

Chapter 2

Government, Enterprise, and Entrepreneur: Are These Relationships the Primary Productive Force?

Economic growth without enterprise development would be like a pond without a source of water, while enterprise development without entrepreneurs would be like a bow without an arrow. In modern China, the growth of entrepreneurs and development of enterprises is related to government under the market economic system.

A series of studies discussed in this chapter focused on how enterprise development and entrepreneur growth are linked by the relationships among governments (government officials), enterprises, and entrepreneurs. Numerous predecessors and their research have paved a road toward understanding the modern market system. This system is simply defined in traditional economic theories as the price mechanism of free competition, but now increasing importance is attached to non-free competition and non-price mechanisms in the market. In particular, the price mechanism of free competition is, by no means, a useful framework for entrepreneurs because it is only applicable to homogeneous commodities or factors in huge quantities, and entrepreneurial ability has never been valued by the price mechanism of free competition. Governments and their officials play an important role in elements beyond the market system or price mechanism, while entrepreneurs connect governments and enterprises. Chapters 3, 4, and 5 consist of three mutually independent empirical studies of the interactive relationships among governments, enterprises, and entrepreneurs.

This chapter has three sections. Section 2.1 presents theoretical analysis of the duality of the government–enterprise relationship and the market system. In Sect. 2.2, we analyze our survey data as well as enterprise survey data of the All-China Federation of Industry and Commerce (ACFIC) (2007) to show the development of Chinese enterprises (mainly private enterprises) and the history of entrepreneur growth, and to provide preliminary evidence for the interactive relationship among governments, enterprises, and entrepreneurs. In Sect. 2.3, we explore the role of the market system and government–enterprise relationships in economic development.

2.1 Government–Enterprise Relationships

In this book, we build an analytical framework to examine the interactive relationships among governments, enterprises, and entrepreneurs; the framework has three parts (see Fig. 2.1). Enterprises and governments are two of the three most important aspects of the market system,¹ so the government–enterprise relationship constitutes the first component part of the analytical framework.

The simplest model of a market system is based on a traditional economic analytical framework, which is most importantly characterized by anonymous market transactions and the neutrality of the market system toward individuals in that market. Government provides institutions and resources (including public goods) to enterprises, while the latter offer the former tax revenue and political achievement. At this stage, government does not act in opposition to the market, neither control nor intervene in it, or concern itself with dangers to its operation. The government is highly likely to promote the market mechanism and contribute to economic development if it is a “market-augmenting government” instead of one that tends to represent the interest of any special group (Olson 2000).²

However, markets have never been anonymous—in ancient or modern times. According to political economics, a government is made up of specific officials who are rational doers with individual interests. At the same time, enterprise organizations should have a personalized representative—the entrepreneur. The interactions between individual representatives of government and enterprise constitute another profile of the government–enterprise relationship and of the market system, and are largely ignored in traditional economics. The standard government–enterprise relationship reflects the anonymity of the market system. A government official allocates resources that are useful to the development of the enterprise through his interaction with the entrepreneur. Of course, some government officials are unselfish, while others are engaged in rent-seeking activities and gain various direct and indirect interests from enterprise development when they are allocating resources. Entrepreneurs are aware of the importance of political connections and thus also actively participate in the administration and discussion of state affairs and build connections with government. Meanwhile, through their political connections they also get various resources to be used for enterprise development. The relationship between entrepreneur and government official generates trust networks different from market relationships or mandated economic relationships. They are principal-agent relationships among actors who control asymmetrical resources and promote the alliance of mutual interests (Wank 1995). Interaction between a government official and an entrepreneur is entirely

¹The remaining behavioral subject is the consumer of commodities, who is also the worker in the labor market.

²Yao (2008) summarizes the success of China’s economic development by the concept of “neutral government,” the essence of which reflects a “market-augmenting government.”

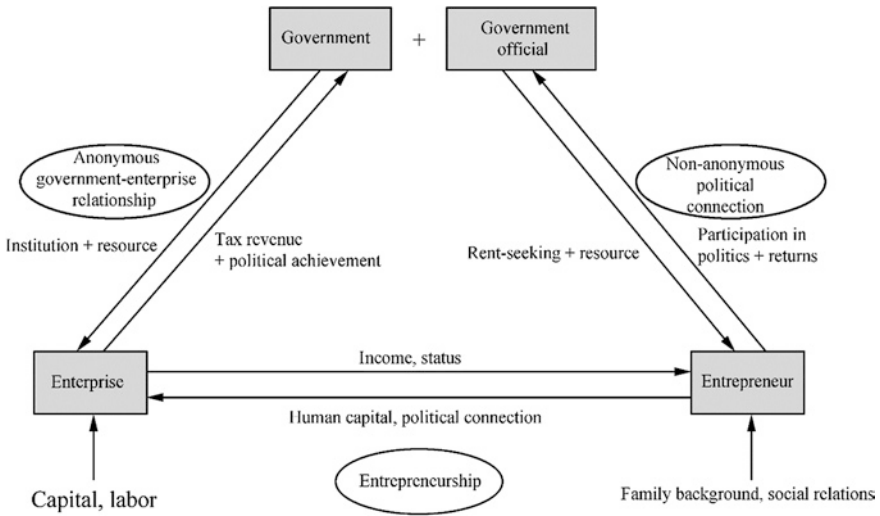


Fig. 2.1 Relationships among government, enterprise, and entrepreneur

individualized. In this sense, the market system is nonanonymous and no longer neutral toward individuals. In other words, the process of resource allocation by the market is also a process of inequality generation due to entrepreneurs having different political connections.

The anonymous and nonanonymous features of the market system can never be overemphasized. The government provides institutions and resources to enterprises, and those resources in essence are allocated under an institution designed by the government. The government determines the dos and don'ts for entrepreneurs by institutions and policies. The problem is that the boundary between "do" and "don't" is very ambiguous due to a very simple economic reason. That is, any institution depending on language and text incurs costs, which will be increasing, but its marginal benefits are decreasing, when all details are clearly defined. The revelation of all details of the institution means that some phenomena targeted will most probably not occur or that the designer of the institution will not be able to predict what will happen. Therefore, it is nonoptimal and unnecessary to cover all the details by the institution. As a result, the institution is born imperfect, because it has "loopholes" and "gaps." Some new unexpected things appeared in the loopholes and gaps during the period of major economic development. Two entirely opposite interpretations naturally existed though they were not designed to exist by the institution. One is that what is not prohibited by the institution can be done, and the other is that what is not allowed by the institution cannot be done. The evolution of an institution invariably lags behind the reality and stipulates post-event dos and don'ts. Those people who are bold enough to break prohibitions may create history and become heroes if their behavior is eventually recognized, but it may also be deemed illegal and these people may be imprisoned if their

actions are recognized as don'ts. More importantly, the boundary between do and don't changes as people's concepts change. An illegal thing in one period is likely to be recognized later as legal. There are many examples of this in the era of great reform in China. The history of the development of Chinese enterprises and of reform and opening-up is a story of constant adjustments to the boundaries between do and don't.^{3,4}

Enterprises particularly depend on government policy for development when the boundary between do and don't is vague, while rent is generated because the government (or a government official) has the right to decide and interpret that boundary. Government officials, no matter in Zhejiang, Guangdong, or Beijing, decide (or acquiesce in) which things can be done at many critical moments, reserving great room for enterprise development. Sometimes government officials also take individual political risks.⁵ The most direct way to help enterprises is for government to share control and earnings with enterprises, and the most outstanding example of this is to wear the red hat of collectivism in township enterprises (become collective enterprises).⁶ According to a survey in the mid-1990s, 33 % of 13 rights of management of township enterprises were "entirely decided by district and township government," 33 % "co-decided by government and enterprises" and the remaining 34 % "independently decided by enterprises" (Chen 1995). Many private enterprises have put on a red hat. According to a joint questionnaire by the Center for Private Economic Studies under the Chinese Academy of Social Sciences, Horizon Market Survey and Analysis Company and the Information Center of the ACFIC, surveyed private entrepreneurs believed red-hat enterprises accounted for 50–80 % of collective enterprises in 1993, and 50 % private entrepreneurs in a survey of 360 private enterprises believed such a proportion was roughly between 30 and 50 % in 1994. A sampling survey by the State Administration of Industry and Commerce in 1994 indicated that 83 % of township enterprises were private. In the same year, statistics gathered by authorities in Dongyang City, Zhejiang province, show that counterfeit collective private enterprises accounted for more than 70 % of collective enterprises. These data were sourced from Dai (2005) who also lists different instances of private enterprises taking off the red hat. As private property rights under the red hat are not legally

³Many enterprises and entrepreneurs naturally push history forward in the process of historical evolution with many blurred areas and ups and downs. Maybe it would be more suitable to write such history in literary rather than economic language. For a history of such enterprises, see Wu (2007).

⁴De Soto takes ownership, as an example, in *The Mystery of Capital* to illustrate the following truth. "Law must stay in harmony with people's practical lifestyle. The precondition for vitality of law is to keep in touch with various social contracts that have taken shape in reality." (de Soto 2000, Chinese translation, p. 84). The reason why some countries are underdeveloped is that the law in these countries ignores social contracts in reality and consequently a large amount of capital fails to "legally" create value (de Soto 2000).

⁵Take Zhongguancun in Beijing as an example. There were many debates among intellectuals in the 1980s on the wisdom of enterprise establishment in Zhongguancun which received crucial support from the Beijing municipal government and Haidian district government (Ling 2007).

⁶Weitzman and Xu (1994) call such a right to control "ambiguous property right".

protected, some enterprises were successfully transformed, some confiscated, some suspended or closed down by the government, and some entrepreneurs were “dismissed” or even sentenced to imprisonment. Government seemed to hold power over the life and property of enterprises and entrepreneurs. Solinger (1993) argues that to a great extent that China depends on state regulation or control over property rights. By better understanding property right as the right to use and keep earnings as well as to own goods (resources), it is clear that no fundamental change has happened today to change governments’ attitudes to property rights and the operation of the market mechanism. Here, to Solinger “today” refers to 20 years ago, government’s regulation and control on the market is still a character of modern Chinese economy.

Government also directly or indirectly controls and allocates resources by various means. Some resources controlled by government are “dominant,” such as government accounting and finance, and some are “recessive,” such as market monopoly of some state-owned enterprises.

Government financial resources and procurement are “big orders” in any country, and any enterprise which gets such resources will achieve great development. Lenovo, a widely known Chinese computer producer, once encountered fierce competition from foreign branded computers. Chuanzhi Liu, Chairman of the Board and Chair of the Executive Committee of Lenovo Group Limited, once lobbied the Ministry of Electronics Industry and “hoped to develop industry procurement policies in favor of the development of national industries and preemptively buy homemade products under the same cost performance.” With support from the ministry, Lenovo frequently outbid transnational corporations in seeking government procurement.⁷

Government strictly control financial resources. It is more difficult for private enterprises to get financing in the regular financial system and banks have for a long time adopted discriminatory loan policies against private enterprises.^{8,9}

⁷See Wu (2007) Volume II, p. 47 for Lenovo’s story.

⁸Financing difficulties faced by private enterprises and SMEs, in particular, are sometimes attributed to the non-standard behavior of enterprises, such as incomplete loan applications and non-transparent internal financial information.

⁹Wu (2007) tells the story of how private enterprises seek development under government control. As he puts it in one note on p. 109 of Volume I of this book, “What is contrary to Wenzhou is Shanghai—the biggest commercial city in China.” It is characterized by the strongest planned economy and the strictest government control, where local private enterprises still lacked the dynamic for growth in the early 1990s. According to China Business Times on January 18, 1992, the Shanghai Municipal Financial Office still issued No. 287 Document in 1991 to clearly prohibit products of private enterprises in Shanghai from “entering into major and famous stores in the Nanjing Road and Huaihai Road.” Not one of the 2,195 private enterprises in Shanghai was allowed to establish joint ventures with foreign companies because “there was no example in Shanghai”. Banks in Shanghai were “banned from granting loans to private enterprises” and credit cooperatives were only allowed to grant loans to private enterprises worth less than RMB3,000 by mortgage of negotiable securities or guarantee of strong state-owned enterprises.

Table 2.1 Views of urban residents on the greatest population divisions

Group with greatest difference	Frequency	Proportion	Cumulative distribution
No answer	17	0.29	0.29
Don't know/Not clear	405	6.87	7.16
Between the poor and the rich	1,934	32.81	39.97
Between officials and common people	2,448	41.53	81.51
Between urban and rural residents	218	3.70	85.21
Between people with and without property	229	3.89	89.09
Between managers and the managed	210	3.56	92.65
Between well-educated and poorly educated people	330	5.60	98.25
Between workers and white collars	103	1.75	100.00
Total	5,894	100.00	

Data source CGSS data 2003 and authors' calculations

The development of the stock market has long been regarded as a means for state-owned enterprises to avoid such a problem. A reasonable explanation for such discriminatory policy is that state-owned enterprises undertook to offer guarantees of employment during the period of transformation and this distorted finance allocation. As well, financing preferences favoring state-owned enterprises at some cost to efficiency were the result of a policy choice that struck a balance between growth and stability (Chen 2004a, b).

Administrative monopoly of state-owned enterprises related to government represents a recessive resource and may be leveraged by enterprises. Huawei, a well-known private telecommunications equipment supplier, is a good example of this. It turned its telecommunications office into its "partner" through a "joint venture" with local telecommunications administrations across the country and easily sold its products to "joint-venture enterprises" in the mid- and late 1990s. National financial resources were used to buy Huawei products, enabling joint-venture enterprises to share high profits and the employees of telecommunication bureaus to enjoy increased income.¹⁰ Given the important role played by government, it is no wonder that more than 40 % of China's urban residents believe the greatest population division is between "officials and the common people," and this difference does indeed rank No. 1 among various population divisions (Table 2.1).

When researching government–enterprise relationships, we read an inspiring article entitled "From Feud to Family and Network Capitalism" written by Boisot and Child (1996).

Some key quotes from their article include:

An economic organization model characterized by close connection between government authority and enterprise keeps emerging in many economic fields in China ... The relationship between government department and enterprise is regulated by market mechanism in the economic models in other societies, while connection between them is managed and

¹⁰See Wu (2007) Volume II, pp. 97–100 for the story of Huawei's joint ventures.

intervened into by man-made administrative order or interaction in China ... Independent administration among different industries or regions is maintained due to a combination of government function and enterprise management realized by interpersonal communication and consultation.

Market-oriented private enterprises have to rely on their own efforts because they operate under tough budget constraints and thus remain small size with inadequate investments. Many Chinese private enterprises have attempted to make up the shortcoming by seeking close connections with local governments, but they often fail to get enough support. They have to pay a ‘management cost’ for market access and policy protection provided by local government or register their enterprises as collective enterprises to obtain more support (Kraus 1991; Nee 1992) ... The major personal relationship in China lies in local governments rather than in other enterprises.

The state does not institutionalize a society which standardizes behavior and transactions based on informal traditional customs.¹¹

“Chinese tradition supports a close industrial alliance of government officials and local authorities.” “Western governments stipulate rules and externally standardize market operation, while the Chinese government directly engages in transaction fields instead of formally defining internal and external differences, which are consequently interpreted by potentates who can make interpretations at will.” “Decentralization of authority directly leads to a family-based, localized and inter-personalized institution order instead of generating a market economy in the specific traditional social organization in China where an effective coded rule (legal institution) is absent.”

Traditional Western views argue that the property right is regulated by law in democratic societies, while property right is guaranteed in the relatively informal process in the social and economic network community of in China.¹²

According to common understanding, the government’s role will be gradually replaced by the market mechanism, which is only one familiar aspect of the process of marketization. As Nobel economics prize winner Joseph Stiglitz wrote in the foreword to Karl Polanyi’s classic work, *The Great Transformation: The Political and Economic Origins of Our Time*: “Polanyi reveals the myth of the free market: no genuine free and self-regulated market has ever existed. Governments of industrialized countries played a positive role in their primary transformation.” He also lightly satirizes the role of privatization in transforming economies: “Privatization is very easy: all that we should do is to allocate properties to our friends and expect rents from them” (Stiglitz 2007). Unfortunately, cases of “allocating properties to friends” also occurred in China. We once studied some cases of corruption in the process of enterprise transformation and found that managers of Chinese state-owned enterprises also leveraged relations with specific government departments or officials to manipulate the process to gain profits under a seemingly fair market mechanism (Lu et al. 2008).

¹¹“Informal traditional customs” in China include acceptance of the role of government in a market system.

¹²Quotations from Chinese translation in the pp. 43–86 of Li and Zhang (2005).

The third relationship we study is that between enterprise and entrepreneur. Entrepreneurs earn income from enterprise development; and as proved by our empirical studies, entrepreneurs of larger enterprises can lay a foundation to gain higher social status and more political resources. However, entrepreneurs are also crucial to the development of enterprises. This is a cut-and-dried matter in management science, but the attention of economic researchers into the factors that determine enterprise success has shifted to the entrepreneur in recent years. J.B. Say stated around 1800 that entrepreneurs “transfer resources from fields with low productivity and output to fields with high productivity and output.”¹³ In 1911, Joseph Alois Schumpeter emphasized in the *Theory of Economic Development* the importance of entrepreneurs to economic development but after that mainstream economic theories virtually ignored entrepreneurs. For a long time, economic researchers have established a basic framework of analysis of enterprise performance built from input factors (including capital, labor, and human capital), productivity (including scale economy), and institutional environment. According to corporate governance theory, an enterprise’s governance structure significantly affects its performance, while the entrepreneur only succeeds under a corporate governance structure and incentive mechanisms. In this approach, heterogeneity among entrepreneurs is given little importance.¹⁴

Managerialists are naturally dissatisfied with the cold-shouldered attitude of economists toward entrepreneurs. As Drucker (1985, Chinese translation, p. 24) sneers: “Classical economics optimizes existing things, which is consistent with present mainstream ideas of economic theories (including Keynesianism, as well as Friedman’s monetarist school and the supply-side economics). It pays attention to giving fullest play to existing resources and tries its utmost to build equilibrium. It classifies ‘entrepreneur’ into ‘external forces’ together with climate and weather, government and politics, plague and war as well science and technology because it cannot explain ‘entrepreneur’. Of course traditional economists (regardless of their school or doctrine) do not deny the existence of these external forces and acknowledge their importance. However, these external forces are excluded from their studies and cannot be interpreted and explained by their model, equation or prediction.”

There is a profound cause behind the indifference to the entrepreneur’s role in traditional economic theory or neoclassical price theory; this reason is also a basic issue in economic theory. Market simulation by neoclassical price theory is mainly based on analysis of supply and demand. For suppliers, enterprises mainly differ in their production costs. When prices change, those enterprises having a higher supply cost can enter the market when prices go up, and on the contrary, those same enterprises will leave the market when prices fall. Enterprises with lower production costs are more likely to earn higher profits in an institution of market competition. What factors contribute to differences in enterprises’ production costs?

¹³This translation is quoted from Drucker (1985), p. 19.

¹⁴See literature review by Bertrand and Schoar (2003).

Traditional economic theories summarize them as technology and size. Where do differences in technology and size come from? This question is not thoroughly studied in traditional theory, nor differences among actors discussed in price theory. Consequently, differences among entrepreneurs are not considered important.

Another more profound issue is that traditional price theory basically assumes any resource can be priced by the market on the condition that the value of the resource is estimated in advance. Economists eventually became aware that price value may depend on price in turn. The quality of one commodity can be roughly judged by its price when information is asymmetrical (Stiglitz 2007). Similarly, the effort made by an enterprise manager hinges on his remuneration when information is asymmetrical. As a result, designing an effective mechanism to stimulate entrepreneurs (managers) to make greater efforts and pursue profit becomes an important topic in economic studies. However, where does difference in enterprise performance come from, if we assume for the argument that all entrepreneurs are the same, if enterprises only need to design an incentive mechanism? Moreover, the incentive mechanism is important because it is impossible to get information about entrepreneur ability in advance and differences in enterprise performance can only reflect entrepreneurs' abilities *ex post* and under similar incentives. It is no wonder that the issue of the entrepreneur is not addressed in traditional price theory because an entrepreneur's ability cannot be priced in advance.

Economists have finally started to consider and study entrepreneurs. Unlike managerialists who directly measure entrepreneurs' characteristics to explain differences in enterprise performances, most economists still stick to the original analytical framework in their empirical studies when determining enterprise performances, with enterprises' input factors, governance structures and institutional environments remaining the most fundamental variables taken into account. Labor and capital used by enterprises feature strong homogeneity due to huge quantity. Labor can be controlled in empirical studies despite its heterogeneity (e.g., education). Other differences in enterprise performance will depend on the entrepreneur's ability if differences in corporate governance and institutional environment are controlled. The contribution of an entrepreneur to an enterprise relies on his human capital, social capital, and political connections. Obviously, an entrepreneur's human capital exerts an influence on enterprise development, as our empirical studies have proven. Comparatively, an entrepreneur's social relationships and political connections represent brand-new perspectives in the latest research.

Social relationships are important at least in the early stages of economic development. Li (2003) and Dixit (2003) argued that market transactions were based more on relationships than rules in the early stages of economic development due to the narrow scope of transactions, but a "relationship-based society" contributed to maintaining the low cost of market transactions. A rule-based society will have one "scale economy" effect to stipulate and implement rules and a relationship-based society¹⁵ transforms into a rule-based one when one rule that is developed

¹⁵Another common term for a relationship-based society is "acquaintance society."

may be applicable to more and more transactions as improvements are made in economic development and expansion of market transactions. Wang (2005, 2006) further proposed that “market scope determines the form of contract.” He theoretically described the following process of economic development: people make transactions across markets in the early stages of economic development when market scope is narrow. To put it simply, a transaction relationship may exist between two people in the market in different times, which can be understood as an “interconnected relational contract.” Rational calculation crosses time and markets in a traditional society with narrow market scope. A man may suffer a loss in one transaction but will be compensated from his counterparty by a transaction at another time in another market.

Entrepreneur growth and enterprise development naturally depend on relationships in a relationship-based society. Djankov et al. (2006) studied Chinese, Russian, and Brazilian entrepreneurs and found they were more likely to have other entrepreneurs among their relatives and friends. Social relationships are invariably related to blood relationships and geographic connections. In China, family and clan connections play very important roles in the development of township enterprises which can leverage these connections to increase unity, trust, and opportunities. Private township enterprises achieve stronger development in regions where family and clan connections are stronger (Peng 2004). One prominent feature of social relationships and blood connections is the development of family enterprises, which are actually not unique to China but are a worldwide phenomenon.¹⁶ Many scholars have argued that familism in social and economic development in China is in conflict with modernization. However, Whyte (1996) states that the Chinese family is not necessarily a resistant force against development. “Overall change to the Chinese family model reduces some characteristics seeming to generate resistances to modern economic activities and increases more positive characteristics,” Whyte argues. “Entrepreneur familism” is still playing a role in China.

“Relationship” in China has two meanings. One is that transactions are often made based on relationships and contracts are invariably implemented by relationships; the other is that relationships with people having special rights means additional resources in a hierarchical society and thus social relationships are combined with political connections. These two meanings are uniform in Chinese society, but the latter involves asymmetry of power in such a hierarchical society. It becomes very difficult to define gain and loss in the cross-space, relationship-based contract which is consequently difficult to put into written form and be verified and implemented by a court. This is when ethics become very important. Ethics refers to important codes of conduct to be followed by all members of society and cannot be used to judge stakeholders’ gains and losses in one event at one time. As a result, enacting ethics is flexible and many rational results may appear—such as multiple equilibria. Consequently, authority becomes very important in a relationship-based

¹⁶See summary of relevant studies in collected papers by Li and Zhang (2005).

society, which chooses and judges by selecting from multiple rational results. We can understand why traditional society is somehow characterized by autocracy and rule by man as long as we understand the importance of authority in a relationship-based society. In Chinese history, family authority undertook a responsibility to maintain internal family ethical norms, while the emperor maintained national ethical norms. Family authority, at macro-level, accords with government authority at state level. Narrow market scope contributes to a relationship-based society, which is maintained by authority, laying a “micro foundation” for intervention in and control over the economy by government.

Political connections become special relationships and thus are useful to enterprise development. The influence of an entrepreneur’s political connections on enterprise performance is a global phenomenon, and the importance of political connections is self-evident in China’s economy in which government power intervenes in numerous market behaviors. The influence of Chinese entrepreneurs’ political connections has been proven in empirical studies in Chinese and English literature in recent years. Primarily, from the perspective of financing behavior, Hu (2006), Yu and Pan (2008) concluded that enterprises with political connections were more able to procure larger and longer loans than those without political connections. First, Fan, Rui, and Zhao (2008) found that compared with listed enterprises without political connections, the liability ratio of listed enterprises having relationships with corrupt officials significantly decreased after corrupt officials were arrested, which led to a fall in share price. Second, in respect to tax, the political background of enterprise executives who once held government positions led to tax preferences being given to enterprises (W.F. Wu, C.F. Wu, and Liu 2008a). Enterprises’ preferences in finance and tax are also embodied in their business performances. Li et al. (2008) found private entrepreneurs who were Party members helped enterprises obtain loans from banks or other policy institutions and were trusted more by the legal system, and these factors promoted enterprise performance. Government–enterprise connections played a stronger role in the regions, where the market system and legal protection were weaker. Similarly, W.F. Wu, C.F. Wu, and Rui (2008b) stated that work experience of private enterprise executives in local government increased corporate value in the regions where government intervention was prevalent. The stronger the government intervention was, the more positive the influence was.

However, some studies have found that the government backgrounds of executives of Chinese listed enterprises (most samples were state-owned enterprises) led to decline in business performance instead of an increase in corporate value because enterprise leaders with political backgrounds were appointed to better address local unemployment and financial issues without relation to enterprise characteristics (Fan, Wong, and Zhang 2007). According to empirical observations, the positive role of government–enterprise connections in enterprise development better explains why private enterprises are keen on building government–enterprise connections by participating in state affairs (Li, Meng, and Zhang 2006; Chen, Lu, and He 2008).

Our studies have found that an entrepreneur who was a deputy to the National People’s Congress and CPPCC member did bring higher profits to his enterprise (see Chap. 3). Moreover, perhaps participation by entrepreneurs in state affairs is

a growing trend because of the benefits brought to the enterprise by the entrepreneur's political connections. This applies to members of various senior government bodies and to entrepreneurs whose parents were government officials, while entrepreneurs' education seems to be insignificant (see Chap. 4).

Below is a conversation between Ming Lu, one of the authors of this book, and an entrepreneur:

- Ming: You are a deputy to the NPC and member of several local CPPCCs. Are entrepreneurs now keen on participating in state affairs and, if so, why?
- Entrepreneur: To be frank, maybe it is useless for entrepreneurs like me to participate in state affairs. Very professional knowledge is required to develop policies and we don't know much about them. Why do we participate in state affairs? On one hand, entrepreneurs are more willing to pursue social status after they accumulate wealth. On the other hand, entrepreneurs can contact different platforms after participating in state affairs. The higher level of political participation is, the higher the level of people we contact.
- Ming: Do you think political participation is conducive to enterprise development?
- Entrepreneur: Of course, yes. An entrepreneur may be cold-shouldered when he asks others to help if he is not a CPPCC member or a deputy to the NPC. However, entrepreneurs who are CPPCC members or deputies to the NPC are on an equal footing at the meeting with other members, especially government officials, who will immediately always help us.
- Ming: Do you see entrepreneurs as being keen on participating in the administration and discussion of state affairs?
- Entrepreneur: Local entrepreneurs spare no effort in doing that.

Institutions shape human behavior and one behavioral model will become a convention and a culture after being repeatedly observed. What really control human behavior are conventions in life. The behavioral model for most people is actually "evolutionary stable equilibrium." To put it simply, an individual who deviates from the behavioral model may suffer loss. In regard to government–enterprise relationships, political connections are used to gain private interests and corruption will develop when resources are allocated by public power and not all people get equal access to resources. Corruption is likely to become an "evolutionary stable equilibrium" in society when it becomes a behavioral model for most people. Djankov et al. (2006) researched Chinese, Russian, and Brazilian entrepreneurs and found those in Russia and China more frequently believed it was reasonable to accept or pay a bribe in some circumstances. They found that 36 % of Russian entrepreneurs and 22 % of non-entrepreneur respondents believed it was reasonable to accept or pay a bribe. 21 % of Chinese entrepreneurs and 8 % non-entrepreneur respondents thought the same. There was no significant difference in attitude toward bribery among entrepreneurs and non-entrepreneur respondents in Russia and China where tolerance to bribery was high. Fifty-six percent of Russian entrepreneurs and 25 % of Chinese entrepreneurs believed bribery was reasonable to some extent. In China, entrepreneurs were more optimistic about the efficiency

of courts than non-entrepreneur respondents and argued that local government was friendlier toward entrepreneurs and fostered a better business environment. Compared with Russian and Brazilian respondents, the Chinese spoke highly of the attitude of governments at all levels to entrepreneurs. The research also found that an enterprise will achieve faster growth and expansion when its entrepreneur forces changes to local government rules by means of bribery.

Our studies found, like other studies, that an entrepreneur's education and political connections brought more profits to enterprises. At the time of writing, enterprise development depended more on the entrepreneur's personal resources and decisions. We found that an enterprise makes higher profits if the decision-making of its entrepreneur is dictatorial and directive. A dictatorial decision can improve efficiency of the decision-making in an economy featuring an irregular institution, complicated information, and rapid development, although it may lead to mistaken decisions. For larger enterprises, directive decision-making is more conducive to increasing enterprise profits and entrepreneurs with better education are more able to leverage directive decision-making to increase enterprise profits (see Chap. 3).

Close government–enterprise relationships represent an environment for survival and development of Chinese enterprises and entrepreneurs in the transformation period, in which entrepreneurs are in an embarrassing situation. On one hand, they obtain government support and resources when they build political connections and thereby accelerate enterprise development. On the other hand, they suffer from the burden of government intervention. We used a satisfaction indicator to comprehensively evaluate entrepreneurs' psychological status. We found that higher income indeed brought greater satisfaction to enterprises, but at the same time, the satisfaction of entrepreneurs who believed governments imposed increasingly heavier burdens on enterprises was significantly lower. In this sense, entrepreneurs earn income, status and greater satisfaction by leveraging political connections to obtain conditions and resources conducive to enterprise development, but they pay a price for that. At the same time, middle-aged entrepreneurs with better education are more likely to feel greater satisfaction (see Chap. 5).

See Fig. 2.1 for the analytical framework of interactive relationships among governments (government officials), enterprises, and entrepreneurs. Data will be further discussed in the next section.

2.2 Government, Enterprise, and Entrepreneur: Findings Based on Surveys

The relationships among governments, enterprises, and entrepreneurs are explored in Sect. 2.2 based on our survey and survey results of the All-China Federation of Industry and Commerce (ACFIC). Only survey studies on private enterprise development that have been constantly conducted by the federation since 1993 can dynamically reflect those relationships during China's reform period despite the

existence of many other research projects. A large quantity of rare data and information was collected by biennial survey studies and published in 2007 (ACFIC). We make cross-stage comparisons in this section based on 2007 survey data from the federation instead of reviewing the development history of private enterprises based on all the data for the following two reasons. First, in terms of the research theme of this book, it is stated in 1990s literature that “there exists an economic organization model characterized by close connections between functional government departments and enterprises in China” (Boisot and Child 1996) and that alliance of entrepreneurs and government officials “is rooted in interpersonal relationships among government, enterprise, and entrepreneur who are familiar with and trust each other” (Wank 1995). Therefore, we hope to know whether the relationship between governments, enterprises, and entrepreneurs has changed significantly over past 10-plus years. Second, survey data of the ACFIC (2007) are only available with information about cross-time changes to relationships among governments, enterprises, and entrepreneurs, and this information has not been fully sorted and analyzed in present publications to demonstrate the cross-time changes of relevant characteristics. “Nationwide survey” in this book means the survey by ACFIC (2007).

Our survey data were sourced from an enterprise survey by Fudan University in Liuzhou, Guangxi, in 2006, which targeted four districts and three counties (Liujiang, Luzhai, and Liucheng) under the jurisdiction of Liuzhou city. We distributed 1050 questionnaires, with 250 in each of four districts, 20 in Luzhai county, 20 in Liujiang county, and 10 in Liucheng county, according to the proportion of enterprises in those areas. In the end, 831 correctly filled out questionnaires were examined. The questionnaire gathered personal and family background information on entrepreneurs and basic information on their enterprises.

Table 2.2 shows the reasonable distribution of survey samples. About one-third of the enterprises were engaged in manufacturing and most were non-state-owned. State-owned enterprises only accounted for 2.43 %. Three-quarters of the enterprises had registered capital below RMB1 million; and profit-making enterprises made up 56.2 %.

2.2.1 Entrepreneur Growth

Our survey data and large sample survey data of private enterprises nationwide reported by ACFIC (2007) share very similar distribution. Among our survey samples, male entrepreneurs accounted for 75.77 % and females 24.23 %. The most concentrated age distributions were 41–50 years old (39.92 %) and 31–40 years old (31.71 %). In the 2006 nationwide survey, male entrepreneurs made up 85.8 %, females 14 %, and entrepreneurs aged 33–57 accounted for 87.5 %. Both our survey and the ACFIC survey indicated that about half of entrepreneurs had college diplomas or above. Most entrepreneurs we surveyed had college diplomas or above (55.78 %), followed by high-school diplomas (23.96 %) (see Table 2.3). In the

Table 2.2 Basic information of survey samples (%)

Industry composition	Agriculture, forestry, animal husbandry, and fishery	3.73	Type of ownership	State-owned	2.43
	Finance, insurance	0.80		Collective	6.39
	Mining	1.20		Private	49.68
	Real estate	8.67		Joint venture	2.43
	Manufacturing	34.53		Limited liability	28.35
	Social services	8.53		Shareholding	9.96
	Electricity, gas, and water production and supply	0.67		Foreign-invested	0.38
	Health, sports, and social welfare	0.93		Hong Kong-, Macau-and Taiwan-invested	0.38
	Construction	1.73	Size	Mega	8.54
	Education, culture and art, and radio, film and television	1.06		Large	16.13
	Geological survey, water conservancy	0		Medium-sized	29.36
	Scientific research and comprehensive technology service	0.40		Small	45.97
	Transport, warehousing, posts, and telecommunications	2.40	Profit	Profit-making	56.20
	Wholesale, retail, catering	14.93		Balanced	21.90
	Other industries	20.42		Loss-generating	21.90

Notes A mega enterprise has registered capital above RMB5 million, a large enterprise between RMB1-5 million, a medium-sized one between RMB0.5-1 million, and a small enterprise below RMB0.5 million

Table 2.3 Composition of entrepreneurs' education

	Above elementary school	Elementary school	Secondary school and junior vocational school	High school and high vocational school
Quantity	10	17	138	195
Proportion (%)	1.23	2.09	16.95	23.96
	Junior college	Undergraduate	Postgraduate (master)	Doctor-postgraduate
Quantity	276	159	16	3
Proportion (%)	33.91	19.53	1.97	0.37

Data source Authors' survey

Table 2.4 Degree of education of private entrepreneurs (1993–2006)

Survey year	1993	1995	1997	2000	2002	2004	2006
High school (vocational school)	35.9	38.1	41.7	39.2	41.9	33.6	36.6
University (junior college included) and postgraduate	17.2	18.4	20.2	38.4	38.4	51.8	49.3

Data source ACFIC (2007)

Note Survey data is for previous year before the year mentioned and similarly hereinafter

Table 2.5 Entrepreneurs' foreign language proficiency

	Proficiency in more than two foreign languages	Proficiency in one foreign language	Average proficiency in one foreign language	No foreign language proficiency
Quantity	13	44	253	464
Share (%)	1.68	5.68	32.69	59.95

Data source Authors' survey

nationwide survey (2006), entrepreneurs having a high-school diploma accounted for 36.6 % and those having college diplomas and above for 49.3 %. An entrepreneur's education was a key indicator of the entrepreneur growth. As shown in Table 2.4, there has been a significant improvement in the level of education of entrepreneurs, particularly in the proportion receiving college education and above. Chen (2005) also reported the trend of significant increase in the average years of education of private entrepreneurs from the 1980s to the early twenty-first century.

Our survey also included information that reflected entrepreneurs' human capital from other perspectives. First, as proficiency in a foreign language becomes more important in opening up China, our information indicates that about 40 % of entrepreneurs believe they can learn at least one foreign language to the average level (see Table 2.5).¹⁷ Meanwhile, we observed that many entrepreneurs have received other types of education or training in addition to common school education. As shown in Table 2.6, about 6 % of entrepreneurs have gained an MBA and more than half have received training in economic management and leadership.¹⁸ In addition, many successful entrepreneurs were once in the army. China Economic Weekly (Issue 30, 2004) listed the top 10 demobilized-soldier entrepreneurs in its cover article, including Chuanzhi Liu at Lenovo, Shi Wang at Vanke, Zhiqiang Ren at Huayuan, Zhengfei Ren at Huawei, Yonggang Zheng at Binbin and Zexian Xu at COSCO Property. The story provided a business directory of an additional 40 successful entrepreneurs who were former soldiers. In our report, 8 % entrepreneurs

¹⁷Language reward has been studied in some recent literature. Generally, foreign language proficiency leads to higher income (Berman, Kevin, and Erez 2003; González 2005; Christofides and Swidinsk 2008).

¹⁸However, no studies have been done on whether entrepreneurs received such management education and training before or after they become entrepreneurs, which is an important issue in evaluating the role of such education and training in an entrepreneur's ability.

Table 2.6 Entrepreneurs' training and experience

	Valid answered questionnaires	Respondents answering "Yes"	Share (%)
Participated in domestic and foreign courses and have a diploma	758	45	5.94
Participated in business training in economic management and leadership	794	429	54.03
Joined in the army	782	63	8.06
Went to work in the countryside and mountainous areas	790	165	20.89

Data source Authors' survey

report on their army experience. Admittedly, it is unclear whether an entrepreneur's army experience contributes to enterprise development although it may be suggested that it helps to improve an individual's sense of organizational discipline and may influence his management as an entrepreneur.¹⁹ Some studies have shown that the experience of educated youths going to work in the countryside and mountainous areas (*Shangshan Xiaxiang*) during the Cultural Revolution may influence their later performance, including their income. Such experience may cultivate a spirit of struggle under adverse circumstances and help youths build more extensive social networks. Whether a future entrepreneur's experience of working in rural areas contributes to enterprise development is yet to be studied.²⁰ About 21 % of entrepreneurs in our survey once worked in rural areas.

Experience has been considered an important component of human capital after that concept was introduced to economics. In particular, some enterprises can only obtain specific human capital by learning from experience (by doing) not by school education. Experience obtained in work is of great importance to entrepreneurs. As well as experience measured by working years in the general literature, we observe entrepreneurs' work experience in the industry and at the enterprise to measure their specific human capital. On average, entrepreneurs had worked for more than 8 years at the enterprise or in that industry before joining the enterprise. In Chap. 3, we note that 23.63 % of valid samples of enterprises had a history of 3–5 years, 37.47 % enterprises 6–10 years and 24.40 % 10–20 years; and 75.59 % of entrepreneurs participate in the establishment of their enterprise. As a result, we infer that many entrepreneurs directly participated in the development of the enterprise (Table 2.7).

¹⁹Huawei under the leadership of Zhengfei Ren is a typical case of military management. However, the questions of whether an entrepreneur's army experience influences his behavioral model and whether military management is conducive to enterprise development are yet to be answered.

²⁰Interestingly, some reports have found that some private entrepreneurs have enthusiastically sent their children to military camps in recent years, such as a report by Xinhuanet on November 10, 2004, entitled *Entrepreneurs Send Their Sons to Army*, (http://news.xinhuanet.com/mil/2004-11/10/content_2200528.htm) as well as a report by Xinmin Evening News on December 12, 2006 entitled, *Enthusiasm for joining the army appears in New Economic Organizations in Shanghai*.

Table 2.7 Entrepreneurs' experience

	Valid answered questionnaires	Mean value
Working years in the industry before joining the enterprise	672	8.12
Working years at the enterprise	760	8.56

Data source Authors' survey

2.2.2 Enterprise Decision-Making

The importance of entrepreneurs and their decision-making to enterprise development is expounded in Sect. 2.1. Decisions made by entrepreneurs are centralized in China due to rapid change and uncertainty about the environment for enterprise development. Indeed, more than 40 % of entrepreneurs in our survey said important enterprise decisions in human affairs, production management, income and welfare allocation are made by senior leaders, and more than one-third of enterprises said the decision-maker in these three categories was a leader (see Table 2.8).

Series surveys by the All-China Federation of Industry and Commerce (2007) suggest the change trend of decision-maker of private enterprises. Generally speaking, both important business decisions and general management decisions are made by the entrepreneur or major investor. The board of directors increasingly plays a role in enterprise decision-making, but survey data from 2006 indicated that more than one-third of enterprises responded that the entrepreneur or major investor is an enterprise's decision-maker and that those enterprises have always outnumbered enterprises whose decisions are made by the board of

Table 2.8 Enterprise decision-maker

	Human affairs		Production management		Income and welfare allocation	
	Respondents	Share (%)	Respondents	Share (%)	Respondents	Share (%)
Senior leaders	323	44.37	298	41.27	293	40.92
Group leadership	243	33.38	247	34.21	262	36.59
Employee collective	20	2.75	16	2.22	29	4.05
Functional department	54	7.42	81	11.22	50	6.98
Relevant government department	3	0.41	4	0.55	5	0.70
Others	107	14.70	99	13.71	101	14.11
Valid answered questionnaires	728		722		716	

Data source Authors' survey

Note These three questions have multiple choices, so the sum of respondents is not equivalent to the total respondents

directors in all data years (see Table 2.9). Our survey also found that enterprises whose entrepreneur has a directive decision-making style achieve better performances, supporting the above results.

Entrepreneurs inevitably suffer work overload due to their importance. More than 90 % of respondent entrepreneurs work for more than 8 h for each of the normative five working days; more than 55 % work more than 10 h every day; and more than 20 % work more than 12 h every day (see Table 2.10).

2.2.3 Government–Enterprise Relationship

Enterprises have to make contact with various government departments due to the close relationship between governments and enterprises. On average, enterprises need to make more than one contact with departments in industry and commerce, labor and social security, environmental protection, and quality inspection, among others, every month and almost two contacts with tax departments. Also, enterprises receive more than 2 “visits” by government departments every month (see Table 2.11). About 44 % of enterprises surveyed believed that the burden of contact with government is low and is even ignored and about one-third enterprises thought the burden was “just so so,” while 22 % responded that the burden was

Table 2.9 Enterprise decision-making by private entrepreneurs (1993–2006)

Survey year	1993	1995	1997	2000	2002	2004	2006
Important business decision-maker is entrepreneur (%)	63.6	54.4	58.7	43.7	39.7	36.4	36.9
Important business decision-maker is the board of directors (%)	15.2	19.7	11	26.3	30.1	26	25.5
General management decision-maker is investor (%)	69.3	47.3	53.7	35.4	34.7		39.1
General management decision-maker is the board of directors (%)	5.1	15.1	10	18.2	25.9		

Data source All-China Federation of Industry and Commerce (2007)

Table 2.10 Entrepreneurs’ daily working hours

Time	Respondents	Percentage (%)	Accumulative percentage (%)
Fewer than 6 h	7	0.92	0.92
6–8 h	65	8.55	9.47
8–10 h	259	34.08	43.55
10–12 h	261	34.34	77.89
12–14 h	124	16.32	94.21
Above 14 h	44	5.79	100.00

Data source Authors’ survey

Table 2.11 Frequency of contact between enterprises and government departments

Government department contacted	Average frequency	Number of ≥ 2 contacts	Share of ≥ 2 contacts (%)	Valid answered questionnaires
Industry and commerce	1.33	93	17.99	517
Tax	1.94	243	37.73	644
Labor and social security	1.21	61	15.37	397
Environmental protection	1.20	46	13.65	337
Quality inspection	1.34	63	18.00	350
Others	0.88	26	15.95	163
Government department received	2.07	195	39.23	497

Data source Authors' survey

Table 2.12 Burden on enterprises caused by contact with government departments

Burden of PR cost on enterprise			Change trend of the burden		
	Respondents	Share (%)		Respondents	Share (%)
Very heavy	60	8.78	Increasingly heavy	143	21.5
Heavy but tolerable	90	13.18	Increasingly low	131	19.7
Just so	233	34.11	No change	392	58.95
Low	181	26.50			
Can be ignored	119	17.42			
Valid answered questionnaires	683		Valid answered questionnaires	665	

Data source Authors' survey

heavy or very heavy. In addition, 21.5 % of enterprises believed the burden was increasing (see Table 2.12).

Enterprises also pay various fees to governments for direct contact. Research has found that the central government in China tends to collect more money from local fees and off-budget fees and repeatedly issues administrative orders to redevelop allocation rules and transfer more financial burdens to local governments. Off-budget and outside-the-system fees erode the tax base and lead to a larger budget deficit, resulting in more incidental charges. Tax reform in 1994 was actually reform to the centralization of financial power and further aggravated the vicious circle (Chen, Hillman, Gu 2002). Data from the ACFIC (2007) explained the changes to fee burdens on private enterprises. From the perspective of the median fee amount and the proportion of fees to sales volume, fee burdens

Table 2.13 Fee burdens on private enterprises (1997–2006)

Survey year	1997	2000	2002	2004	2006
Median of fee amount (RMB 10,000)	3.9	2.0	3.0	3.0	3.0
Median proportion of fees to sales volume	1.1	0.5	0.52	0.47	

Data source All-China Federation of Industry and Commerce (2007)

Table 2.14 Three expenses of private enterprises (RMB10,000)

	2004年		2006年	
	Gross amount	Mean value	Gross amount	Mean value
Fees	88,793.1	48.8	102,378.3	48.0
Apportionment	8,438.9	5.7	11,429.8	5.3
PR, entertainment	30,438.6	14.2	29,171.7	10.8

Data source All-China Federation of Industry and Commerce (2007)

on enterprises seem to have eased over the years to 2006 (see Table 2.13). Judged by the three major expenses incurred by private enterprises—fees, apportionment and PR and entertainment—the burdens on enterprises decreased during 2003–2005 (see Table 2.14). However, the report said that the drop was mainly due to decreases in those “three expenses” in the eastern region, while only PR and entertainment expenses decreased in the central region and only apportionment declined in the western region (ACFIC 2007).

Interactions between governments and enterprises are actually special transactions under the market economic system. Enterprises get what they want by paying taxes, fees and providing “entertainment,” but the role of the price mechanism is distorted and price is not the only determinant of resource allocation in the transaction process. In addition to financial resources, enterprises can receive other things such as help in dispute settlement. According to a survey on enterprises in the Yangtze River Delta, 9.6 % of enterprises chose “administrative intervention by local government” as the most effective way of dispute settlement and 12.1 % “private channels” (e.g., mainland partner) although 53.3 % chose “direct negotiation with the counterparty” and 36 % “judicial channel in the Chinese mainland.” Interestingly, compared with private and collective enterprises, more state-owned enterprises chose “administrative intervention by local government” and most foreign-funded enterprises unexpectedly chose that method (Y.J. Wang et al. 2007a) (Table 2.15).

2.2.4 Enterprises’ Social Networks and Political Connections

Alliances between entrepreneurs and government officials are “rooted in interpersonal relationships among government, enterprise, and entrepreneur who are familiar with and trust each other” (Wank 1995). Remarkably, interactions

Table 2.15 Most effective way of dispute settlement in eyes of enterprises in the Yangtze River Delta (%)

Most effective way of dispute settlement	Foreign-funded enterprises	State-owned enterprises	Private enterprises	Collective enterprises
1. Direct negotiation with counterparty	46.6	52.5	56.4	54.9
2. Judicial channel in the Chinese mainland	37.5	36.0	35.6	33.3
3. Administrative intervention by local government	17.8	15.8	8.6	9.8
4. Private channels (e.g., mainland partner)	8.7	5.0	11.8	5.9
5. No effective way	5.5	6.5	5.7	5.9
6. Others	4.0	2.2	4.9	3.9
Total	120.2	118.0	123.0	113.7

Data source Wang et al. (2007b), p. 154, Table 6.14

Note Total exceeds 100 % because of multiple choices

between enterprises and governments are mainly conducted by entrepreneurs and government officials, demonstrating the nonanonymous nature of the market mechanism. Zeng (2006) classifies enterprises in the Pearl River Delta into majority, minority, and neutrality categories. Enterprises in the majority category have the strongest innovation ability, depend most on networks, maximize external relations and are most willing to trust strangers and formal institutions. “Most bosses of these enterprises keep a good relationship with government which is based on micro interpersonal relationships. It is found in the survey that bosses of enterprises in the majority category most frequently contact government officials after work and show most significant importance of after-work activities. Meanwhile, most of them said ‘the relationship is the primary productive force’ or ‘the relationship is the most important productive force’.”²¹

Political connections facilitate decision-making by entrepreneurs. Ao (2005) reports the top three practices that are most likely to be chosen by private entrepreneurs to express their opinions on public policies are proposals by an NPC deputy or a member of the Communist Party of China Central Committee (CPPCC), reports by news media and direct appeals to a government leader. Zeng (2006, p. 103) also provides two cases to demonstrate how entrepreneurs helped to solve disputes with local residents by leveraging their relationships with governments and how they received interest-free loans from the Guangdong Bureau of Small and Medium Enterprises by leveraging their private relationships with relevant government officials. Entrepreneurs’ social networks and political connections are analyzed in this section.

²¹Zeng (2006), p. 156, annotation.

Table 2.16 Political status of entrepreneurs

	CPC member	Member of democratic parties	Communist Youth League member	Masses
Quantity	219	10	96	446
Proportion (%)	28.4	1.3	12.45	57.85

Data source Authors' survey

Table 2.17 Entrepreneurs' social posts and political participation

	Valid answered questionnaires	Respondents with "Yes"	Share of respondents with "Yes" (%)
Take office at industry associations and chambers of commerce	777	177	22.78
Deputy to NPC or CPPCC member at all levels	641	128	19.97

Data source Author's survey

According to our statistics on entrepreneurs' political identity, 28.4 % of entrepreneurs were CPC (the Communist Party of China) members and 1.3 % were members of democratic parties.²² Our survey data indicated that enterprises who were NPC deputies or CPC members account for 19.97 % of the total, while 22.78 % of entrepreneurs took office at industry associations and chambers of commerce and similar bodies (see Tables 2.16 and 2.17).²³

Table 2.18 shows the status of and changes to entrepreneurs' social networks and political connections. Data suggest that many entrepreneurs surveyed in 1993 and 1995 had friends who were cadres at all levels and that many entrepreneurs were closest to relatives who were cadres at all levels, with a higher proportion of these proportions in urban areas. A high proportion of entrepreneurs were cadres at all levels before starting their business, and this figure is higher in urban areas than in the countryside. From the perspective of trends, before 2000 more entrepreneurs were cadres at all levels before starting business and the proportion declined after that. Chen (2005) reported that cadres might have increased rather than lost their advantages during market transformation. The proportion of private entrepreneurs whose last title before starting their business was as a state cadre (including military officer but excluding village cadre) before 1992 was 13.7 %; this rose to 16.8 % during 2000–2001. The proportion of private entrepreneurs

²²In China, there are 8 small parties called as democratic parties, but they are not competing with the Communist Party of China (CPC).

²³According to survey data of the ACFIC (2007), a nationwide survey in 2006 did not report the proportion of entrepreneurs who participated in state affairs. A survey in 2004 suggested 52.5 % of private entrepreneurs act as NPC deputies or CPPCC members. However, such a high proportion may be attributed to the sampling method of the survey or because some entrepreneurs were NPC deputies and CPPCC members at the same time.

Table 2.18 Social networks and political connections of private entrepreneurs (1993–2006)

Survey year	1993	1995	1997	2000	2002	2004	2006
<i>Private entrepreneurs whose friends were cadres at all levels (%)</i>							
Urban areas	42.4	46.2					
Rural areas	39.4	42.2					
<i>Private entrepreneurs whose closest relatives were cadres at all levels (%)</i>							
Urban areas	37.9	39.1					
Rural areas	31.2	26.4					
<i>Private entrepreneurs who were cadres at all levels before starting business (%)^a</i>							
Urban areas	22.1	24.2	25.5	43.4 ^b	59.13	41.6	30.2
Rural areas	17.0	17.3					
<i>Political participation</i>							
Deputy to the People's Congress (%)			6.4		17.4	18.9	
CPPCC member (%)			12.7		35.1	33.6	
CPC member (%)	13.1	17.1	16.6	19.8	29.9	33.9	32.2
Member of democratic parties (%)	6.5	5.0		6.7	5.7	6.7	2.0
Member of associations of industry and commerce (%)	90.2	77		85.3	83.4	66.1	
Hope to join the Part (%)		26.5	24.1	10.8			
Hope to join a democratic party (%)		10.4		5.1			
Hope to join the association of industry and commerce (%)		44.7		5.3			
<i>Effective means of improving entrepreneurs' social status (%)^c</i>							
Join the Party		18.1	11.8	7.6	11.1	11.8	24.1
Become a deputy to People's Congress		34.2	15.6	30.9	25.5	15.3	28.8
Take government post		6.0	6.4	4.6	25.4		
Do our best to expand business size		83.3	81.6	81.6	80.6 ^d	87.8	73.7
Make more frequent contact with government and Party leaders		27.6	21.5	15.7		31.6	22.8
<i>Comment on status (1 is highest and 10 is lowest)</i>							
Income	4.5	4.5	4.7	4.7	4.7	5.12	5.64
Social prestige	4.0	4.2	4.6	4.3	4.1	5.15	5.1
Political participation	4.6	5.1	5.7	5.0	5.0	5.76	5.11

Data source ACIC (2007)

Notes

^aData 1995 covered cadres in government bodies, public institutions, or enterprises; data 1997 covered entrepreneurs who started their business in 1992; data 2000 excluded village cadres; data 2002 covered leaders of government bodies, public institutions and enterprises; data 2004 included lessees/contractors (14.2 %) of state-owned/collective enterprises and excluded village cadres (2.8 %)

^bData 2000 indicated the larger an enterprise was, the more likely the entrepreneur had been a cadre. The corresponding proportions are 20.5 % (paid-up capital < RMB10 million), 29.1 % (paid-up capital between RMB10-100 million) and 45.7 % (paid-up capital > RMB100 million)

^cData 2002–2006 involved “specific plans,” “present plans” and “most imperative plans” after the speech delivered by General Secretary Jiang Zemin

^dData 2002–2006 involved “developing enterprises well”

whose highest rank was section-level cadre before they started business stood at 11 % in 1997, increased to 14.4 % in 2000 and rose to 15.3 % in 2002.

July 1, 2001, was an important turning point for entrepreneurs' political connections and political participation. On that day, General Secretary of the CPC, Jiang Zemin, delivered a speech at the 80th anniversary meeting of the CPC. He stated that private enterprises constituted one of the new social classes since reform and opening-up that, "guided by the Party," had contributed to developing productivity and other undertakings of the socialist society by honest work. He said: "They have united with workers, peasants, intellectuals, cadres and officers and the People's Liberation Army and are constructors of socialism with Chinese characteristics. Excellent ones of these classes may be included in the Communist Party of China." The spirit of this speech was written into the Report to the Sixteenth National Congress of the CPC and the revised Party Constitution. The social status of private entrepreneurs was further acknowledged after the private economy was recognized as an important part of the socialist market economy in the Report to the 15th National Congress of the CPC.

Survey data suggested a significant increase in the number of private entrepreneurs who were NPC deputies, CPPCC and CPC members after 2002 but a decline in the numbers who joined associations of industry and commerce. This might indicate mutual replacement among different political connections. Chen (2005) reported the number of entrepreneurs who identified themselves with the CPC after starting business showed a significant rise during 1985–2002. In 2002, nearly 20 % of entrepreneurs became Party members after they started in business, and an increasing number of entrepreneurs acted as deputies to the People's Congresses at all levels or as CPPCC members. The proportion of entrepreneurs who were deputies to the People's Congresses increased from 10.3 to 18.2 % during 1997–2004 and that of entrepreneurs who were CPPCC members rose from 22 to 30.6 %. More and more private entrepreneurs took up positions at local Party-related and government bodies. The proportion stood at 2.3 % in 1997 and had increased to 3.3 % by 2002 (excluding village-level organizations).

The survey also studied the opinions of private entrepreneurs about ways to improve their social status but no significant trend was evident. In a survey in 2006, more than 20 % of entrepreneurs still chose to join the CPC and industry associations or foster relationships with Party members. Much attention should be paid to the comments by entrepreneurs on their social status in income, prestige and political participation. Unexpectedly, entrepreneurs said their social status derived from income kept decreasing, while status from political participation fluctuated.

2.3 Conclusion

It is clearly stated in this chapter that to understand entrepreneur growth and enterprise development, it is necessary to focus on analyzing the interaction among governments (officials), enterprises, and entrepreneurs and to reveal the

nonanonymous aspect of the market system. In China, government plays a very important role in enterprise development because government and commerce are closely combined traditionally in China and because contemporary China has moved away from an economy characterized by comprehensive government intervention. In fact, government–enterprise connections are not only very important in transforming and developing economies like China. On the contrary, the importance of government–enterprise connections provides a brand-new perspective on understanding the operation of a market economy.

Will government intervention into enterprises naturally decrease during the establishment of a market economy? Will government–enterprise connections become less important? Will the important role of entrepreneurs in enterprise development due to government–enterprise connections consequently weaken? All these questions need to be empirically studied and observed. Chapters 3, 4 and 5 will present answers to these three questions by empirical studies of the interaction framework between governments (officials), enterprises, and entrepreneurs that we explored in this chapter. First, in contemporary China, entrepreneurs indeed act as the soul of enterprise development. Their decision-making style exerts an important influence on enterprise performance and their human capital and political connections also become important resources for enterprise development (see Chap. 3). Second, to develop political connections, entrepreneurs are enthusiastically participating in state affairs, and the transformation of economic resources into political resources can be observed (see Chap. 4). Third, the development model of government intervention in an economy exacts a price. Government intervention has imposed increasingly heavy burdens and significant adverse impacts on entrepreneurs’ satisfaction and entrepreneur growth (see Chap. 5). Our empirical studies provide evidence of the interactive relationships among governments, enterprises, and entrepreneurs. However, more cross-time and cross-region comparative studies are needed to determine the trends of change of these relationships because of the scarcity of such studies in China due to limited data. The next three chapters will present more specific discussions based on progress in these studies. No observation indicates that government–enterprise connections are no longer important. On the contrary, the trend is to develop government–enterprise connections from the perspective of observation, and entrepreneurs are keen to participate in state affairs.

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