Analysis and Discussion of the Problems in the Process of State-owned Enterprise Reform

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Abstract

The reform of state-owned enterprises is an important aspect and a central focus of the socialist market economy reform. State-owned enterprises are categorized into monopolistic and competitive entities. Some state-owned enterprises with natural monopolies require a high level of government supervision and policy support, while other state-owned enterprises with low industrial concentration need to relax control to enable them to actively engage in market competition. At present, China's state-owned enterprise reform has entered the fifth stage of mixed ownership reform. With the intervention of non-state capital and the marketization of state-owned enterprises, the economic performance of state-owned enterprises has also improved, enabling them to better fulfill their social responsibilities. However, at both theoretical and practical levels, the reform of state-owned enterprises still encounters numerous challenges. These include policy burdens and insider control, employee incentives and innovation development, management buy-outs, and the loss of state-owned assets. This paper argues that state-owned enterprises still need to deepen market-oriented reforms, especially focusing on internal incentives and innovative development issues, in order to continuously enhance the operational efficiency of enterprises.

Keywords

State-owned enterprise reform, policy burden, employee incentive, management buy-out

Since the reform and ‘opening up’, with the steady progress of China's economic system reform, the reform of state-owned enterprises has become the central link of the economic reform and transition led by the government. To delegate benefits and expand enterprise autonomy as a starting point, the reform of state-owned enterprises has experienced the decentralization, power separation, modernization, shareholding system, and mixed ownership reform stage, the implementation of the modern enterprise system reform in 1993 (laid-off tide), strategic restructuring, state-owned assets supervision and a series of reform measures, gradually refined reform goal, strengthen the reforming power, achieved certain results (Yudong Qi et al., 2019). The central corporate social responsibility blue book, according to 2009 top 100 enterprise social responsibility development index below 30 points, and in 2020, the number, rose to 58.9 points, shows that in the reform process of Chinese enterprises in responsibility management, market responsibility, social responsibility, environmental responsibility in areas such as performance is more and more bright eye. According to the State-owned Assets Supervision and Administration Commission of the State Council, in 2011, 69.38% out of the top 500 companies in China were state-owned, accounting for more than half. In 2020, out of the top 500 Chinese enterprises, only 48 were state-owned, indicating a decline in state-owned enterprises. This trend shows that the state-owned economy is gradually making room for the private economy. Nevertheless, the reform of state-owned enterprises still faces many problems, which still have room for discussion in theory and practice. At the present stage, China's state-owned enterprise reform is in the stage of mixed ownership reform. For this reform, on the one hand, scholars represented by
Wu and Zhang believe that property rights reform is the core of state-owned enterprise reform, while scholars represented by Justin Yifu Lin believe that the most important thing of state-owned enterprise reform is to remove the policy burden (Zhang Hui et al., 2016). Through the summary of the previous literature and the verification of the actual situation, the author concluded that the reform of state-owned enterprises.

1. Policy burden and insider control problems are superimposed

State-owned enterprises due to their state-owned nature must face budget soft constraints, the problem's most fundamental reason is the burden of strategic policy and social policy, the former requires the government to focus on developing capital-intensive or technology-intensive strategic enterprises, while the latter requires state-owned enterprises to undertake employment and improve social welfare social functions (Lin, 2004). To some extent, some state-owned enterprises cannot effectively participate in the market competition. Therefore, SOE reform needs to weaken the impact of the policy burden on SOE. But in essence, the property rights arrangement itself principal-agency mechanism makes the enterprise, managers have a moral hazard problem: in the case of two rights separation, the interests of the owners and operator are usually inconsistent, and the information asymmetry and incentive incompatibility problem, this leads to the business operators for personal gain in the possibility of policy burden. This problem further led to the emergence of insider control, including the phenomenon of “revolving door”, senior executive adjustment, pan-administration (Qi Yudong et al., 2019), and internal friction caused by the power struggle of internal personnel (Zhang Weijing, 2000). In fact, state-owned enterprises are not simply economic organizations, but also political organizations, undertaking political functions is an important function of state-owned enterprises, such as the decisive role in the basic industries that regulate the national economy and people's livelihood, mainly includes the network industries (including power, telecommunications, aviation, railway, natural gas and water industries).

2. Employee incentive and innovation development face obstacles

Centralization cannot provide incentives (Qian Yingyi, 1999), while lack of incentives causes innovation. The most important purpose of the reform of state-owned enterprises is to stimulate them to participate in the market economy competition and achieve innovation-driven development while improving employees and social welfare. Liu Ye et al. (2016) pointed out by analyzing the data of Chinese industrial enterprises that the mixed ownership reform of state-owned enterprises in competitive industries can significantly improve the efficiency and total factor productivity (TFP) of state-owned enterprises, and intellectual property protection can also have an extremely positive impact. Pan et al. (2022) conducted a long-run empirical testing, which demonstrates that the privatization of China's state-owned enterprises has a significant positive impact on enterprise innovation by reducing agency costs. However, the reform is still facing such as central-local disharmony, and there are "hidden rules" in the organization. On the one hand, the wine table culture of state-owned enterprises is still prevalent, and the grass-roots workers are exhausted in all kinds of social parties and wine tables, while the main responsible work content is not substantially expanded and improved. On the other hand, the management is solidified, and a considerable number of managers occupy the management positions for a long time, and the dead positions are vegetarian. However, grassroots employees lack promotion channels for a long time, restrain their work enthusiasm, and form a negative situation of connection between the upper and lower levels. This is not good for enterprises to improve business performance, complete specific assessment indicators, and realize the value appreciation of state-owned enterprises, and will also inhibit the innovation of enterprises. In 2021, the resignation of SMIC Liang Mengsong attracted attention. In this case, the contradiction between technology-based state-owned enterprises for research and development personnel and managers is worth pondering. How to introduce, make good use of, and retain talents in state-owned enterprises may be another level of innovation and development.

3. Management buy-out (MBO) leads to the loss of state assets

The new regulatory system for the reform of state-owned enterprises is mainly based on capital management, and a three-tier regulatory framework has been established from the SASAC to the state-owned capital investment and operation companies to the state-owned enterprises (Liao Hongwei et al., 2018). Although facing the opportunistic risk of regulators, the three-tier structure (Figure 1) has also effectively reduced the intervention of state-owned assets regulators in the operation of state-owned enterprises, weakened bounded rationality, and reduced transaction costs. But at the same time, due to the limitations of state-owned shareholders in some competitive areas, in the process of adjusting the layout of the state-owned economy, China's state-owned enterprise reform introduced the management buyout (MBO).
However, the measure is controversial, the most famous of which is the "Lang Gu dispute." Lang Xianping believes that MBO will erode state-owned assets, but Gu Chujun believes that the management’s becoming a shareholder will help improve the efficiency of business operations and achieve the interests of owners and operators. Most of the controversy has focused on the loss of state assets, the reasons can be summarized into three points: First, since the interests of the central and local governments disagree, local governments may conspire with local state-owned enterprises to circumvent central regulation, for example, the MBO case, lead to the loss of a large number of state-owned assets (Zheng Hongliang, et al., 2018); It is difficult for management to match the purchase price fully with the asset price of state-owned enterprises. On one hand, managers have an incentive to underestimate state assets. On the other hand, there are difficulties in measuring the assets of state-owned enterprises themselves. These factors often result in management buy-out prices being lower than the actual value of state-owned assets. This discrepancy can lead to the loss of state-owned assets (as seen in 2016). Additionally, the lack of a perfect bidding mechanism can lead to the widespread occurrence of discount trading phenomena (Zheng Wei, 2013). Furthermore, irregularities, insider trading, and management risks are present. Management can also reduce the acquisition cost by deliberately decreasing the net asset value per share during negotiations (Zheng Wei, 2013).

Figure 1. The three-tier structure of state-owned enterprise supervision.

4. Conclusion

In general, the reform of state-owned enterprises is the only way for China's economic system to reform. This process has become long and difficult by taking into account the regulatory mechanism, property rights arrangements, policy burden, innovation incentives, and other issues. After more than 40 years of trial and error and exploration, the reform of state-owned enterprises in China has achieved some results, but the nature of state-owned enterprises itself leads to many problems facing state-owned enterprises are still difficult to solve. A considerable number of central enterprises have been listed in the world rankings, but how to coordinate the contradictions between central enterprises and local state-owned enterprises and how to solve the regulatory evasion caused by information asymmetry still needs to be explored.

Based on promoting the property rights reform and optimizing the management, how to realize the innovation incentive is also an important issue. The case of SMIC Liang Mengsong has attracted much attention to the conflict between R&D personnel and managers in state-owned enterprises. In addition, the promotion channels and incentives for employees still need to be solved. At present, the reform of state-owned enterprises has been implemented for three years (ended) and five years of action. Only by "focusing on the big and releasing the small" and constantly learning and trying new ways and methods of corporate operation can we achieve steady and long-term development.

On the whole, the current state-owned enterprises can be improved from the following five aspects: (1) Strengthen the financial statements and budget audits, and promote the transparency of the company system. (2) Integrate with major national strategies in line with China's national conditions, such as rural revitalization, green sustainable development, and the Belt and Road strategy, and promote development cooperation. (3) Effectively connect various industries and enhance the service role of people's livelihood and well-being. (4) Simplify enterprise management procedures,
and promote enterprise flat management. (5) Enterprise managers should establish a good personal image and enhance social ties.

The reform of state-owned enterprises needs to consider reform, development, and stability, promote efficiency and social equity. This is essential not only to enhance the pivotal role of state-owned enterprises in the national basic industry but also to uphold the responsibility and mission of fostering world peace and stable development. It is crucial to truly achieve 'clear property rights, delineated powers and responsibilities, separation of government and enterprises, and scientific management'. Promoting the reform and development of the Chinese economic system can be achieved through the reform of state-owned enterprises. State-owned enterprises are representatives of China's economy and the main connection between China and other countries. The reform of state-owned enterprises can also promote the stability of the world economy through exchanges and cooperation among countries.

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