

The Evolution of State-owned Enterprises in South China: The Choice of Property Right System Perspective

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ABSTRACT The purpose of this paper is to explore the evolutionary pattern of state-owned enterprises in China. The researchers focused on the three state-owned enterprises of the same industry in south China that experienced diverse property right reform roads in the late 1990s and showed differing outcomes. Combined with the method of business anthropology, this paper asserts that different models of property right can affect different human behavior paths, which would produce the final destiny of the enterprise. The researchers conclude that the property right reform of Chinese state-owned enterprises in the future should be a mixed model that can achieve the governance balance.

INTRODUCTION

In the late 1990s, the Chinese economy had gone through hardship under the guidance of the premier Zhu, and one of the most important measures was carrying on the reform to the state-owned enterprises (SOEs) drastically. In this round of reform, some enterprises revived, while others disappeared. So far, leftist scholars have resolutely defended the principles of government ownership, while the scholars on the right (free market) have persisted in the principle of full privatization property right that SOEs should transform public ownership into private ownership through market transactions. This paper, based on long-term attention and in depth study of property right reform of three SOEs in south China, will compare the research achievements of the reform of SOEs in Chinese academic circles, especially under the background of the theory of full privatization by scholars is very popular. Several key questions arise in evaluating the choice of property rights system. First, is the idea of "shock therapy" feasible, directly selling SOEs in practice? Second, how does the property right of SOEs influence employee behavior, which could affect the development of enterprises? Third, what kind of property right structure can promote the better development of SOEs? And what is the mechanism of the action?

The paper is the primary attempt to answer this, and find how China's SOEs should reform after all and explore how to carry out the property right reform, which have to be consistent with era-oriented development in the process of the history of Chinese national capital control system, through in-depth studies of different property right evolution path and different outcomes in three Chinese SOEs without any theory paradigm.

Literature Review

The relevant study shows restarting the property right reform of SOEs is the key in the current China's economic development (He 2011). Hence, the property right reform of SOEs is not only a microcosmic problem, but also a macro matter. To solve the problem, it could allow human capital to share enterprises. Profits as a production element and to construct SOEs' double-layer property right system which combines public (state) ownership and staff, individual ownership is a way out (Wang 2000). To realize the diverse structure of property right of state-owned enterprise, construct the basic outlet of SOEs (Qiu 2001; Zhou 2005). To achieve this path, only through the property right trading market and the joint system of stock cooperation, promote the development of SOEs (Smyth

and Zhai 2001). Additionally, some scholars note that the reform should set out from the perspective of contract theory or from the “planned” contracts, transition to market contract, implement the worker’s labor contracts and property right of investors, entrepreneurs incentive combination, promote the development of SOEs (Zhang 2005). Based on the distinction between holding responsibility and management responsibility, to promote the reform of SOEs’ property right diversification, since that is the basis for the development of SOEs (Wang 2011; Wang 2012). Some researchers suggest that low degree of state-owned equity diversification is one of the important reasons affecting the development of SOEs, but not simple diversified shareholding reform, only through the establishment of appropriate concentration equity (He 2004). Many others believe that the direction of change is toward private ownership, and the first thing is the privatization of SOEs in the next following years (Zhang 1995). The reform and development of SOEs should further follow the principle of the market economy, and SOEs can not play the main role in the market economy any more (Yang 2013). Opposed to this view, SOEs could not carry out the reform of equity against the loss of state-owned assets, especially diversification equity (Cai 2012; Liang 2012). The reform of SOEs should be taken to the market-oriented reform, gradually form public welfare structure types and competitive SOEs, and take a different reform path and strategy (Chen 2013). Some scholars further pointed out that SOEs’ reform should stick to the socialist direction through the reform of property right system, solve the problem of internal governance of SOEs, then promote the development of SOEs (Liu 2014). Thus arises the question of how to stick to the socialist direction of SOEs, and to promote its rapid development as well? Some research has pointed out that the mixed ownership may be the correct direction of the reform of SOEs, which can optimize enterprise property rights structure, and push the balance configuration among the responsibilities, the right and the benefit (Lin 2014). Implementing the mixed ownership economy is the key to further reform SOEs, which can make SOEs’ management mechanism clear, optimize the structure of state-owned economy, break SOEs development dilemma (Shi 2014). In addition, the implementation of the mixed ownership is conducive to the improvement of the legal person

governance structure of SOEs, the efficiency of enterprise resource allocation, private capital flowing into SOEs’ reform of property rights, releasing the whole social capital to participate in the real economy.

Three streams of research can be identified due to the above studies. One stream believes that the implementation of the mixed ownership can guarantee the socialist property of the reform of SOEs, meanwhile optimizing the property right structure and governance structure of SOEs, and promote the rapid development of SOEs. Another stream advocates for full privatizations, which transform into the market enterprises by thoroughly separation from the government. The other stream highlights state-owned enterprise classification management that different strategy management should be taken to dissimilar category of SOEs to promote development, which should not be a fundamental property right reform. What is the degree of connection between these theoretical research results and SOEs’ property right running? Investigators will elaborate the path of the property right reform of SOEs in China through the quantities analysis of the sample enterprises.

METHODOLOGY

Business anthropology is a new edge discipline, which combines anthropology theory and method into the practice of business management. At present, the role of the business anthropologist has been widely recognized since the majority of problems in business administration can be solved (Tian 2012). The subject of this study is to explore the proper evolution pattern of state-owned ownership, yet there exists a big controversy in the current theoretical circle, for this reason, using business anthropology methods, investigators can obtain more in-depth research and more real and scientific conclusions including participant observation, interview, group investigation, diversity of the technologies and methods of network analysis (Tian 2010). With the department of local state-owned assets management full support, investigators obtained three sample enterprises, the model of property rights are public, mixed and private. Nine researchers participated in this study, three of whom are authors of this paper. The others are master graduate students of business administration in a southern Chinese University of tech-

nology, divided into three groups, and each group was responsible for a sample enterprise. The researchers analyzed the background of the three sample enterprises and first conducted a literature review together, and then entered into the field work to collect raw data and information respectively. At the end of each period investigators swapped research information and compare the similarities and differences, discussed and corrected the problems existing, until obtained data conforming to study expected, then took the data processing, and finally drew a conclusion.

Cases for this Study

Enterprise A absolutely persisted in socialism property right system, uniting to engage in discourse with the government against the property right reform. Workers' protests had taken place several times like other parts of China at the same period. Finally the government compromised, and the enterprise was immune from the capitalistic fate. However, under the pressure of national reform tide, the leaders of the enterprise hoped to keep up with the trend of the times: reform. So the government put forward such proposal of property right reform, socialist property accounted for 70% of enterprise equity, corporate executives and staff accounted for 30% of the enterprise equity. The overall kept socialist color. Today, the enterprise is still in operation, but the scale is shrinking year by year. Enterprise A had 650 employees before reform, but now has only 70 employees, and renting has become the main business.

Enterprise B, because senior executives could not effectively display their abilities for the long constraints of socialist property put forward such property reform to the government, enterprise managers and staff accounted for 70% of enterprise equity, socialist property accounted for 30%. The government approved such reforms. The enterprise has become better and better with 10 years of development, which currently has developed into influential aquatic products processing enterprises in southern China. The sales are both strong in exports and imports. Enterprise scale had 580 employees reform ago, to 1150 employees today.

Enterprise C, in the wave of reform, firmly resisted property of socialism through multiple negotiations with the government, finally bought

by a private boss, thoroughly capitalist. After the reform, enterprise C obtained a rapid development. Under the management of a private boss, business efficiency was greatly improved. In 2008, however, with the influence of financial crisis of the western capitalist world, enterprise C exports blocked, with sluggish sales in domestic channels, and then the problem of working capital became very prominent. Banks urged to receive their loan. These negative factors have worked on enterprise C closed from 2009 to now. At present, the boss is planning to enter into house industry by land used for workplace, in the future the area of the factory will become an upscale residential district, and enterprise C will become history.

Participant Observation

Participant observation is the primary research method in implementing business anthropology. Three study groups implemented eight management cycles of observation (each management cycle for 7 days) in fieldwork, observing the behavior of employees and senior managers. The field workers created about 265 observation records. The observation locations were the workshop, the market department, the HR department, the administration office, the financial department, and the labor union.

In-depth Interviews

In-depth interviews tend to be more quantitative and cover more subjects, which deeply explores the subject's feelings and perspectives. In the interview process, investigators selected twelve interviewees on average from each of the three enterprise samples. As to the successors and retired senior management, investigators posed the following questions: How do you perform the given tasks that the supervision and administration department of state-owned assets or the boss ordered? How does the model of property rights of SOEs help asset motivate employees' work and senior management make decision? In your career, what do you think of the reform of property right of SOEs? What kind of property right model can fully arouse the enthusiasm of your management? Do you think the pattern of property right has effect on the staff behavior, and if yes, how to affect? What do you think of the current pattern of property rights?

For common staff, investigators asked the following key questions: Does the reform of property right influence your work and your benefit? If yes, how to affect? What kind of cases will you regard your enterprise as your home. The questions aimed to obtain the association between the choice of property right of state-owned enterprise and the behavior of senior managers and staff.

In the process of interview, Investigators put ourselves as a loyal listener and focused on listening to the interviewees' special information with our talk time no more than 5% of the interview time, in addition, from time to time guiding the interviewees in our interview outline by questioning at intervals. Investigators did 44 hours and 25 minutes interview recording, resulting in 257,800 words after sorting out all these facts. The researchers made interview memos after the interview, mainly adopted interpreting (to a tentative interpretation of the results), method (to discuss method used in interview and its influence on the research process).

Data Processing

Open Coding: Converting data into concept was the first step to open coding. Investigators took materials in accordance with the category of the research subject by conceptualization process, the final were classified according to the data. Investigators logged in and wrote some analytical memos in order to increase the awareness of information. The basic principle was to our best efforts to be detailed log. In particular, the investigators focused on the words of the parties, to be named for each coding for data raised the question as much as possible, continued to compare to the relate entries and made a backup. The data reached saturation.

Axial Coding: The main task of this stage was to find and construct the relationships among concepts (for example, causality, chronological relationship, semantic relationship, situational relationship, similar relationship, differential relationship, peer relationship, type relationship, structural relationship, functional relationship, process relationship, strategy relationship, etc.). To arrange related concept first, then take category based on these relationships, and finally polymerize the concept of saturated state again, and formed sixteen categories.

Selective Coding: Selective coding category was in the process of integration and refining, which could connect each of the major categories and integrate into a larger theoretical framework. Investigators distinguished four core categories after select coding; namely, property right, behavior, efficiency, and sustainable development, which was summarized as the reform path of SOEs. Under the theoretical framework, Figure 1 presents the close relation of the key four categories. Property right as a logical starting point keeps two-way linkage in behavior, efficiency, and sustainable development of enterprises. Behavior as a logical starting point, maintains two-way linkage with property right, because specific property rights affects human's behavior choices, in turn specific behavior further strengthens the specific property right model, but behavior retains one-way linkage in efficiency and sustainable, for efficiency and sustainable development are the result of specific behavior which is determined by property right. Efficiency affects the evolution of a model of property rights and sustainable development of enterprises, yet it can not determine human's behavior choices. Likewise sustainable development impacts the evolution of a particular property right, but it can not determine people's behavior and efficiency, because it itself is results of specific behavior and efficiency.

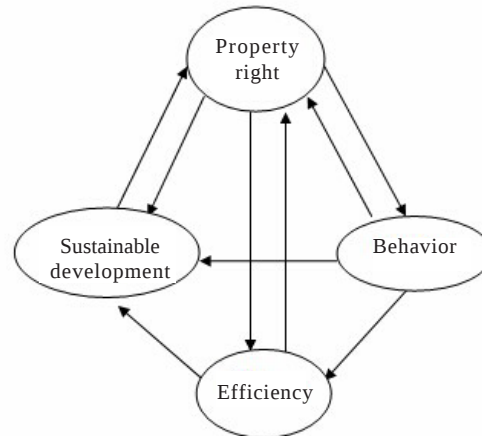


Fig. 1. The diagram of the reform path of state-owned enterprises

RESULTS AND DISCUSSION

Property right is the logical starting point in the change of SOEs. Inconsistent property right

arrangements affect the behavior options of executives and staff. Interview data can tell us that property right is how to work upon human's behavior by covering three enterprises.

Interview of Enterprise A and the Evolutionary Model of Property Right

"In the early development of the reform, we were easy to loan from banks. Cash flow was plenty. The enthusiasm of staff once was better than that in prior of the restructuring, enterprise effectiveness gradually revealed. Later more and more discrimination between the government and the enterprise executives emerged in terms of enterprise development strategy, senior managers placement, enterprise profit distribution, and so on, until the government using 70% of the big shareholders' right adjusted the enterprise management, enterprise managers had to take orders by the government."

"Enterprises returned to the previous state slowly with working enthusiasm of staff escaping. The core staff retired earlier and entered into private enterprises for high salary. Gradually, the enterprise was in financial embarrassment that capital became difficult to find. In 2004, through selling a piece of land to obtain the funds to pay off bank loans, then enterprise collapsed. Since then enterprise had been in decline."

"The most confusion problem to us in this process was corruption of the government officials, which regarded enterprise as their own

"ATM", the daily expenditures of food and drink and their personal consumption often hung on the enterprise's name, some directly to disburse as business expenses. Although we knew that was illegal, our fate was in the hands of government officials, now we are numb as to the action."

"The elder managers retired and the successors rely on rental fixed assets which can support the employees' salary right now. These managers have become secondary caretaker for government assets (the primary caretaker is the department of supervision and administration of state-owned assets). We can't see the future of the enterprise, just waiting for the government's instruction."

Investigators called the model of A enterprise's property right as "the type of government ownership", which resulted in the inertia of decisions, sequentially impacted the efficiency of enterprises, leading to poor performance which caused the loss of financial credit, until loss of sustainable development power, and the enterprise is stagnant finally. This model of property right made the government officials rich, employees poor, and the state damaged. Figure 2 provides a summary description of the evolution of the government ownership property right.

Interview of Enterprise B and the Evolutionary Model of Property Right

"Our enterprise soon entered into the speedway of development after the reform, now our

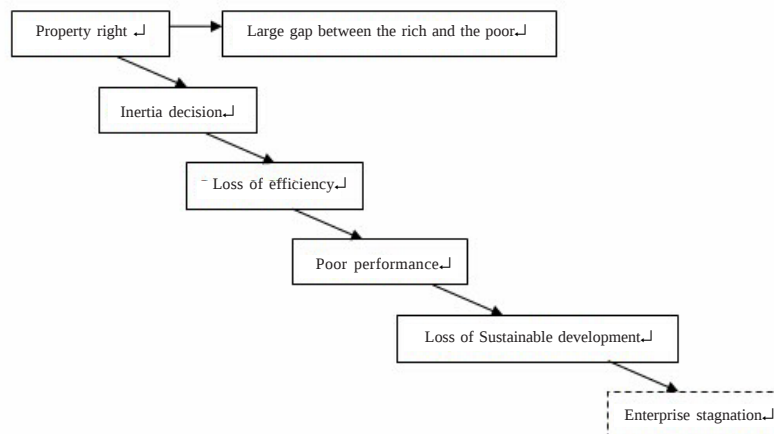


Fig. 2. The evolutionary model of the government ownership

enterprise has become an influential aquatic products processing enterprise in southern China. In our enterprise, state-owned shares is the first major shareholder, but not appear such kind of dilemma that state-owned shares control enterprise absolutely, the main reason is employees will take their own shares voting right granted to enterprise managers to perform when the department of state-owned shares to want to intervene the decisions in business running, so state-owned shares can't strongly intervene in business decision-making."

"The equity structure of our enterprise can be sure of the effective protection of the enterprise's management independent and the continuity of sustainable development strategy. Furthermore, 30% of the state-owned shares are the first big shareholders, so our enterprise belongs to the category of SOEs in the market, and this title of state-owned can bring many benefits, such as loan from banks, expanding the domestic market. After all the credit of SOEs is better than that of private enterprises, the other party would prefer to deal with SOEs under the same conditions during the transaction in the market, this is our competitive advantage."

"Our enterprise can combine with the advantage of public firms and private firms, which create the following obvious advantages: enterprise's financing, distribution channels, and social network, especially obtaining preferen-

tial treatment from the government. Reviewing my tenure, I think the reform model of property right is feasible, which the equity of SOEs is 30% while that of the staff is 70%. The structure of property right should correspond to national conditions. Our enterprise goes in the path of common prosperity that enterprise managers and employees have profit share besides salary each year. Employees generally live a wealthy life."

Investigators named the model of enterprise B's property right as "the type of labor ownership" (see Fig. 3), which aroused employee's working enthusiasm, sequentially encouraged the initiative of employee's participating decision making, continued to improve the efficiency of the enterprise, then brought inexhaustible power to enterprise development, and made credit enhanced and raised the ability of sustainable development, which made the future of enterprise optimistic. This model of property right can combine with the efficiency of private enterprise and goodwill of public ownership well, optimizing the enterprise competitiveness in the market, and avoiding functional departments of the government and enterprise executives from misbehave. It is a kind of ideal ownership structure. Meanwhile, the model also can practice the dream of the reform for common wealth by the Chinese Communist Party, which can provide reference value for the initial distribution of social wealth.

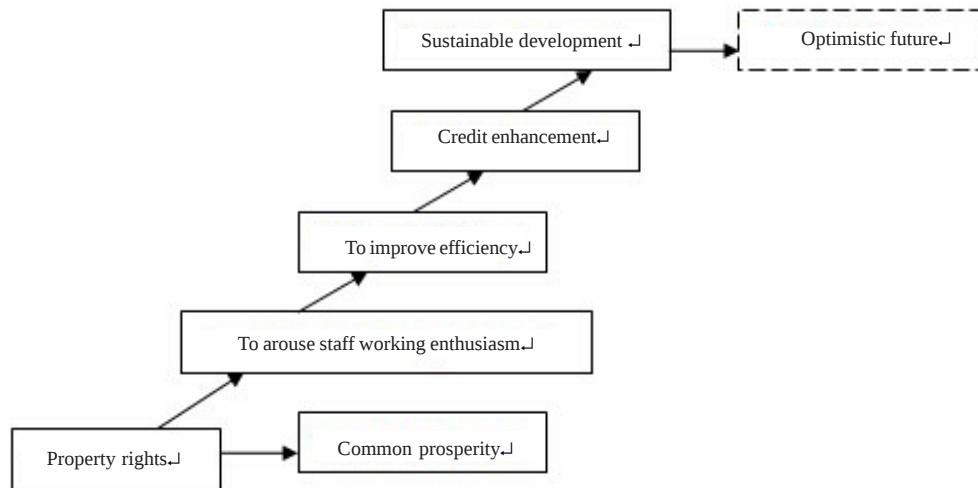


Fig. 3. The evolutionary model of labor ownership

Interview of Enterprise C and the Evolutionary Model of Property Right

"At the beginning of the reform our enterprise achieved the supernormal development, employees' pay was the highest in aquaculture industry in south China, for the reason, young men were employed in our enterprise following with a group of beautiful girls and many state-owned enterprise workers retired early to our enterprise. Our enterprise had become the local star enterprise for a period of time. Workers were proud of that."

"The managers just followed the command of the boss who was only final decision-maker, no appearing such kind of internal factionalism phenomenon and decision stalling phenomenon in SOEs."

We were concentrating on the development of the enterprise along the same direction. Nevertheless the 2008 financial crisis made the enterprise's performance bad, because our business relied on exports. Then the boss wanted to explore new business implementing diverse development strategy. But the project failed unfortunately due to the decision making. Under the pressure of internal and external forces, the enterprise had been in closed state since the end of 2009, which only retained a handful of elder managers who created the enterprise together with the boss to guard the enterprise."

"Our enterprise development can be summed up the success and failure of the affairs is due to He Xiao, the absolute power of decision-making that we all just perform what the boss only decided to will lead to the hidden dangers to the development of the enterprise, which lacked external intelligence support to decision mak-

ing. We summarized that that man's control could ruin the future of the enterprise."

"I think it is imperative to prevent the huge harm of the decision-making errors by the scientific mechanism no matter what the ownership of the enterprise is. When our enterprise developed well, banks wanted to lend to us. Now the situation has changed; our enterprise can no longer loan money from banks, unlike SOEs, and we only maintain daily cash flows through private lenders. In the aquatic products processing industry, our enterprise is very difficult to recover the previous. We plan that the factory will built a high-grade residential area, which the enterprise is about to convert to the housing completely. But the future is uncertain. The situation of Staff is bad. The boss lost money earned before, only have a worthless piece of land."

Investigators entitled the model of C enterprise's property right as "the type of boss ownership", which caused autonomous decision following high efficiency of the enterprise, but highly centralized decision could have relatively easy access to the crisis of enterprise development that the failure of projects caused the loss of credit, which brought about uncertain social wealth distribution. The model may influence social stability of the future. Figure 4 summarizes this evolution model.

CONCLUSION

The evolution model of enterprise B has been the best among the three property right models over the years. How can the property model be better to promote the enterprise sustainable development in China, and to some extent, to pre-

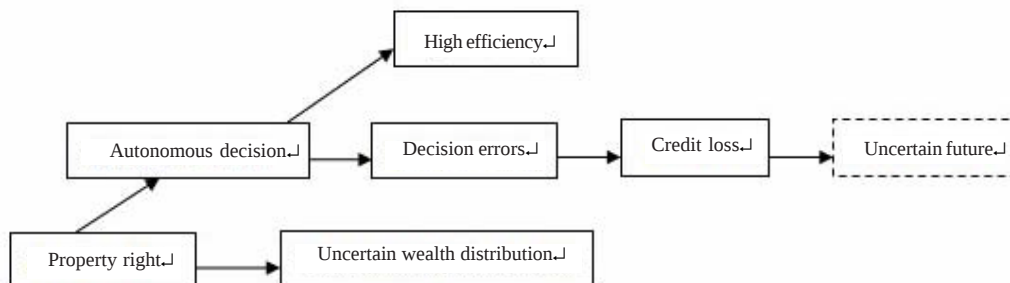


Fig. 4. The evolutionary model of boss ownership

vent the internal enterprise from large gap between the rich and the poor? Investigators think that should closely relate to the special history of the Chinese society evolution, especially the history of Chinese central government control of national economy.

Since salt and iron were run on a franchise by the western Han, each feudal dynasty of China would have controlled the power of management and operated at those aspects connected to the national economy and people's daily life supplies. The system had been continuing. Furthermore, the past dynasties should manage the industry of craft strictly; effectively manage commodity circulation system, which were the long tradition for deep participation economic operation by the government. That worked Chinese people to rely more on the government and trust state-owned economic organization naturally; yet they are filled with special fear simultaneously, for once the power of the government can't use correctly, the power of state-owned economic organizations may become tool to oppress people. The result is that Chinese people are overwhelmed by mixed love-hate feelings to SOEs, with the present being no exception.

The model of property right of enterprise B is variant from that of traditional SOEs, and also that of private enterprises, which is a hybrid model that not only can meet the desire for the efficiency of private enterprises, but the nostalgia for the advantages of SOEs. It can provide a psychological safety net within the workplace and incentive staff positive behavior, which can bring an important reference to the property right reform of Chinese SOEs in the future.

RECOMMENDATIONS

Today, we should think about this issue from diverse perspectives, such as the history of system evolution, the development of the history, and so on, rather than the only way to eliminate SOEs when investigators discuss the reform of SOEs in China. China can not live without SOEs, because not only SOEs are an important means to control regional political power for the past dynasties, but an important means to ensure central authority. The decline of the previous dynasties in the economic performance attributed to weaken the central government control of the economic, while the ability of the original economic rising. Furthermore, the investigators think

that the existence of the SOEs, especially central government-led enterprises, is the key factor to ensure control the whole situation by the government. The central government should be difficult to control and command the local without the power of SOEs, and then the state should be of unrest.

The case study results reported in the current study provide a useful first step toward a more advanced understanding of the correlation between the choice of property right and the path of human behavior in the reform of SOEs. Future investigations should explore the new property right structure with more flexible ways, which can take the advantages of SOEs, meanwhile absorb the essence of private enterprise. Only that can the new model of property right promote the development of national economy.

In addition, investigators believe the following factors should be taken into account in the reform of SOEs. First, to build a "firewall" can define the supervision and administration department of the state-owned assets and executives of SOEs through legislation, which can avoid excessive intervention for decision making by the government. Alternatively, by the introduction of "host system" the third independent party is in charge of supervising the equity of SOEs on behalf of the government. Second, it is imperative to establish a semi-closed channel development for senior executives of SOEs. Currently, the senior executives of state-owned enterprise are appointed from the government officials who can also be transferred back to the government simultaneously. This placement should result in executives' teams of SOEs to be unstable, affecting the continuity of strategy management. Investigators believe that the development of semi-enclosed channel establishment is very important that the government officials can be assigned to SOEs, but not transferred to the government again. This can not only keep executive team stable and ensure continuity of the strategy, but constrain managerial opportunism.

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