

EC2374

Economy of Modern China

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Topic 3 (cont) Urban & Industry

Reforms & development of urban China

- China's industrialization
- urban industrial reform
- corporate governance
- future prospects

Topic 3 (cont) Urban & Industry

China's industrialization

- a late comer: did not occur after 1949
 - Big push industrialization
 - Acceleration during the reform through
- **Industrialization, reform, and restructuring**
 - Marketization, decentralization, economic opening
 - Restriction on labor movement remains
 - Change in ownership composition and industry mix
 - Trade and FDI significant

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urban industrial reforms

- pre-reform system

- state-owned and urban

- 1978: SOEs accounted for 78% of industrial output & 76% industrial employments

- the rest by rural and urban collectives, owned by local govts

- resources were allocated by administrative means

- prices set by govt

- profits remitted to govt as revenue dual track pricing

- the govt's control over resources was less central than USSR

- fragmentation across regions

- limited trade across administrative regions

- vertical integration

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urban industrial reforms

- 1978 to mid-1990s
 - existing hierarchical relationships remain
 - introduce market incentives
 - “profit retention” => “contract profit-loss responsibility
 - dual track pricing
 - introduced “tax for profit”
 - more reliance on market and less price distortion
 - encourage new forms of firms
 - rural collectives
 - private and household
 - foreign invested enterprises

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urban industrial reforms

- 1978 to mid-1990s: incentive and autonomy
 - rapid increase in output
 - especially in non-state sector
 - export expanded rapidly: FIEs and TVEs
 - some improvement in productivity
 - modest improvement among SOEs
 - more market-oriented business environment
 - growing competition
 - declining subsidy
 - hardening of budget constraints

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urban industrial reforms

- post-1996: real restructuring
 - forced by increasing financial difficulties
 - restructuring SOEs to improve profitability
 - lay off large number of workers
 - “grasping the large, and letting the small go”
 - central government vs. local governments
 - maintain control of resource related, capital intensive industries & public utility
 - various ways to restructure
 - corporatization, privatization, bankruptcy, and mergers and acquisition
 - provide a uniform legal framework
 - Company Law (1994)

Share of SOEs and SHEs, 2008

	# of firms	total assets
mining and washing of coal	9%	76%
extraction of petroleum and natural gas	37%	96%
smelting and pressing of ferrous metal	4%	60%
smelting and pressing of non-ferrous metal	6%	45%

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urban industrial reforms

- post-1996: real restructuring
 - rapid growth continued, except in employment
output, export, labor productivity, and product quality
 - increase in market-oriented business behavior
rapid expansion of foreign-invested enterprises
accelerated growth of domestic private manufacturing
Increasingly commercial orientation of state-controlled corporate groups
 - FIEs become significant in many industries
garments, instruments & meters, electronics & telecommunications, textiles, etc.
Integrating Chinese industry with the global business community
more standard practices observed

Share of FIEs in respective sectors, 2008

	# firms	output	asset	VA	emp	EX
Overall	18%	30%	26%	27%	29%	69%
Smelting and Pressing of Ferrous Metals	8%	14%	12%	12%	9%	18%
Manufacture of communication equipment, computers and other electronic equipment	42%	81%	70%	77%	74%	92%
Manufacturing of raw chemical materials & chemical products	15%	27%	28%	29%	15%	49%
Manufacturing of transport equipment	19%	45%	38%	48%	28%	51%
Manufacturing of electrical machinery & equipment	22%	35%	35%	36%	40%	68%
Manufacture of Textile	18%	23%	28%	24%	25%	47%
Manufacturing of apparel, footwear & caps	37%	42%	46%	48%	50%	62%

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corporate governance

- definition
 - a concept characterizing the contractual relation between different members of a firm, including shareholders, managers, and employees
- objectives
 - provide a good incentive structure for short-term as well as long-term business operation
 - provide an effective management selection mechanism

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corporate governance

- the state sector post1996
 - establish modern corporations
 - separate non-core functions of SOEs
 - lay-off workers/shut down factories
 - corporatization
 - joint-stock corporations/limited liability companies
 - state oversight through board of directors
 - objectives:
 - strengthen autonomy
 - profit maximization
 - protect public ownership/interest

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corporate governance

- the state sector post1996

- corporatization in practice

- slow and uneven in improvement

- established SASAC in June 2003

- oversight based on profit and productivity

- monitoring of managers: lack of constraints

- managerial abuse: asset stripping

- dividend payment to the state

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corporate governance

- SASAC [State-owned Assets Supervision & Administration Commission]
 - act as the owner of state assets
 - protect the value of government assets
 - dispatch supervisors to audit and monitor
 - appoint members of boards of directors
 - establish procedures for appointing managers
 - approve major decisions including merger, bankruptcy
 - report enterprise performance to government
 - local SASACs established for local SOEs
 - also regulatory body: issues rules & regulations

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corporate governance

- Challenges for SASAC
 - Conflicting roles and objectives?
 - as representative of the owner
 - as monitor
 - as regulator
 - Administrative/financial power
 - In relation with government ministries
 - In relation with the large SOEs
 - Conflict of interest

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future prospects

- challenges facing Chinese industries
 - government, SOEs, and market
 - increasingly more market-oriented behavior
 - government administrative intervention
 - weak implementation of rules and regulations
 - increasingly powerful interest groups
 - market fragmentation and weak industrial structure
 - local protectionism
 - low concentration
 - over capacity and low competitiveness

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future prospects

- challenges facing Chinese industries
 - industrialization reaching its limit?
 - Lewis turning point
 - worker shortage problem
 - industrial upgrading & endogenous growth
 - technology capacity: R&D investment
 - heavy reliance on foreign technology
 - constraints on low-tech manufacturing

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future prospects

- challenges facing Chinese industries
 - State vs. non-state industries
 - heavy reliance on external demand
 - weak economic prospect of western economies
 - weak domestic consumer demand
 - weak corporate governance
 - select capable manager
 - formulate effective short-term and long-term incentive
 - evaluation of business performance

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future prospects

- the way forward?
 - the proper role of government
 - relations between SOEs & central/local governments
 - industrial policies vs. competition policies