'an unprecedentedly strong boost to the center's fiscal capacity *vis-à-vis* the provinces. The previous "system of fiscal contract" (*caizheng baoganzhi*) was now to be abolished and replaced by a "system of tax-sharing" (*fenshuizhi*)' (see Jae Ho Chung, 'Beijing Confronting the Provinces: The 1994 Tax-sharing Reform and its Implications for Central-Provincial Relations in China', *China Information*, IX (2/3), Winter 1994–5: 1). Taxation reform had long been a very sensitive issue. As early as the period 1982–4 Zhao Ziyang had favoured a 'tax-for-profit' approach and this had been supported by both Deng Xiaoping and by conservative reformers including Chen Yun (see Shirk 1993: 251–79). Zhao had argued that it was an approach that would enhance the independence of the state-owned enterprises. It was also an approach that in Zhao's formulation should be a two-stage project. The second, more radical stage, of this reform was, as White points out, 'introduced politically by Zhao Ziyang and intellectually by the economist Ma Hong'. This second-stage was planned to begin in late 1984, but

> the transition between stage one and two made heavy weather during 1985–6 and was finally abandoned in the spring of 1987 when it was announced that financial relations between state and enterprise would henceforth be organised according to a "contract responsibility system".
>
> (White, *Riding the Tiger*, 1993: 131–2)

See also Shirk 1993: 280–329. Shirk has asked 'why was it possible for enterprise profit contracting to replace tax-for-profit less than three years after the tax scheme had been implemented? [She answers her own question.] The tax scheme was an easy target for the broadly popular contracting approach' and she talks of the 'fast oxen stampede' of large state-owned enterprises lobbying against the policy (see Shirk 1993 particularly p. 282 and p. 285). For figures on decreasing taxation receipts see *Zhengming*, 195, 1/1/94, *FBIS* 19/1/94.

59 *Renmin ribao* 9/1/94, and *Qiye guanli*, 12, 1/12/95, *FBIS* 9/2/96. See also Christopher Honnor (1994) 'Taxation Reforms Capital, Indirect, and Consumption Tax Changes', *Access China*, 13, March/April. The management of the Second Automobile/Dongfeng group had negotiated

their taxation with representatives from the Ministry of Machine Building Industry each year. If those representing management's interest did well in these negotiations they returned as conquering heroes and if not they made their apologies to other members of the enterprise group's management.

60 *Xinhua*, in English, 15/12/93 and *China Daily*, in English, 2/4/94.

61 *Xinhua*, in English, 15/12/93, *Xinhua* 12/1/94, *FBIS* 13/1/94. Honnor has noted that 'foreign investors operating in Special Economic Zones and Special Development Zones expressed concern over the new VAT. The foreign investors had secured a special tax exemption from the old CICT taxes. However, it appears that Ministry spokespersons have left the door open to allowing tax credits to foreign entrepreneurial investors whose tax burdens may have been unexpectedly increased' (Honnor 1994: 23; see also *China Daily* (*Business Weekly*), in English, 5–11 December 1993; see also Stephen Herschler 1995).

62 *Renmin ribao* 9/1/94, *FBIS* 21/1/94.

63 It has been pointed out that in the face of a national income that dropped 'too quickly . . . government bonds increased rapidly'. They became (and in many respects still are) 'a major way to create new revenue'. See *Caijing wenti Yanjiu*, 2, 5/2/95. See also *Zhongguo xinwen she* 9/9/92, *FBIS* 29/9/92, *Xinhua* 22/11/92, *FBIS* 25/11/92, *Xinhua* 9/8/92, *FBIS* 10/8/92, *Xinhua* 23/1/96, *FBIS* 2/2/96.

64 *Jingji guanli*, 11, 5/11/93, *FBIS* 6/1/94. Even as early as 1 April 1994 (just a few months after the VAT had been put in place) there were reports of 'the forgery of invoices for value-added tax greatly disturbing the country's new tax reform'. There was a call for 'the country's police, taxation and judicial workers to take severe measures to stop criminal activities concerning invoices'. See *China Daily*, in English, 1/4/94.

65 That situation 'made it difficult for state macroeconomic regulation and control to achieve good results due to the loss of effective financial support'. Indeed Western commentators were noting that while 'a decrease in the profit tax-take was as intended by [the] reforms', in the Chinese experience, 'the extent of the fall had come as a surprise to the government'. See Hussain 1994: 27. Hussain also noted that almost all of the decrease in the ratio of (Chinese) government revenue to GNP is accounted for by the decrease in profit taxes relative to GNP. He argued that 'the main problem on the Chinese government's expenditure side is the change in the composition of government expenditure in the 1980s' (*ibid*).

66 *Beijing Review*, in English, 10–16 January 1994.

67 See *Xinhua*, in English, 11/4/94 and 26/4/94, *Zhongguo xinwen she* 22/3/94, *FBIS* 1/4/94 and *Zhongguo xinwen she* 14/7/93, *FBIS* 1/4/94.

68 *Xinhua* 16/7/96, *FBIS* 31/7/96 and *Zhongguo shuiwu bao* 8/12/95, *FBIS* 15/2/96. See also Herschler 1994: 243.

69 See Herschler 1994: 242.

70 See Dali Yang, 'Reform and the Restructuring of Central-local Relations', 1990: 83.

71 The rise in living standards is not, of course, only reflected in increased consumption tax. In Shanghai in 1995 the amount of personal income tax collected increased by over 98 per cent compared with the previous year. It amounted to 1.51 billion yuan. *Xinhua*, in English, 20/1/96. See also Herschler 1994.

72 Zhengming, 195, 1/1/94.

4 OWNERSHIP REFORM

1 *Renmin ribao* 16/12/94, *FBIS* 6/1/94.
2 See Arnold Harberger, 'Strategies for Transition', 1992: 297 and Ma Hong and Liu Shijin, 'How To Correctly View the Reform of the State-Owned Property Rights System', *Jingji ribao* 21/3/95, *FBIS* 8/5/95. Ma Hong is a former director of the Chinese Academy of Social Sciences and former director of the Industrial Economics Institute of the Chinese Academy of Social Sciences. In his retirement he has been the honorary director of the Research Centre on Economic, Technological and Social Development under the State Council.
3 *Xinhua* 9/1/95, *FBIS* 31/1/95. A recent sample survey of state enterprises indicated that as many as 70 per cent 'are burdened with heavy debts'. See *China Daily* (*Business Weekly*), in English, 2–8 April 1995. Moreover, the non-payment of an estimated one-third of bank loans by state enterprises has turned the banking system's book capital 'into uncollectable debts and messy accounts'. It also means that the banks continue to be obliged to 'provide a steady stream of new supplemental funds' (*Caijing wenti yanjiu*, 10, 15/10/94, FBIS 6/1/95).
4 *Renmin ribao* 2/12/94, *FBIS* 18/1/95, *Xinhua*, in English, 17/5/95. See also interview with Ma Hong and Li Shijin, *Jingji ribao* 21/3/95, and interview with Chinese Academy of Social Sciences Industrial Economics Institute deputy director – Chen Jiaqui, reported in Hong Kong published *Ching chi tao bao*, 40, 10/10/94, see *FBIS* 12/1/95. In addition see Harberger 1992: 298.
5 *Jingji yanjiu*, 10, 20/10/95, *FBIS* 15/2/96.
6 *Zhenli de zhuiqiu*, 11, 11/11/94, *FBIS* 19/1/95.
7 *Zhenli de zhuiqiu*, 12, 11/12/94, *FBIS* 3/4/95.
8 *Zhenli de zhuiqiu*, 11, 11/11/94.
9 Ma Hong and Liu Shijin, *Jingji ribao* 21/3/95, and *China Daily* (*Business Weekly*), in English, 15–21 January 1995.
10 See Ma Hong and Liu Shijin, *Jingji ribao* 21/3/95. By 1994 there were an estimated 5,000 joint stock enterprises with nearly 200 of these traded on China's official share markets. *Renmin ribao* 16/12/93, *FBIS* 6/1/94.
11 *China Daily* (*Business Weekly*), in English, 2–8 April 1995, *Zhongguo tongxun she*, published in Hong Kong, 24/12/94, *FBIS* 12/1/95.
12 *ibid*.
13 *ibid*. See also Steven Cheung, 'Privatization vs. Special Interests: The Experience of China's Economic Reforms', 1990.
14 *ibid*. China's bankruptcy law had been passed in 1986. It was much debated and was passed with only a narrow margin of support. There was little disagreement over the idea of enterprise bankruptcy, but there was concern over whether China's reforms had reached the point where the law could be successfully implemented. As I note, to date, it has been used only sparingly. See Wang Huijiong and Li Shantong, *Industrialization and Economic Reform in China*, 1995: 129.
15 See Gordon Rausser and Leo Simon, 'The Political Economy of Transition in Eastern Europe: Packaging Enterprises for Privatisation', 1992: 269.

16 *Jingji ribao* 25/11/94, see also *Renmin ribao* 5/1/95, and interview with Chen Jiaqui.
17 *Jingji cankao bao* 11/12/94, *FBIS* 9/2/96.
18 Zhao Ziyang had originally intended that the Enterprise Law would be a vehicle for promoting the separation of Party responsibility from the administrative responsibilities of state administration. But the law very quickly came to be associated with the other level of Zhao's administrative concerns. It was used only as a vehicle for promoting the separation of enterprise management responsibilities from the responsibilities of government bureaucracy (see *Jingji ribao* 19/2/93, *FBIS* 5/3/93 and *Jingji yanjiu*, 11, 20/11/94, *FBIS* 30/1/95).
19 Other Chinese commentators have argued that since the Fourteenth Party Congress decision to promote a market economy, many of the 'ideological barriers to market reforms' have been removed. See *Jingji yanjiu*, 11, 20/11/94, *FBIS* 30/1/95. See also Hong Kong published, *Ching chi tao pao* 12/2/96, *FBIS* 2/7/96, *Renmin ribao* 19/1/95, *FBIS* 25/1/95 and *Renmin ribao* 27/12/94, *FBIS* 31/1/95.
20 See *Jingji Yanjiu*, 10, 20/10/94, *FBIS* 5/1/95.
21 See *ibid.*, *China Daily*, in English, 24/4/95, and *Renmin ribao* 19/1/95.
22 See *Renmin ribao* 25/1/95, *FBIS* 1/2/95, *Jingji Yanjiu*, 10, 20/10/94, and *Jingjixue dongtai*, 5, 18/5/95, *FBIS* 21/7/95.
23 *Renmin ribao* 19/1/95. 'The major investors in China are Chinese from Hong Kong and Taiwan, taking up to 76%'. Hong Kong capital comprising 63 per cent and Taiwanese capital 13 per cent. See Chan 1995.
24 *Zhongguo xinwen she*, in English, 22/1/96.
25 Chan 1995: 48. Though Guangdong is the mecca for Hong Kong investors above all others, it is the Korean investors that are earning themselves the worst name in relation to workers' pay and conditions.
26 An announcement by Jiang Zemin at the 1995 meeting of the Asia-Pacific Economic Cooperation Forum (APEC). Published in Hong Kong in *Kuang-chiao ching*, 12, 16/12/95, *FBIS* 15/2/96.
27 See *Zhongguo xinxi bao* 18/11/94, *FBIS* 18/1/95, *Zhongguo xinwen she*, in English, 1/2/96 and the Hong Kong published *South China Morning Post*, in English, 31/6/96.
28 *Zhongguo xinxi bao* 18/11/94, *FBIS* 18/1/95 and *Renmin ribao* 2/12/94, *FBIS* 18/1/95. Companies that had issued shares before the Corporation Law was implemented have been required to re-register. If they do not meet the regulations required by the law they can be listed as ordinary companies, but they cannot be called either 'limited' or 'shareholding' companies. *Xinhua*, in English, 2/4/96.
29 *Jingji yanju*, 11, 20/11/94, *FBIS* 30/1/95.
30 *Beijing Review*, 2, in English, 9–15 January 1995.
31 *Renmin ribao* 13/1/95, *FBIS* 31/1/95.
32 *Beijing Review*, 2, in English, 9–15 January 1995.
33 *China Daily*, in English, 24/4/95, *Guanli shijie*, 1, 24/1/96, *FBIS* 28/3/96, and *Xinhua*, in English, 7/5/95.
34 *Guanli shijie*, 1, 24/1/96, *FBIS* 28/3/96.
35 *Zhongguo gaige*, 10, 13/10/94, *FBIS* 13/1/95.
36 *Guanli shijie*, 1, 24/1/96, *FBIS* 28/3/96.

37 *ibid.* and *Renmin ribao* 21/10/91.
38 Interviews conducted at the Shi-yan headquarters of the Second Automobile/Dongfeng corporation in 1992, 1994 and February 1996. See also *Xinhua*, in English, 3/1/95. Official Party/state sources argue that:

> the enterprise reform today has some connection with past enterprise reforms but with differences. Its general goal is to mold an independent subjective aspect of economic operation that falls in line with market competition . . . . [This] requires standardisation of the series of relationships between the enterprise and the investor, the enterprise and the debtor, the enterprise and the government . . . .
>
> (*Renmin ribao* 19/1/95)

39 Interviews conducted in Shi-yan in 1991.
40 Information drawn from interviews conducted with Second Automobile/Dongfeng staff in 1989, 1991 and 1996. In the February 1996 interviews it was pointed out that the various branches within the Second Automobile/Dongfeng group could only borrow from the corporation bank if the corporation had funds available. The People's Bank is permitted to give credit notes to the Second Automobile/Dongfeng group's own bank.
41 Interviews conducted in February 1996 with Second Automobile/Dongfeng economists. See also *China Daily*, in English, 24/4/95.
42 Material from Second Automobile/Dongfeng interviews.
43 *Xinan jingi ribao* 2/1/96, *FBIS* 15/2/96 and *Zhongguo gaige*, 9, 13/9/94, *FBIS* 4/1/95.
44 *Jingji yanjiu*, 11, 20/11/94, *FBIS* 30/1/95.
45 *Shenzhen tequ bao* 10/1/95, *FBIS* 25/1/95.
46 *Caimao jingji*, 10, 11/10/94, *FBIS* 23/1/95.
47 *ibid.*
48 *Xinan jingji ribao* 2/1/96, *Zhongguo gaige*, 9, 13/9/94. By the end of 1994 shares traded on the A share market had an estimated gross value of 192,000 billion yuan. See *Zhongguo xinwen she*, in English, 5/5/95.
49 See Xiaochuan Zhou, 'Privitization Versus a Minimum Reform Package', *China Economic Review*, 4 (1), 1993; *Xinan jingji ribao* 2/1/96, *China Daily*, in English, 24/4/95 and *Beijing Review*, in English, 3/5/95.
50 *ibid.* See also *Xinhua*, in English, 2/4/96.
51 *Ching chi tao bao*, 47, Hong Kong published 28/11/94, *FBIS* 1/2/95.
52 *ibid.*
53 *Caimao jingji*, 10, 11/10/94.
54 *ibid.*
55 *Guoji maoyi*, 11, 20/11/94, *FBIS* 23/1/95 and *Jingji kexue*, 5, 20/10/94, *FBIS* 23/1/95.
56 See Scott Thomas (1992) 'Political Economy of Privatization: Poland, Hungary and Czechoslovakia'; and Jan Winiecki (1992) 'Privatization in East-Central Europe: Avoiding Major Mistakes'.
57 Shirk, *The Political Logic of Economic Reform in China*, 1993: 345–6.

CONCLUSION

1 Gordon Rausser, 'Lessons for Emerging Market Economies in Eastern Europe', 1991: 311.
2 As Yimin Lin has pointed out the managers of China's large state-owned enterprises were subject to pressure from workers who 'expected to receive more services and conveniences' than fellow workers in the less prestigious small state or collective enterprise sector of the urban economy. Moreover, those who worked in the small state and collective enterprises were not surprised to be treated in a less advantaged manner than those who belonged to large state-owned enterprises. See Yimin Lin 1992: 391.
3 *Jingji cankao bao* 19/6/95, *FBIS* 26/7/95.
4 See White, *Riding the Tiger*, 1993: 143.
5 Today there are an increasing number of examples of local government administrators acting on behalf of the wage-earner sector of their constituency. For example, the Beijing Municipal Government's action in subsidising the price of staple foods, even after price reform had been effected.

The use of the apt term 'the national scramble' is drawn from Brantly Womack and Guangzhi Zhao, 'The Many Worlds of China's Provinces', 1991: 170.

Bibliography

AUTHOR'S INTERVIEWS IN THE PEOPLE'S REPUBLIC OF CHINA

Interviews with managers and economists from the Second Automobile/ Dongfeng corporation, conducted December 1985 and January 1986, July 1987, September 1988, October 1989, May 1991, June 1992, September 1994 and February 1996.

Interviews with economists from the Industrial Economics Institute of the Chinese Academy of Social Sciences in October 1989 and May 1991.

Interview with Ma Hong in October 1989. (Ma Hong is the former President of the Chinese Academy of Social Sciences and Honorary Director of the Research Centre of Economic, Technological and Social Development under the State Council.)

OTHER INTERVIEWS

Interview with Finance Minister – Liu Zhongli held in 1992. Reported in *Xinhua* 18/9/92.

Interview with Ma Hong and Liu Shijin, 'How to Correctly View the Reform of the State-Owned Property Rights System', published in *Jingji ribao* 21/3/ 95.

Interview with Chen Jiaqui, Deputy Director of the Chinese Academy of Social Sciences Industrial Economics Institute. Published in Hong Kong by *Ching chi tao bao* 10/10/94.

Interview with Janos Kornai titled 'Hungary's Reform: Halfway to the Market', published in *Challenge*, May–June, 1985.

Bossanyi, K. (1990) 'An Interview with Janos Kornai', *Acta Oeconomica*, 42 (3–4).

PEOPLE'S REPUBLIC OF CHINA BOOK PUBLICATIONS

Beijing Institute of International Finance (1993) *The Banking System of China*, Beijing: China Planning Press.

Deng Xiaoping *The Selected Works of Deng Xiaoping*, vol. 3; quotations reproduced in *Renmin ribao* 5/11/93 and *Xinhua* 9/11/93.*
Office of the Research Group on Economic System Reform under the State Council (1987) *Preliminary Plan for Deepening Economic System Reform in 1988 (Draft for Solicitation of Opinions)*; supplement to *Jihua jingji yanjiu*, 5, November; reproduced in trans. in *Chinese Law and Government* 25 (3), summer, 1992: 76–95.
Wang Huijiong and Li Shantong (1995) *Industrialization and Economic Reform in China*, Beijing: New World Press.
Xue Muqiao (1986) *China's Socialist Economy*, revised edn, Beijing: Foreign Languages Press.
Zhong Huaiwen (1989) *Years of Trial, Turmoil and Triumph*, Beijing: Foreign Languages Press.

PEOPLE'S REPUBLIC OF CHINA PARTY APPROVED JOURNAL AND NEWSPAPER PUBLICATIONS

Beijing Review, Caijing wenti yanjiu, Caimao jingji, China Daily and *Daily* (*Business Weekly*), *Gongren ribao, Guangming ribao, Guanli shijie Guoji maoyi, Jiefang ribao, Jihau jingji yanjiu, Jingji cankao bao, guanli, Jingji kexue, Jingji ribao, Jingji yanjiu, Jingjixue dongtai, Jinrong shibao, Qiye guanli, Renmin ribao* and *Renmin ribao overseas edition, Shenzhen tequ bu, Xinan jingji ribao, Xinhua Press, Yangcheng wanbao, Zhenli de zhuiqiu, Zhongguo gaige, Zhongguo shuiwu bao, Zhongguo xinwen she* and *Zhongguo xinwen she,* in English, *and Zhongguo xinxi bao.**

HONG KONG PUBLISHED JOURNALS AND NEWSPAPERS

Agence France-Presse – Hong Kong, Ching chi tao bao, Kuang-chiao ching, Lien ho pao, Ming pao, South China Morning Post, Zhengming and *Zhongguo tongxun she.**

*Chinese language editions translated and reproduced by *Foreign Broadcast Information Service (FBIS).*

BOOKS PUBLISHED OUTSIDE THE PEOPLE'S REPUBLIC OF CHINA

Baum, R. (ed) (1991) *Reform and Reaction in Post-Mao China*, London: Routledge.
— (1994) *Burying Mao*, Princeton, NJ: Princeton University Press.
Benewick, R. and Wingrove, P. (eds) (1988) *Reforming the Revolution: China in Transition*, London: Macmillan.
— (1995) *China in the 1990s*, London: Macmillan.
Brugger, B. and Reglar, S. (1994) *Politics, Economy and Society in Contemporary China*, London: Macmillan.
Brus, W. and Laski, K. (eds) (1989) *From Marx to the Market*, Oxford: Clarendon Press.
Byrd, W. (ed.) (1992) *Chinese Industrial Firms Under Reform*, Oxford: Oxford University Press.

Clague, C. and Rausser, G. (eds) (1992) *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.
Dassu, M. and Saich, T. (eds) (1992) *The Reform Decade in China*, London: Kegan Paul.
Ding, X.L. (1994) *The Decline of Communism in China*, New York: Cambridge University Press.
Dirlik, A. and Meisner, M. (eds) (1989) *Marxism and the Chinese Experience*, Armonk, NY: M.E. Sharpe.
Dittmer, L. (1994) *China Under Reform*, Boulder, CO, San Francisco, CA and Oxford: Westview Press.
Dorn, J. and Wang Xi (eds) (1990) *Economic Reform in China*, Chicago, IL: University of Chicago Press.
Dreyer, J. (1993) *China's Political System*, London: Macmillan.
Dwyer, D. (ed.) (1994) *China: The Next Decade*, Harlow: Longman.
Garnaut, R. and Liu Guoguang (eds) (1992) *Economic Reform and Internationalisation*, Sydney: Allen and Unwin.
Goldman, M. (1994) *Sowing the Seeds of Democracy in China*, Cambridge, MA: Harvard University Press.
Goodman, D. (1994) *Deng Xiaoping and the Chinese Revolution*, London and New York: Routledge.
— (ed.) (1997) *China's Provinces in Reform*, London and New York: Routledge.
Goodman, D. and Segal, G. (eds) (1991) *China in the Nineties*, Oxford: Clarendon Press.
— (1994) *China Deconstructs*, London and New York: Routledge.
Hamrin, C.L. and Suisheng Zhao (eds) (1995) *Decision-Making in Deng's China*, Armonk, NY and London: M.E. Sharpe.
Hannan, K. (compiled and edited) (1995) *China, Modernisation and the Goal of Prosperity*, Cambridge: Cambridge University Press.
Hicks, G. (ed.) (1990) *The Broken Mirror: China After Tiananmen*, Harlow: Longman.
Jia Hao and Lin Zhimin (1994) *Changing Central-Local Relations in China*, Boulder, CO, San Francisco, CA and Oxford: Westview Press.
Jiwei Ci (1994) *Dialectic of the Chinese Revolution*, Stanford, CA: Stanford University Press.
Keun Lee (1991) *Chinese Firms and the State in Transition*, Armonk, NY: M.E. Sharpe.
Kornai, J. (1980) *Economics of Shortage*, Amsterdam: North Holland Press.
— (1986) *Contradictions and Dilemmas*, Cambridge, MA and London: MIT Press.
— (1990a) *The Road to a Free Economy*, New York and London: W.W. Norton.
— (1990b) *Vision and Reality, Market and State*, Hertfordshire: Harvester Wheatsheaf.
Lardy, N. (1992) *Foreign Trade and Economic Reform in China, 1978–1990*, Cambridge: Cambridge University Press.
Lieberthal, K. and Oksenberg, M. (1988) *Policy Making in China*, Princeton, NJ: Princeton University Press.
Meisner, M. (1986) *Mao's China and After*, New York: The Free Press / Macmillan.

Nolan, P. (1995) *China's Rise, Russia's Fall*, London: Macmillan.
Nolan, P. and Dong Fureng (1990) *Market Forces in China*, London: Zed Books.
Riskin, C. (1988) *China's Political Economy*, Oxford: Oxford University Press.
Shirk, S. (1993) *The Political Logic of Economic Reform in China*, Berkeley, CA: University of California Press.
Solinger, D. (1993) *China's Transition From Socialism*, Armonk, NY: M.E. Sharpe.
Ting Gong (1994) *The Politics of Corruption in Contemporary China*, Westport, CT, London: Praeger.
Totten, G. and Zhou Shulian (1992) *China's Economic Reform*, Boulder, CO, San Francisco, CA and Oxford: Westview Press with The Centre for Pacific Asia Studies, Stockholm University.
Unger, J. (ed.) (1991) *The Pro-democracy Protests in China*, Sydney: Allen and Unwin.
Watson, A. (ed.) (1992) *Economic Reform and Social Change in China*, London: Routledge.
White, G. (1991) *The Chinese State in the Era of Economic Reform*, Armonk, NY: M.E. Sharpe.
— (1993) *Riding the Tiger*, London: Macmillan.
Xiaohua Yang (1995) *Globalization of the Automobile Industry*, Westport, CT and London: Praeger.

JOURNAL ARTICLES AND CHAPTERS IN BOOKS PUBLISHED OUTSIDE THE PEOPLE'S REPUBLIC OF CHINA

Bei Duoguang, Koontz, A. and Xiangqian Lu, L. (1992) 'The Emerging Securities Market in the PRC', *China Economic Review* 3 (2).
Bei Tao and Holton, R. (1989) 'Interprovincial Trade and Economic Development in China', *China Economic Review* 1 (1).
Bergère, M.-C. (1992) 'Tiananmen 1989: Background and Consequences', in M. Dassu and T. Saich (eds), *The Reform Decade in China*, London: Kegan Paul.
Bernholz, P. (1990) 'The Importance of Reorganizing Money, Credit, and Banking When Decentralizing Economic Decisionmaking', in J.A. Dorn and Wang Xi (eds), *Economic Reform in China*, Chicago, IL: University of Chicago Press.
Blecher, M. (1991) 'Sounds of Silence and Distant Thunder', in D. Goodman and G. Segal (eds), *China in the Nineties*, Oxford: Clarendon Press.
Breslin, S. (1992) 'China's Interrupted Evolution', *The Journal of Communist Studies* 8(1), March.
Byrd, W. (1992) 'The Second Motor Vehicle Manufacturing Plant' in W. Byrd (ed.), *Chinese Industrial Firms Under Reform*, Oxford: Oxford University Press.
Cauley, J and Sandler, T. (1992) 'Agency Theory and the Chinese Enterprise Under Reform', *Chinese Economic Review* 3 (1).
Chai, J (1992) 'Consumption and Living Standards in China', *The China Quarterly* 131, September.
Chan, A. (1995) 'The Emerging Patterns of Industrial Relations in China and the Rise of Two New Labor Movements', *China Information* IX (4), Spring.

Cheung, S. (1990) 'Privatization vs. Special Interests: The Experience of China's Economic Reforms', in J. Dorn and Wang Xi (eds), *Economic Reform in China*, Chicago, IL: University of Chicago Press.
Chingboon Lee (1993) 'China's Transition Towards the Market: "Socialization" of the Safety Net', *China Economic Review* 4 (2).
Clague, C. (1992) 'The Journey to a Market Economy', in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.
Dali Yang (1990) 'Patterns of China's Regional Development Strategy', *The China Quarterly* 122, June.
— (1994) 'Reform and the Restructuring of Central-Local Relations', in D. Goodman and G. Segal (eds), *China Deconstructs*, London: Routledge.
Davis, D. (1992) 'Job Mobility in Post-Mao Cities: Increases on the Margins', *The China Quarterly* 132, December.
Ding Wang (1990) 'A Model for China's Industrial Firms During the Transitional Period', *China Economic Review* 1 (2).
Dirlik, A. (1989) 'Postsocialism? Reflections on "Socialism With Chinese Characteristics'", in A. Dirlik and M. Meisner (eds), *Marxism and the Chinese Experience*, Armonk, NY: M.E. Sharpe.
Dittmer, L. (1995) 'Informal Politics Reconsidered', *The China Journal* 34, July.
Du Mengkun (1992) 'Price Reform', in G. Totten and Zhou Shulian, *China's Economic Reform*, Boulder, CO, San Francisco, CA and Oxford: Westview Press with The Centre for Pacific Asia Studies, Stockholm University.
Dye, T. (1990) 'Economic Growth and Reform in China's Provinces, Municipalities, and Regions', in J. Dorn and Wang Xi (eds), *Economic Reform in China*, Chicago, IL: University of Chicago Press.
Field, M. (1992) 'China's Industrial Performance Since 1978', *The China Quarterly* 131, September.
Gang Yi (1990) 'Inflation and Price Instability: An Empirical Study of the People's Republic of China', *China Economic Review* 1 (2).
Garnaut, R. and Ma Guonan (1993) 'How Rich is China?: Evidence From the Food Economy', *The Australian Journal of Chinese Affairs* 30, July.
Geng Xiao (1991) 'Managerial Autonomy, Fringe Benefits, and Ownership Structure: A Comparative Study of Chinese State and Collective Enterprises', *China Economic Review* 2 (1).
Gold, T. (1991) 'Urban Private Business and China's Reforms' in R. Baum (ed.), *Reform and Reaction in Post-Mao China*, London: Routledge.
Goldberg, V. (1980) 'Relational Exchange: Economics and Complex Contracts', *American Behavioural Scientist* 23 (3).
Goodman, D. (1991) 'The Authoritarian Outlook', intro. to D. Goodman and G. Segal, *China in the Nineties*, Oxford: Clarendon Press.
— (1997) 'China in Reform: The View from the Provinces', in D. Goodman (ed.), *China's Provinces in Reform*, London and New York: Routledge.
Guanzhong, J.W. and Chui Zhang (1993) 'Investment Under Risk in Property Rights', *China Economic Review* 4 (1).
Halpern, N. (1991) 'Economic Reform, Social Mobilization, and Democratization in Post-Mao China', in R. Baum (ed.), *Reform and Reaction in Post-Mao China*, London, Routledge.

Hannan, K. (1989) 'Corruption in China: Post Reform Inequalities, Inadequate Infrastructure and a Suction Based Economy', *The Australian Quarterly* 61 (3), Spring.
— (1991) 'Economic Reform and the Fixed Asset Problem', *Access China* 1, March.
— (1995a) 'The Left Hand Doesn't Know What the Right Hand is Doing: Industrial Reform in China', *Evatt Papers* 3 (2).
— (1995b) 'Reforming China's State Enterprises, 1984–92', *The Journal of Communist and Transition Politics* 11 (1), March.
Harberger, A. (1992) 'Strategies for Transition', in C. Clague and G. Rausser, *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.
Herschler, S. (1995) 'The 1994 Tax Reforms: The Center Strikes Back', *China Economic Review* 6 (2).
Hoe Ee Khor (1992) 'China – Macroeconomic Cycles in the 1980s', *China Economic Review* 3 (2).
Honnor, C. (1994) Taxation Reforms Capital, Indirect, and Consumption Tax Changes', *Access China* 13, March/April.
Huang Yasheng (1990) 'Web of Interests and Patterns of Behaviour of Chinese Local Economic Bureaucracies and Enterprises during Reforms', *The China Quarterly* 123, September.
— (1995) 'The Strategic Investment Behaviour of Chinese Local Governments During The Reform Era', *China Economic Review* 6 (1).
Huizhong Zhou (1993) 'Bargaining and Market Decisions of State Enterprises in a Transition Economy', *China Economic Review* 4(1).
Hussain, A. (1994) 'The Chinese Economic Reforms: an Assessment', in D. Dwyer (ed.), *China: The Next Decade*, Harlow: Longman.
Jae Ho Chung (1994–5) 'Beijing Confronting the Provinces: The 1994 Tax-Sharing Reform and its Implications for Central-Provincial Relations in China', *China Information* IX (2/3), Winter.
Kelly, D. (1991) 'Chinese Marxism Since Tiananmen Between Evaporation and Dismemberment', in D. Goodman and G. Segal, *China in the Nineties*, Oxford: Clarendon.
Kemme, D. (1989) 'The Chronic Shortage Model of Centrally Planned Economies', *Soviet Studies* XLI (3), July.
Khan, A., Griffin, L., Riskin, C. and Renwei, Z. (1992) 'Household Income and its Distribution in China', *The China Quarterly* 132, December.
— (1993) 'Sources of Income Inequality in Post-Reform China', *China Economic Review* 4(1).
Kornai, J. (1979) 'Resource-Constrained Versus Demand-Constrained Systems', *Econometrica* 47 (4), July.
Korzec, M. (1988) 'Efficiency Wages and Enterprise Behaviour in China', *The Journal of Communist Studies* 4 (1), March.
Lee, P.N.-S. (1993) 'Housing Reform Under Deng Xiaoping', *Chinese Law and Government* 26 (1), January–February.
Levy, R. (1995) 'Corruption, Economic Crime and Social Transformation Since the Reforms: The Debate in China', *The Australian Journal of Chinese Affairs* 33, January.
Li Yunqi (1991) 'Changes in China's Monetary Policy', *Asian Survey* XXXI (5), May.

Liu Funian (1990) ‘Financial Reform: A Prerequisite for Development’, in J.A. Dorn and Wang Xi (eds), *Economic Reform in China*, Chicago, IL: University of Chicago Press.
Ma Guonan (1992) ‘How Large Are China’s Budget Deficits?’, *Access China* 7, September.
McKinnon, R. (1992) ‘Taxation, Money, and Credit in a Liberalizing Socialist Economy’, in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.
Meisner, M. (1989) ‘The Deradicalization of Chinese Socialism’, in A. Dirlik and M. Meisner (eds), *Marxism and the Chinese Experience*, Armonk: M.E. Sharpe.
Minghua Zhao and Nichols, T. (1996) ‘Management Control of Labour in State-Owned Enterprises: Cases From the Textile Industry’, *The China Journal* 36, July.
Naughton, B. (1991) ‘Macroeconomic Management and System Reform in China’, in G. White (ed.), *The Chinese State in the Era of Economic Reform*, Armonk, NY: M.E. Sharpe.
— (1993) ‘Deng Xiaoping: The Economist’, *The China Quarterly* 135, September.
Newbery, D. (1991) ‘The Safety Net During Transformation: Hungary’ in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.
O’Leary, G. (1992) ‘Redefining Workers’ Interests’, in A. Watson (ed.), *Economic Reform and Social Change in China*, London: Routledge.
Polumbaum, J. (1991) ‘Making Sense of June 4, 1989: Analyses of the Tiananmen Tragedy’, *The Australian Journal of Chinese Affairs* 26, July.
Pye, L. (1995) ‘Factions and the Politics of *Guanxi*: Paradoxes in Chinese Administrative and Political Behaviour’, *The China Journal* 34, July.
Rausser, G. (1991) ‘Lessons for Emerging Market Economies in Eastern Europe’, in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.
Rausser, G. and Simon, L. (1992) ‘The Political Economy of Transition in Eastern Europe: Packaging Enterprises for Privatisation’, in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.
Saich, T. (1991) ‘Much Ado About Nothing: Party Reform in the 1980s’, in G. White (ed.), *The Chinese State in the Era of Economic Reform*, Armonk, NY: M.E. Sharpe.
— (1992a) ‘The Fourteenth Party Congress: A Programme for Authoritarian Rule’, *The China Quarterly* 132, December.
— (1992b) ‘The Reform Decade in China: The Limits to Revolution From Above’, in M. Dassu and T. Saich (eds), *The Reform Decade in China*, London: Kegan Paul.
Sautman, B. (1992) ‘Sirens of the Strongman: Neo-Authoritarianism in Recent Chinese Political Theory’, *The China Quarterly* 129, March.
Selgin, G. (1990) ‘On the Importance of Decentralising Money’, in J.A. Dorn and Wang Xi (eds), *Economic Reform in China*, Chicago, IL: University of Chicago Press.
Shambaugh, D. (1993) ‘Deng Xiaoping: The Politician’, *The China Quarterly* 135, September.

Shea Jia-Dong and Yen Tzung-Ta (1992) 'Comparative Experience of Financial Reform in Taiwan and Korea: Implications for Mainland China', in R. Garnaut and Liu Guoguang (eds), *Economic Reform and Internationalisation*, Sydney: Allen and Unwin.

Solinger, D. (1991) 'Urban Reform and Relational Contracting in Post-Mao China: An Interpretation of the Transition from Plan to Market', in R. Baum (ed.), *Reform and Reaction in Post-Mao China*, London: Routledge.

— (1996) 'Despite Decentralization: Disadvantages, Dependence and Ongoing Central Power in the Inland – The Case of Wuhan', *The China Quarterly* 145, March.

Stiglitz, J. (1992) 'The Design of Financial Systems for the Newly Emerging Democracies of Eastern Europe', in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.

Sullivan, L. (1988) 'Assault on the Reforms: Conservative Criticism of Political and Economic Liberalization in China, 1985–86', *The China Quarterly* 114, June.

Tang Tsou (1995) 'Chinese Politics At The Top: Factionalism or Informal Politics? Balance-of-Power Politics Or A Game To Win All?', *The China Journal* 34, July.

Thomas, S. (1992) 'The Political Economy of Privatization: Poland, Hungary, and Czechoslovakia', in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.

Unger, J. and Chan, A. (1995) 'China, Corporatism, and the East Asian Model', *The Australian Journal of Chinese Affairs* 33, January.

Walder, A. (1987) 'Wage Reform and the Web of Factory Interests', *The China Quarterly* 109, March.

— (1989) 'Factory and Manager in an Era of Reform', *The China Quarterly* 118, June.

— (1991) 'Workers, Managers and the State: The Reform Era and the Political Crisis of 1989', *The China Quarterly* 127, September.

White, G. (1987) 'The Politics of Economic Reform in Chinese Industry: The Introduction of the Labour Contract System', *The China Quarterly* 111, September.

— (1988a) 'State and Market in China's Labour Reforms', *The Journal of Development Studies* 24 (4), July.

— (1988b) 'The New Economic Paradigm: Towards Market Socialism', in R. Benewick and P. Wingrove (eds), *Reforming the Revolution*, London: Macmillan.

— (1989) 'Restructuring the Working Class: Labor Reform in Post-Mao China', in A. Dirlik and M. Meisner (eds), *Marxism and the Chinese Experience*, Armonk, NY: M.E. Sharpe.

— (1994) 'Democratization and Economic Reform in China', *The Australian Journal of Chinese Affairs* 31, January.

Winiecki, J. (1992) 'Privatization in East-Central Europe: Avoiding Major Mistakes', in C. Clague and G. Rausser (eds), *The Emergence of Market Economies in Eastern Europe*, Oxford: Blackwell.

Womack, B. and Guangzhi Zhao (1991) 'The Many Worlds of China's Provinces', in D. Goodman and G. Segal (eds), *China Deconstructs*, London and New York: Routledge.

Wood, A. (1993) 'Joint Stock Companies With Rearranged Public Ownership: What Can We Learn From Recent Chinese and East European Experience With State Enterprises?', *China Economic Review* 4 (2).

World Bank Country Study (1992) *China Reform and the Role of the Plan in the 1990s*, Washington, DC: World Bank.

Xiaochuan Zhou (1993) 'Privatization Versus a Minimum Reform Package', *China Economic Review* 4(1).

Xiaokai Yang (1993) 'Theories of Property Rights and China's Reforms', *China Economic Review* 4 (2).

Xu Yi and Chen Baosen (1981) 'On the Necessity and Possibility of Stabilizing Prices', *Social Sciences in China* 3.

Yeh K.C. (1992) 'Macroeconomic Issues in China in the 1990s', *The China Quarterly* 131, September.

Yimin Lin (1992) 'Between Government and Labor: Managerial Decision-making in Chinese Industry', *Studies in Comparative Communism* XXV (4), December.

You Ji (1991) 'Zhao Ziyang and the Politics of Inflation', *The Australian Journal of Chinese Affairs* 25, January.

— (1993) 'Dismantling Party/State Controls in China's State Enterprises', unpublished PhD thesis submitted to The Australian National University, September.

Young, G. (1992) 'Contemporary "Socialism" and the Chinese Communist Party', *Copenhagen Papers in East and Southeast Asian Studies* 7.

Index