

AN INQUIRY INTO THE PRIVATIZATION OF THE CHINESE STATE-OWNED ENTERPRISES

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1. The function of the state-owned enterprises

Today, state-owned enterprises have always been a painstaking problem for their deficiency. However, since there exist such problems as natural monopoly, externally economic & uneconomic problems, and the effect of scale economy in this world, certain degree of the existence of state-owned enterprises will still be in necessity. It makes up for the market failure for its publicity and sociality. We can not completely deny the function of state-owned enterprises simply because of its widely admitted malpractice. In order to maximize social interests, it is necessary for government to control certain parts of industry that are suitable to manage by government. However, government should absolutely withdraw from those industries that are not fit to manage by government. To a formerly central-planned economy like China, however, the main task that government is facing with at present is how to withdraw from those inefficient government-controlled industries. We may call this process privatization.

2. The Inevitability of making the state-owned enterprises privatized

The Inevitability of the privatization of the state-owned enterprises: The world in which we live is in constant changing. As a country's development period changes, part of the state-owned enterprises will finish their historical mission, and it is the goal of profit become the prime managing purpose. In order to improve the operating efficiency of state-owned assets or property rights, it is indispensable to sell parts of the property rights to different individuals and organizations in the background of a market economy. Hence, the task of privatization of the state-owned enterprises ensues. Practice proves that the idea that only the government's solo-capital investment ventures can preserve the nature of public ownership is at least unilateral if not wrong. A Path-breaking event is that the 15th session of Chinese Communist Party's representatives meeting has made a new definition on the realization of the public

ownership: solo-public-capital investment ventures is not the only way of realizing the public ownership; public-capital-controlled ventures (government capital share is in dominant position among the capital shares) is the other way of realization of public ownership. This has officially open up a path for state-owned enterprises to be privatized. Today, most of the state-owned enterprises are open to outside capitals of any form to form cooperate or joint-ventures. Realization of public ownership may take various forms such as advantage stock holding; disadvantage stock holding. Ownership selling out is also an important way to privatize the state-owned enterprises.

3. strategic thinking on the privatization of the state-owned enterprises:

From the perspective of nature of products and services the industry provides, we can divide the whole industry into two parts: competitive industries and monopolistic industries. In China, monopolistic industries are usually those fields that are of critical importance to the national economy such as transportation, telecommunication, resources exploitation, energy production, and military industry, et. Other industries are competitive. For the purpose of social benefit and national safety, and in terms of the Chinese specific national situation, government should still keep a certain degree of control over them. These industries are not among the lines to be privatized.

Those industries that are not suitable to be privatized yet bear following characteristic:

- 1) The industries for which managing principles are not market-oriented. For example, money printing and military uniform manufacturing industries can not accept the marketing signaling. They can only be directed by the government dictation.
- 2) The industries whose products can not be merchandised. Gold, some rare metals, and some special resources, they can not be taken to the market for free exchanging.
- 3) The industries prices of whose products and services are regulated by government rather than be determined by market in certain time and under certain conditions, These industries include such basic industries as postal industry, public utility industry water and electricity supply, railways, et.
- 4) The industries concerning national security.

According to the statistical data in 1996, state-owned enterprises are losing money in the following industries:

money unit: RMB yuan

	MARKET OCCUPIED	OUTPUT QUOTA	NUMBER OF FIRM	TOTAL FUND	TOTAL ASSET	TOTAL PROFIT
	(%)	(million)		(million)	(million)	(million)
FOOD INDUSTRY	43.7	37912	5306	13011	56300	-15.1
CLOTHING	6.8	10214	1102	3271	14618	-0.91
LEATHER PRODUCTS	10.9	8155	847	2968	15355	-2.97
WOOD PROCESSING	21.5	7140	1265	4457	17835	-3.52
FURNITURE PRODUCING	8	2018	594	732	3391	-0.11
EDUCATION& SPORTS	12.2	3970	527	1181	6558	0.36
PLASTICS	12	13945	1609	5411	23735	-0.64
METAL MANUFACTURES	16.8	22789	2507	8178	43956	-2.84
TEXTILE	39.2	182533	4345	48408	267195	-60.28
OTHERS	8	5678	1092	1911	8232	-1.43
TOTAL		294354	19194	89528	457175	-87.44

Government can start the privatization process with these money-losing industries, and then expand the process gradually from the less profitable ones to profitable ones.

1. Privatization of the Chinese state-owned enterprises: methods and stages

In China, the history of reform of the state-owned enterprises is actually the history of privatization of the state-owned enterprises. Looking back into the history, the outlines of the stages of privatization become more and more distinctive. It can be divided into two periods:

- 1) Contracting out system period: the primary stage of privatization.
- 2) Auction or stock transferring period: advanced stage of privatization.

The primary stage has past by now. Contracting out system is the main way of privatization in 80's. On the one hand, since not demanding drawing a clear line on the property rights between that of the managers(lessee) and that of owners(government), this method was not politically sensitive, and was therefore carried smoothly. On the other hand, however, just because it does not concern the problem of property rights, It was and could only be a transitional way often used during the primary period of economic reform in socialist countries. Today, China has already stepped on the advanced stage, the stage of auction and stock transferring period. By issuing stocks in the secondary markets, government uses one stone kill two birds:

- (1) Raising money to make new investments in the firms that has long been in badly

needs of money for technical transformation and improvement;

- (2) More importantly, condoning the stock holding structure in the firms which is the most urgent and important task for changing the old management mechanism into the modern enterprises' management mechanism. What is more worth mentioning, for the enterprises that are not yet well prepared for issuing stocks in the public stock market, Chinese people have in practice created a novel form of ownership called "internal stock holding cooperation system" by way of which the company can be shared by all the employee within the company through holding a certain amount of stocks each. As a transitional method, this kind of institution is a very effective way for both transforming the managing mechanism and the property rights structure in state-owned enterprises. It is a creative way of privatization adaptable to the Chinese situation.

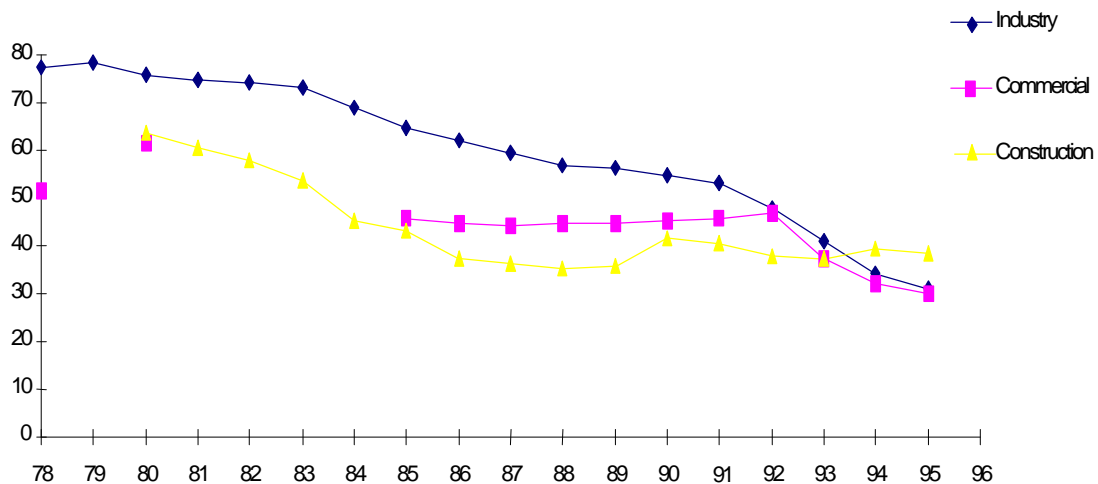
As far as those "totally hopeless" state-owned enterprises are concerned, claiming bankruptcy, reckoning the assets and selling them partly or auctioning them as a whole is necessary. This method is applicable to those small or medium sized state-owned enterprises which account for the most part of the state-owned enterprises in quantity. However, at present, this method could not be carried out extensively for two reasons:

- (1) A big enough private fund for buying the state-owned enterprises should be already existed in society before an enterprise can be sold; For example, if you want sell a car out, the precondition is that there should be someone who can afford it and want to buy it.
- (2) A market of managers that can provide enough qualified managers should be already existed. This is indispensable for good management. However, neither of these two preconditions can be sufficiently satisfied in China at present. Further, whether an auction can be carried out or not also depends on the comparison of these two relative values: the auctioning cost and the value of the auctioned enterprise. If the former value is greater than the latter one, auction itself will be meaningless. Even though there are so many obstacles in the way, things change quickly for better these two years, specially after the 15th session of representative meeting of Chinese Communist Party in 1997.

The program of privatization characterized by contracting out and auctioning has been carrying on smoothly since 1980's, and it has made outstanding achievement.

According to the " World Bank Report On World Development In 1996", the Chinese gross productivity (total productive factors) has been increased by 3 percent each year from 1985-1995 , which, by the international standard, is a very rare phenomenon. This means that one third of the increased output since 1985 should be attributed to the improvement of the efficiency of the whole economy. We will be surprised at the implication of this datum when we relate it with the fact that the proportion of the state-owned enterprises has been falling down during the same period. This is mainly the achievement of privatization.

Following graph interprets downward tendency of the ratio of state-owned enterprises (including manufacturing industry, commercial industry, and the industry of construction) in the whole national economy from 1978 to 1995.



If this tendency keeps on, by the end of this century, the total output of the state-owned enterprises will only account for 20 percent of the whole industry output.

Reference Materials:

- (1) From Plan to Market-----A World Bank Report on the World Development in 1996
- (2) (China Yearly Statistic Data) 1996
- (3) A Study on The Reform Strategy of State-owned Enterprise, Zhi-Yi He, 1996