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The Self-Empowered New Master at the Workplace: Privatization in Russia and China

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THE SELF-EMPOWERED NEW MASTER AT THE WORKPLACE: PRIVATIZATION IN RUSSIA AND CHINA

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A DISSERTATION
PRESENTED TO THE FACULTY
OF PRINCETON UNIVERSITY
IN CANDIDACY FOR THE DEGREE
OF DOCTOR OF PHILOSOPHY

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BY THE DEPARTMENT OF SOCIOLOGY

Advisor: Gilbert Rozman

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ABSTRACT

In the dissertation the author explored how privatization in Russia and China shaped transition from state socialism. In the past two decades, many observers believe that Russia and China have moved along two different tracks in their transitions, and analyses about privatization in the two countries were mainly contributed by economists who focus on ownership change and corporate governance. However, the author found that, in the privatizations of Russia and China, the explanatory power of economics analysis is actually limited, because in both countries ownership structure of privatized firms often does not determine corporate governance. The factors that shape the perceptions of managers and workers on issues like property rights, managerial power, and the position of workers, and what the relationship is between their perceptions on these issues and the choices they made during the privatization process have not been properly explored before.

The author discussed the value orientations of managers and workers, and the interactions between the two groups in Russia and China during privatization, and revealed that outcomes in privatization are shaped by social relations at the workplace, and also by social relations among bureaucrats, SOE managers, and private businessmen. Analyzing the sociopolitical and economic preconditions, guidelines, policy making ramifications, and processes and outcomes of the two privatizations, the author found that, although paths of the two privatizations are quite different, in both countries *nomenklatura* privatization prevailed. Former SOE managers personally invested only a little money, or nothing, have finally empowered themselves to be the new masters of the firms. In Russia and China, the *nomenklatura* privatization produced similar authoritarian management-worker relations at the workplace, which undermine performance of the privatized firms. Ultimately, Russia's economic transition has moved ahead without the real social reconstruction that occurred in

Central Europe, with the result of a backsliding into a capitalist *nomenklatura*-authoritarian rule, and China's economic transition produces a unique communist capitalism, a new capitalism manipulated by the communist party, a first to be observed in world history.

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I would like to thank Vladimir Magun of Sociology Institute of Russian Academy of Sciences, who introduced me to many Russian scholars, and the scholars of *Vox Populi*, a Moscow based public opinion survey organization headed by Professor Boris Andreevich Grushin, for their help in my survey conducted in Moscow area. I also need to thank Matthew Robertson for polishing my writing.

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Chapter 1

Why Privatization Apart from the Ideal Model?

The Cases of Russia and China

The transition from state socialism is a laboratory of large-scale social experimentation for social scientists. How would policy proposals and theories, drawn from experiences of Western countries, be applicable to a society where capitalism emerges from socialism? This challenging exploration has attracted many scholars. In contrast with countries in Central and Eastern Europe, where socialism was more or less imposed, Russia and China, the cradles of two endogenous communist revolutions, provide observers fruitful lessons in whether and how capitalism is embraced by billions of people who once faithfully believed in state socialism.

Conventionally, the economic aspect of the transition is perceived as a process of marketization. The marketization theme emphasizes removing the planning system, freeing prices, interest rates and trade, and transforming state-owned enterprises (SOEs) into firms owned by outside investors with efficiency-oriented corporate governance through privatization. In this arena, economists have contributed a great deal, whereas sociological thinking is often left outside of policy discussions of transition regimes, except in a few fields such as labor policy. However, progress in marketization often does not really follow the rationalistic designs recommended by economists.

In the past two decades Russia and China have both worked on the transformation of SOEs, a key step for a functioning market economy, but selected different strategies. Practices of the two

countries represent alternative possible policy proposals from the World Bank to domestic scholars, from proponents for radical reform to those for incremental change, from the point of view of neoclassical economics to that of Marxism. Most theory-based recipes, such as corporatization, manager's autonomy, workplace democracy, privatization, corporate governance, and workers' self-management, have been tried in experiments. However, results from the big social laboratory indicate that, despite expectations of the policy proponents, real changes in the privatized former SOEs in Russia and China are quite inconclusive. In many privatized enterprises of the two countries, neither proper corporate governance nor satisfying firm performance has been achieved, even after privatization has been in place for a decade. Having no convincing interpretations, many scholars in the field of transition societies have left the issue aside.

In 1848, Karl Marx suggested that, by "abolishing their own previous mode of appropriation," the proletarians ought to "become masters of the productive forces of society."[2] Both the Soviet and Chinese communist parties used the term "masters of production" to describe the sociopolitical status of working class in their ideological propaganda and in industrial management. Although under the rule of the communist regimes industrial firms were integrated into the SOE system which was fully controlled by the state, and SOE workers in the two countries realized that they had never been the real masters of production or of their enterprises, the idea introduced by Marx was deeply rooted in workers' minds and had greatly shaped their attitudes towards privatization. In a privatization process would workers get a chance to become

[2] Karl Marx, "Manifesto of the Communist Party," in Robert C. Tucker ed., *The Marx-Engels Reader*, New York, NY, W. Norton & Co. 1978, 482.

the masters of their enterprises in the new capitalism emerging from state socialism? Russia's voucher privatization of small- and medium-sized SOEs and China's widely experimented employee shareholding provide an opportunity to find the answer.

In late 1980s Gorbachev carried out a workplace democracy policy to incorporate workers into management through creation of representative workers' councils and election of managers. This experiment opened up the door for workers' political participation, but did not improve efficiency.[3] After the Soviet Union collapsed, Russian transformation of SOEs started from a voucher privatization, designed to meet the interests of societal members and to create millions of individual owners for former SOEs. But in most factories a coalition of management and workers selected the option of controlling shares internally by exchanging their vouchers for shares of their own factory.[4] Industrial public properties were thus transferred into the hands of employees. Managers then collected more and more shares from workers, thus the insiders' privatization was transformed into *de facto* managers' privatization. In many enterprises it occurred with workers' tacit approval, whereas workers' self-management did not gain much support.

China, for 15 years after 1980, had insisted on enhancing managers' autonomy in SOEs without formal privatization. Managers were encouraged to create incentives for productivity and profit. The institutional improvements, however, had not alleviated the ever worsening performance

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[3] Donald Filtzer, "Economic Reform and Production Relations in Soviet Industry, 1986-1990," in Chris Smith, and Paul Thompson, eds. *Labor in Transition: The Labor Processes in Eastern Europe and China*, London, Routledge, 1992; Linda J. Cook, *The Soviet Social Contract and Why It Failed: Welfare Policy and Workers' Politics from Brezhnev to Yeltsin*, Cambridge, MA, Harvard University Press, 1993.

[4] Kiril G. Holodkovsky, "*Rossiskaya Privatizatsia: Stolkhnovenye Interesov* (Russia's Privatization: Clash of Interests)," Moscow, Russia, *Mirovaya Ekonomika i Mezhdunarodnoe Otnoshenie* (The World Economy and International Relations), No.1, 1995, 72-86.

of the SOEs. Starting from the late 1990s, China's central government initiated a new campaign of transforming the SOE system, with a strategy of "grasping the large and letting go of the small." While 520 "key-point" SOEs were kept in hands of the government, the remaining 80,000 SOEs, including most of the 8,700 large and medium-size enterprises, were put into a process of corporatization.[5] A 2001 national survey of industrial SOEs estimated that 86 percent had been "transformed" and about 70 percent had been partially or fully privatized,[6] though the government declined to use the term of privatization for ideological reasons. In the process, workers were asked to buy shares of their enterprises in order to keep their jobs, and managers tried many ways to get control of the privatized share-holding companies, from informal approaches to formal management-buy-outs (MBO). Although superficially corporate governance was established for the enterprises, the boards of directors of the companies were dominated by managers, and in many firms managers actually gained more power to process assets of the enterprise and to lay off employees.

No matter how designated policies tried to offer a wider space and more options, the transformation process of SOEs in Russia and China was obviously dominated by insiders, rather than outside investors. The phenomenon may disappoint some privatization proponents, as an insider's control of privatization is perceived as unfavorable for marketization because it is not

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[5] Shahid Yusuf, Kaoru Nabeshima, and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, Washington, DC, The International Bank for Reconstruction and Development/ The World Bank, 2006, 81.

[6] Ross Garnaut, Song Ligang, Stoyan Tenev and Yao Yang, *China's Ownership Transformation: Process, Outcomes, Prospects*, Washington, DC, International Finance Corporation and the International Bank for Reconstruction and Development/ The World Bank, 2005, 5.

efficiency oriented. Moreover, among workers and managers of the two countries, managers had more opportunities and power to manipulate privatization into a spontaneous path with a high social and moral cost. In literature of transition economy, such a process is considered a spontaneous privatization or *nomenklatura* privatization—a pattern in which members of the communist or ex-communist managerial and political establishment turn themselves into business elites in the newborn capitalist economy.[7]

Interestingly, different strategies of SOE transformation in Russia and China have seemingly ended up with similar consequences. First, negative evaluation of the privatization in both countries has been observed in public opinion survey and various interviews, particularly with reference to managerial corruption.[8] Second, workers of privatized enterprises in both countries present a quite similar workplace culture: "an idealization of the past, a pessimistic evaluation of the present, a complete lack of belief in the future, and distrust of company directors."[9] Third,

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[7] Linda Cook, and Vladimir Gimpelson, "Exit and Voice in Russian Managers' Privatization Strategies," *The Communist Economies and Economic Transformation*, 1995, Vol.7, No.4, 465-83; Ding Xueliang, "Who Gets What, How? When Chinese State-Owned Enterprises Become Shareholding Companies," *The Problem of Post-Communism*, 1999, Vol.46, No.3, 22-41.

[8] Kiril G. Holodkovsky, "*Rossiskaya Privatizatsia: Stolkhnovenye Interesov* (Russia's Privatization: Clash of Interests)," 72-86; Pei Minxin, *China's Trapped Transition: The Limits of Developmental Autocracy*, Cambridge, MA, Harvard University Press, 2006, 153-154; Chen Feng, "Subsistence Crises, Managerial Corruption and Labour Protests in China," *The China Journal*, No.44, 2000, 41-63.

[9] Elena Avraamova, Igor Gurkov, and Galina Bulychkina, "Privatization as a Socioeconomic Phenomenon," *The Sociological Research*, No.6, Sept.-Oct., 1996, 21; Yuan Yue, "*1996-1997 Nian Zhongguo Chengshi Shehui Wending yu Fazhan Zhuangkuang de Gongzhong Xintai Fenxi* (Analysis of the Public Opinions on Urban Social Stability and Development in 1996-1997)," and Qiao Jian, "*1996-1997 Nian Zhongguo Zhigong Zhuangkuang de Fenxi yu Yuce* (Analysis and Forecasting of the Status of China's Workers and Staffs in 1996-1997," in Jiang Liu, Lu Xueyi, Shan Tianlun, Li Peilin, Huang Ping and Lu Jianhua, eds. *1996-1997 Zhongguo Shehui Xingshi Fenxi yu Yuce* (Analysis and Forecasting of China's Social Situation in 1996-1997), Beijing, China, China's Social Science Press, 1997, 80-90, 250-263; The Research Dept. of the All China

systemic studies by some economists of performance of privatized industrial enterprises in Russia and China conclude that such reform does not show significant impact on enterprise performance in both countries.[10]

Many scholars, reporters and even politicians in Russia charge that privatization went wrong. The same accusations can be heard in China in recent years. Legal and economic scholars have emphasized efficiency oriented corporate governance and the legal environment as core issues for the success of privatization. Observing from this perspective, one may find that the two countries share a lot in terms of deviation from the ideal model of privatization-the formation of good corporate governance dominated by outside investors. Other scholars and reporters blame corruption in the privatization process, which caused widespread social discontent. Why did the social actions of participants in the privatization process go beyond the ideal model, and why did spontaneous privatization become an irreversible movement? Some economists may believe that with privatization of SOEs having been accomplished, the transformation of the two economies was complete, and correction of poor overall performance would take place with the improvement of the market system. However, a lot of questions remain for sociologists.

Furthermore, if one views the two countries from a comparative perspective, the questions may become even more challenging. First of all, Chinese SOEs, backed by government policies,

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Federation of Trade Union, ed. *Zhongguo Zhigong Zhuangkuang Diaocha 2002* (The 2002 Survey of the Status of Chinese Workers and Staff), Beijing, China, Press of Chinese Workers, 2003, 1033.

[10] Shahid Yusuf, Kaoru Nabeshima, and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 207-209; Yurii Perevalov, Ilya Gimadii, and Vladimir Dobrodei, "Does Privatization Improve Performance of Industrial Enterprises? Empirical Evidence from Russia," *The Post-Communist Economies*, Vol.12, No.3, 2000.

laid off more than 40 million workers within a few years before and during the privatization. The Russian government, by contrast, had never condoned such a policy and state-owned enterprises in Russia have laid off far fewer employees. From point of view of economics, getting rid of redundant labor helps improve the efficiency of privatized enterprises. However, the corporate governance and performance of privatized enterprises in China have seemingly not prevailed over those of privatized enterprises in Russia.

In terms of workplace relations, while Gorbachev's policy of workplace democracy was abandoned with collapse of the Soviet regime, some kinds of workplace democracy practices have been nominally kept in Chinese privatized enterprises. Are workplace relations of the privatized enterprises in China better than those of Russia? The fact is that workplace conflict is infrequently reported in Russia;[11] but in China there have been numerous reports of protests and demonstrations against managers,[12] while some were against layoffs, but more were related to labor disputes. An extreme case in China during privatization was reported in July, 2009, after a CEO of the Tonghua Steel Co., who represented a private company that took over the SOE, was beaten to death by angry workers of the factory.[13]

Taking into consideration that China remains a country under authoritarian rule of the communist party, where workers lack the freedom to demonstrate or strike, while Russian workers may feel free to organize strikes or protests, one may ask why Chinese workers are

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[11] Penny Morvant, and Peter Rutland, "Russian Workers Face the Market", *Transitions*, June 28, 1996.

[12] Lee Ching Kwan, ed., *Working in China: Ethnographies of Labor and Workplace Transformation*, London, Routledge, 2007, 17.

[13] "The Necessity to Improve the Pension System in China", Bonn, Germany, *Deautche Welle*, 1/9/2010 (http://www.dwelle.de/dw/article/0,,5099971,00.html).

seemingly less compliant in a more oppressive political environment. Indeed, Russian workers participated in strikes and demonstrations more in the pre-privatization years than after privatization. But Chinese workers have done almost the opposite--most demonstrations and protests in China have taken place during and after privatization. Obviously, tense workplace relations do not improve efficiency of the firms. However, new Chinese owner/managers seem to accept internal conflicts more than their Russian counterparts do. Why would similar spontaneous privatization in the two countries result in different workplace relations and how do owner/managers of the two countries benefit from their workplace relationships? While these observations and questions make the privatization in Russia and China more puzzling, they suggest a dimension for sociological research on the transformation of SOEs.

Privatization of SOEs is not simply a series of legal practices of transferring public properties into private hands. The activities also mean a privatization of wealth and employment relations;[14] therefore, the privatization should be understood as a social process. Moreover, privatization is not the only task of the transformation of a state-owned enterprise. The transformation also has to deal with the crucial task of restructuring owner-management relationships, which includes, but is not limited to, corporate governance, and management-worker relations. In state socialism the managerial structure of SOEs was part of the overall administrative apparatus, although SOE management had its own interests and often negotiated with higher level government officials. The transition from state socialism requires

[14] Paul Starr, "The Meaning of Privatization," *Yale Law and Policy Review* Vol. 6, 1988, 6-41. This article also appears in Alfred Kahn and Sheila Kamerman, eds., *Privatization and the Welfare State*, Princeton, NJ, Princeton University Press, 1989.

dismantling the old apparatus and creating management autonomy; at the same time, SOE workers are released from the status of state employee and become contract labor. Thus a new relationship between management and workers has to be established. In industrial societies such relations may have different patterns. A harder form of management through efficiency-oriented bureaucratic control, which involves the use of job security and promotion to induce workers' loyalty to the enterprise and motivation for hard work,[15] is often contrasted with a soft alternative, which gives employees greater control over work time and the process of production. In terms of a better labor-capital relationship, forms vary from the workers' cooperative pattern to the employees' stock ownership plans to workers indirect control of enterprises through labor union pension funds. But the lessons of the insiders' privatization in Russia and China and the frequent workplace conflicts in China imply that things were much more complicated in both countries.

Since the Russian voucher privatization program offered workers the rights for ownership, and China's strategy of transforming SOE system let managers obtain shares of their firms and employees buy stock in their own firms, both managers and workers could become insider owners. Therefore, the restructuring of owner-management relations and that of management-worker relations have become twisted together, and involved four key actors, namely government, new outside owners, managers and workers. Government offices and officials at distinct levels (such as central ministries and localities) may have different interests and actions; outside owners, domestic or foreign, may pursue different goals and behave diversely; and the roles of

[15] Richard Edwards, *Contested Terrain: The Transformation of the Workplace in the Twentieth Century*, N.Y., Basic Books, 1979.

managers and workers are even more confusing, as the two actors play dual roles, both as owners and daily operators of their firms. Moreover, managers are in a much stronger position than workers are, although they might own only a small amount of shares at the beginning of privatization. When the insiders' privatization is altered into a managers' privatization, how workers perceive this movement also affects management-worker relations and the performance of the privatized enterprises as well.

Indeed, the transformation of SOEs is a social process shaped by attitudes and actions of its participants. When the relationship between outside owners and insiders is affected by laws and government policies, the formal structure of corporate governance and the informal social networks between the two parties, path dependence of the existing management-worker relationship may restrain directions of privatization and the patterns of new management-worker relationship of the privatized enterprises. As managers and workers pursue their own interests, their attitudes and actions are shaped by government policies, laws and formal or informal agreements and commitments, and also by culturally defined societal norms about informal relations between managers and workers. How shifting and unchanging parts of a value system and social behavior influence the configuration of management-worker relations remains an unfolding arena, and has not yet been properly conceptualized. The puzzles of the privatization in Russia and China imply that understanding the interaction between managers and workers in the privatization process requires a lot of in-depth research and analysis. Furthermore, the characteristics and nature of the management-worker relationship before, during and after privatization greatly affect daily operation of the privatized corporations, and

thus their economic performance and social stability.

Studies of management-worker relation fall in fields of management and sociology. Although it has a close link with marketization, the relationship itself can not be marketized, nor could it be categorized as part of marketization. While literature of marketization usually locates the topic in efficiency-oriented enterprise reform,[16] it often assumes that both managers and workers share an efficiency claim in the reform. However, the real motivations of the two parties, as seen in insider's privatization, are actually different. In sociological literature, while corporate governance[17] and labor relations[18] attract many scholars, restructuring management-worker relations in transition societies, academically standing between the two themes, has so far drawn little attention.[19] Often, discussions of SOE transformation have either treated the new management-worker relationship as a product of corporate governance or a conflict-driven tension. Actually, as the above brief introduction of privatization in the two countries suggests, corporate governance might be manipulated by insiders and the workplace does not inevitably become a battlefield of workers fighting against management for their rights. A

[16] Michael McFaul, and Tova Perlmutter, *Privatization, Conversion and Enterprise Reform in Russia*, Boulder, CO, Westview Press, 1995; Gary H. Jefferson, and Inderjit Singh, eds. *Enterprise Reform in China: Ownership, Transition, and Performance*, Washington, DC, The World Bank, 1999; Anne S. Tsui, and Lau Chung-Ming, *The Management of Enterprises in the People's Republic of China*, Boston, MA, Kluwer Academic Publisher, 2002.

[17] Gerald F. Davis, "New Directions in Corporate Governance," *Annual Review of Sociology*, Vol.31, 2005, 143-62.

[18] John Thirkell, Krastyu Petkov, and Sarah Vickerstaff, *The Transformation of Labor Relations: Reconstructing and Privatization in Eastern Europe and Russia*, Oxford, Oxford University Press, 1998; Lee Ching Kwan, ed., *Working in China: Ethnographies of Labor and Workplace Transformation*, London, Routledge, 2007.

[19] One of the few examples is *Changing Workplace Relations in the Chinese Economy*, edited by Malcolm Warner, London, Macmillan Press Ltd., 2000.

corporation cannot survive without management and workers. The two parties have common interests, and do not have to be in constant conflict. Study of management-worker relations is closest to organization studies, but scholars in that field traditionally focus on organizations of non-communist societies. Now that both Russia and China work on importing capitalism and Russia has experienced the initial democratization, their social experiments may provide incentive and fresh materials for organizational studies.

So far no systematic comparative study of privatization in the two countries has been done, though there are researchers focusing on some of the issues in either Russia or China. The only comparative works about enterprise reform in the two countries were published in 1995 and 1996, when China had not yet initiated nationwide privatization.[20] In the past two decades, Russia and China scholars have done a lot of research about enterprise reform and labor relations in either country. Their contributions provide rich materials for my research, but their analytical dimensions did not lead them to explore the restructuring of management-worker relations. Moreover, their focus on a single country often prevented them from testing the value of assumptions or conclusions drawn from one country in another. For example, some China scholars or Russia scholars attribute characteristics of privatization to Chinese culture or Russian culture. What they haven't tried to think about is a challenging question: what if the

[20] Maurice Ernst, Michael Alexeev, and Paul Marer, *Transforming the Core: State Industrial Enterprise in Russia, Central Europe and China*, Boulder, CO, Westview Press, 1996; Sam Overman, "Privatization in China, Mexico, and Russia: A Comparative Study," *Public Productivity & Management Review*, Vol. 19, No. 1 (Sept.), 1995, 46-59. The International Labor Organization published a paper "Privatization: Lessons from Russia and China" edited by Joseph Prokopenko, *Enterprise and Management Development Working Paper - EMD/24/E*, Jan. 24, 2000. This paper actually compares Russia's privatization with the development of non-SOE sector and the SOE reform in China, but not the privatizations of the two countries.

same characteristics are found in another culture? Certainly, a comparative study of the topic will offer better opportunities to expand the view of single country observation and to obtain findings that single country studies could not get.

My dissertation research has been a long journey. It started in 1995 when massive privatization was done in Russia but no real progress of SOE reform was accomplished in China. In 1995 and 1997 the author went to Russia twice to conduct interviews in Saint Petersburg and Moscow, and in 1996 went to China and did some interviews there. At the end of 1997, the Chinese government initiated a round of unnamed privatization of SOEs, which lasted for about a decade. Only recently have the consequences of the corporatization become clear, thus allowing me to move forward to reach some conclusions.

In this dissertation, through analyzing opinions of workers and managers, cases and media reports from Russia and China, the author discusses how the state, managerial *nomenklatura* and SOE workers in Russia and China played their roles in the privatization process and with what motivations, how values and the existing social relations at the workplace influence self-interested behavior of the two social groups, how the SOE managers in the two countries manipulated the game of ownership change to consolidate their power and authority, and how social actions of the two groups produce the seemingly puzzling results of privatization in the two countries. The thesis will also interpret how different management-worker relations are shaped in privatized industrial enterprises in Russia and China, and why many of the managerial *nomenklatura* of the two countries have developed the similar post-privatization authoritarian management-worker relations that undermine workers' morale.

After most Russian SOE workers chose an insider privatization of their enterprises, their employee ownership turned out to be insufficient to empower them to become the masters of their enterprises, because the power structure that dominated the workplace for decades before and after privatization might weaken the role of employee ownership. In China the authoritarian communist regime paved the way for a spontaneous privatization manipulated by managers at the cost of workers. Consequently, in both countries many self-empowered managers have been transformed into the new masters of the privatized enterprises, while they personally invested only a little money, or nothing. It was not the capitalist institutions introduced into the privatized enterprises that supported the self-empowerment process of the managers; instead, the legacy of state socialism has led privatization astray from an ideal model and contributed a great deal to the configuration of the authoritarian management-worker relations at the workplace. However, some exceptions have been observed in Russia. While many managers employ the authoritarian management approach to empower themselves to be the new masters of enterprises, a few of former SOE manages embraced the idea of workplace democracy and developed a cooperative management-worker relationship at the workplace, thus enabling the employee shareholders of the enterprise to enjoy the feeling that they now really possess the firm after capitalism replaced state socialism.

The dissertation is composed of ten chapters. This introductory chapter is followed by a chapter of literature review and a chapter that introduces research questions, data sources and orienting propositions. The other seven chapters include a chapter about the pre-privatization sociopolitical and economic situations in Russia and China, then two chapters of in-depth

analysis about the privatization process and consequences in Russia, and three chapters about the unnamed privatization in China that has lasted for fifteen years, and, finally, a chapter of comparative discussion in which the author will compare the privatization in Russia and China, and draw some conclusions and point out their theoretical implications.

Chapter 2

Between Corporate Governance and Labor Relations: Reexamining Studies on Management and the Workplace in Transition Societies

Transformation of SOEs is a central task in economic transition. When the planned economy is dismantled, marketization requires necessary economic-social institutions to reconstruct the property rights of SOEs and to improve their poor performance. Studies of the transformation have been a hot topic in the past two decades, and can be briefly categorized into two groups: the management literature contributed by economists and scholars of law and political economy, in which corporate governance is a recent core issue, and the empirical research on the workplace mainly by scholars of labor relations. By reexamining the arguments of the two schools, I find that between the two already cultivated fields of corporate governance and labor relations, there is a necessary third analytical arena: management-worker relations drawing on organization theory, which provides a lens for exploring why privatization in Russia and China has deviated from ideal models.

1. Introducing Corporate Governance into Transition Societies:

An Issue Interpreted through Lessons Drawn from Insider Privatization

In policy discussions of economics, transformation of SOEs is usually simplified as privatization, i.e. assigning state owned properties to private owners. It is expected that privatization would take place as a result of mutually acceptable (Pareto-improving) contracting among relevant actors.[2] Neoclassical economists believe that rational individuals would simply adopt the given blueprint of the transformation based upon economic theory. They perceive proposed transformation programs from the lens of a universal model, and consider the process a rational economic change. Murrell's summary well reflects this thinking: quick privatization of existing state enterprises is often viewed as a necessary and sufficient condition for the success of reform; it is assumed that, given a new ownership structure and market competition, there will be large increases in the efficiency and output of the existing stock of enterprises, which will more than repay the rather large political, social, and organizational costs incurred in the privatization process itself.[3] A designated scenario of this type is that, after the decisive marketization step, the state enterprises would be quickly commercialized and put in the charge of boards of directors and allowed to act independently; the boards would have the power to

[2] Lorene Allio, Mariuz M. Dobek, Nikolai Mikhailov, and David L. Weimer, "Post-communist Privatization as a Test of Theories of Institutional Change," in David L. Weimer ed. *The Political Economy of Property Rights: Institutional Change and Credibility in the Reform of Centrally Planned Economies*, Cambridge, UK, Cambridge University Press, 1997, 321.

[3] Peter Murrell, "Evolution in Economics and in the Economic Reform of the Centrally Planned Economy," in Christopher Clague and Gordon C. Rausser eds. *The Emergence of Market Economies in Eastern Europe*, Cambridge, MA, Blackwell, 1992, 43.

select (and replace) the top managers and to determine reward structures, and managers would be given the power to reorganize production and lay off workers; strong incentives can be provided to managers and workers to carry out the needed restructuring.[4] But political scientists maintain, "reform and privatization measures are rarely justified on economic grounds alone; instead, the reasons that drive the processes are always explicitly political."[5] Actually, when economic analysis is employed in privatization policy-making and policy implementation, consultants often have to bring political and social factors back in. Moreover, in order to understand how these factors affect privatization, one needs to observe what really happens in enterprises. However, much of the economic literature on privatization in Eastern Europe and Russia has failed to focus on the complexities of ownership change and has ignored the enterprise level, because real changes at this level are thought to be contingent upon ownership change.[6]

When widespread insiders' privatization and managers' spontaneous privatization have seemingly refuted claims of the adaptability of the ideal economic model, it turns out that, rather than being a simple economic action, privatization "involves politics, law, justice, morals,

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[4] Christopher Clague, "The Journey to a Market Economy," in Christopher Clague, and Gordon C. Rausser eds, *The Emergence of Market Economies in Eastern Europe*, Cambridge, MA, Blackwell, 1992, 15.

[5] Ezra N. Suleiman, and John Waterbury, "Introduction: Analyzing Privatization in Industrial and Developing Countries," in Suleiman and Waterbury eds. *The Political Economy of Public Sector Reform and Privatization*, Boulder, CO, Westview Press, 1990, 3.

[6] John E. M. Thirkell, Krastyu Petkov, and Sarah A. Vickerstaff, *The Transformation of Labour Relations: Restructuring and Privatization in Eastern Europe and Russia*, Oxford, UK, Oxford University Press, 1998, 64.

and economics."[7] Institutional economists, who disagree in many respects with neoclassical economists, are seemingly more capable of understanding the real process of privatization. Knight and North point out: "In the process of constructing economic institutions, individual actors will be motivated by the benefits that they individually derive from the activities structured by these institutions…In the informal privatization cases, if SOE managers can determine that one form of privatization benefits them more than the other alternatives, they will prefer to establish that form of property rights."[8] At the same time, they try to defend the tenets of neoclassical economics by suggesting that the economic theory is better at predicting the long-run rather than the short-run characteristics of property rights. They argue that in the short run SOE managers may be motivated to choose property rights schemes that produce distributional advantage even if they are Pareto inefficient; but in the long run, if they persist in establishing property rights that are Pareto inefficient, then they will be replaced by the competitive pressure produced by economic actors who employ more efficient rights schemes.[9] Indeed, implementation of SOE restructuring has to deal with short-run problems and troubles up front; it can not simply wait patiently for the arrival of the long-run advancement, while no one really knows when the short-run consequences will turn around.

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[7] Anders Aslund, *Building Capitalism: the Transformation of the Former Soviet Bloc*, Cambridge and New York, Cambridge University Press, 2002, 255.

[8] Jack Knight, and Douglass C. North, "Explaining the Complexity of Institutional Change," in Weimer, David, L. ed. *The Political Economy of Property Rights: Institutional Change and Credibility in the Reform of Centrally Planned Economies*, Cambridge, UK, Cambridge University Press, 1997, 350.

[9] Ibid.

The unexpected insiders' privatization in transition economies, particularly that of Russia, suggests the weakness of the ideal model for SOE transformation based upon pure economics theory, which assumes that "regardless of whoever initially received resources, these resources would flow naturally to their highest-value users after markets were established."[10] Economists then began to move their attention to good corporate governance, which was seen as a new core issue of transition, but they found that the idea of corporate governance did not really exist in Eastern Europe and nobody knew how to solve the problem.[11]

Corporate governance is a "nexus of institutions defined by company law, financial market regulation, and labor law."[12] Three types of law structure corporate governance. First, company law defines the legal standing of publicly and privately held corporations and specifies the legal liability of owners and the relationships among owners, boards of directors, managers, and workers. Second, financial market regulations refer to how firms obtain capital for their operations, where in doing so they specify firms' relationships to banks, other financial institutions, and the public equity and debt markets. Third, labor law defines how labor contracts will operate in a particular society. Such laws include the rights of labor to organize, the conditions under which labor is hired and fired, and how and to what degree workers participate in corporate governance. In societies like the U.S where labor law is weak, corporate

[10] Merritt B. Fox, and Michael A. Heller, "Conclusion: The Unexplored Role of Initial Conditions," in Fox, and Heller, eds. *Corporate Governance Lessons from Transition Economy Reforms*, Princeton, NJ, Princeton University Press, 2006, 367.

[11] Colin Mayer, "Corporate Governance: Market and Transition Economies," paper for presentation at the International Conference on Chinese Corporate Governance, Shanghai, October, 1995.

[12] Neil Fligstein, and Jennifer Choo, "Law and Corporate Governance," *Annual Review of Law and Social Science*, Vol.1, 2005, 63.

boards make decisions to maximize shareholder value without regard to its effect on labor. In Germany, where labor law is well developed, workers have representatives on boards of directors and are viewed as partners in business decision-making.[13]

In the US and most other countries, historically founder-owners and their descendants ran firms, thus ownership and control of firms are in the same hands. As firms grew large, a managerial revolution in the 1920s led to a separation of ownership and control in large corporations; therefore, the control shifted from entrepreneurs to professional managers and ownership became dispersed among thousands of unorganized shareholders.[14] At that time, "firms pursued growth first and profits second… assuming ownership to be largely irrelevant."[15] From the mid-1960s to mid-1980s, the proportion of the average U.S. firm's equity controlled by institutional investors increased dramatically from 16 percent to 43 percent.[16] Institutional investors were concerned with returns on their investment, and began to influence the decision-making of firms and governmental policy. "The rise of shareholder activism in the U.S. has forced a reassessment of the origins of the managerialist corporation."[17] Starting from the late 1970s discussions of corporate governance introduced ideas about power and responsibility into the literature on management. They refer to "the structure of power

[13] Ibid, pp. 63-64.

[14] Berle Adolph Jr., and Gardiner C. Means, *The Modern Corporation and Private Property*, New York, McMillian, 1932.

[15] Gerald F. Davis, "New Directions in Corporate Governance," *Annual Review of Sociology*, Vol.31, 2005, 145.

[16] Michael Useem, *Executive Defense: Shareholders Power and Corporate Reorganization*, Cambridge, MA, Harvard University Press, 1993.

[17] Gerald F. Davis, and Tracy A. Thompson, "A Social Movement Perspective on Corporate Control," *Administrative Science Quarterly*, Vol.39, No.1, 1994, 141.

within each firm that determines who allocates money: who gets the cash flow, who allocates jobs, who decides on research and development, on mergers and acquisitions, on hiring CEOs, on subcontracting to suppliers, on distributing dividends or buying back shares or investing in new equipment."[18] Theoretical debate on corporate governance has explored the structures, processes, and institutions within and around organizations that allocate power and resource control among participants.[19] It reflects a growing need of institutional shareholders to effectively control the operation of corporate CEOs, so that firms can maximize their residuals and distribute the wealth to shareholders.

The literature in the field usually focuses on features of the institutions within advanced market economies, with the debate breaking down between Anglo-American and Continental perspectives. The Anglo-American model relies upon liquid capital markets, which serve as a disciplinary factor in controlling managerial incompetence, whereas the Continental pattern represented by the German system and that of Japan as well centers on stable relations between firms and their bank-owners which own significant amounts of equity and monitor corporate performance. In discussions of efficiency and corporate governance, agency theory gains a dominant position, which interprets the separation of ownership and corporate control as an efficiency-oriented rational choice, while "history, culture, and politics are irrelevant."[20]

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[18] Peter Alexis Gourevitch, and James J. Shinn, *Political Power and Corporate Control: the New Global Politics of Corporate Governance*, Princeton, NJ, Princeton, Princeton University Press, 2005, 1-2.

[19] Gerald F. Davis, "New Directions in Corporate Governanc," 143.

[20] Neil Fligstein, and Jennifer Choo, "Law and Corporate Governance," 67.

Some legal scholars such as Roe argue that the initial separation of ownership and control is not an inevitable consequence of the expansion of large enterprises, but resulted from legal and regulatory constraints that originated in populist political pressures and were sustained by politically influential corporate managers.[21] Actually, creation of the institutions of corporate governance, even in the U.S., was a political and historical accident.[22] This view suggests a move away from the mainstream thinking of the 1980s in the field of corporate governance, focused on efficiency and an individualist orientation, toward a broader political analysis. Roe emphasizes that: "The public corporation is as much a political adaptation as an economic or technological necessity."[23] Davis also takes the same direction in his framework of the politics of corporate control: "Conflicts over corporate control occur at three levels, firm, state government, and federal government. Each level presents distinctive impediments and facilitators of collective action by shareholders and managers."[24]

At the end of 1993, the World Bank organized a research project, "Corporate Governance of Transitional Economies: Insider Control and the Role of Banks." The project introduced the concept of corporate governance into studies of transition economies for policymakers.[25] Earlier discussion about corporate governance in the transitional economies by economists tried to find

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[21] Mark J. Roe, "A Political Theory of American Corporate Finance," *Columbia Law Review*, Vol.91, No.1, 1991, 10-67.

[22] Mark J. Roe, *Strong Managers, Weak Owners: The Political Roots of American Corporate Finance*, Princeton, NJ, Princeton University Press, 1994.

[23] Mark, J. Roe, "A Political Theory of American Corporate Finance," 10.

[24] Gerald F. Davis, and Tracy A. Thompson, "A Social Movement Perspective on Corporate Control," 156.

[25] Aoki Masahiko and Hyung-Ki Kim, eds. *Corporate Governance in Transitional Economies: Insider Control and the Role of Banks*, Washington, DC, World Bank, 1995.

a mechanism of supervision from the outsiders over the insiders. It involved issues such as the disadvantages of insider control, the possible role of banks in corporate governance, and comparative lessons from various practices. The discussion also explored how institutional factors, e.g. the power of government, the historical legacy and social interaction of different interest groups, affected privatization and resulted in insider control.[26] The following discussion further raised the issue of necessity for enterprise restructuring after privatization or re-engineering post-privatization ownership and the governance structure, by looking for appropriate types of owners and instituting a system of governance in which the new owners can have effective influence over the firms.[27] The basic idea of the discussion is how to transplant the portfolio of successful market economies into institutionally-culturally diversifying societies. Fox and Heller have offered a simple definition of good corporate governance: maximizing residuals (profit) and distributing the wealth to shareholders in a *pro rata* fashion.[28] Based upon a 1994 survey of 506 manufacturing firms in the Czech Republic, Hungary, and Poland, Frydman, Hessel and Rapaczynski concluded that privatized firms controlled by outside investors were more entrepreneurial than those controlled by corporate insiders or the state; all state and privatized firms in transition economies engaged in similar types of restructuring, but the restructuring of firms owned by outsider investors was

[26] Ibid.

[27] Roman Frydman, Cheryl W. Gray, and Andrzej Rapaczynski, *Corporate Governance in Central Europe and Russia: Volume I, Banks, Funds, and Foreign Investors; Volume II, Insiders and the State. Budapest,* Hungary, Central European University Press, 1996.

[28] Merritt B. Fox, and Michael A. Heller, "What is Good Corporate Governance?" in Fox and Heller, eds. *Corporate Governance Lessons from Transition Economy Reforms*, Princeton, NJ, Princeton University Press, 2006, 4.

significantly more effective (in terms of revenue generation) than that of firms with other types of ownership. Examining the impact of managerial turnover on revenue performance, as well as differences between managers of firms with different types of ownership, they found that the more entrepreneurial behavior of outsider-owned firms was caused primarily by incentive effects. The authors argued that the success of outsider-owned firms was caused by their greater readiness to accept risks (as evidenced by higher variance of revenues generated by restructuring) and a lesser need to defend, and account for, their managerial decisions.[29]

Among the transition countries, Russia is often mentioned as an example of poor corporate governance both by foreign and Russian scholars. For instance, Fox and Heller point out that the Russian experience counters recent theoretical and empirical research that argues that control by multiple large shareholders may improve firm performance.[30] Based upon studies about cases in Russia, they listed typical pathologies of corporate governance failure for transition economies: unreformable, value-destroying firms not closing; viable firms failing to use existing capacity efficiently; misinvested internally generated cash flows; failure to implement positive net present value projects; failure to identify positive net present value projects; failure to prevent diversion of claims; failure to prevent diversion of assets.[31] Fox and Heller then conclude: "The Russian experience of corporate governance is unique. No other

[29] Roman Frydman, Marek Hessel and Andrzej Rapaczynski, "Why Ownership Matters: Entrepreneurship and the Reconstructuring of Enterprises in Central Europe," in Merritt B. Fox and Michael A. Heller, eds. *Corporate Governance Lessons from Transition Economy Reforms*, Princeton, NJ, Princeton University Press, 2006, 194.

[30] Merritt B. Fox, and Michael A. Heller, "Conclusion: The Unexplored Role of Initial Conditions," 391.

[31] Merritt B. Fox, and Michael A. Heller, "What is Good Corporate Governance?" 5.

place in the world offers such ample and creative corporate governance pathologies, and nowhere else do firms have such strange boundaries and competing insiders so much control."[32] After a decade of the privatization in Russia, a Russian scholar stated: "Privately owned businesses have been the most reluctant sector of the Russian economy to adopt international corporate governance standards… The road to effective corporate governance in privately owned Russian companies will be evolutionary, and will extend over many years."[33]

Actually, Russia is not the only case of poor corporate governance. One can find from China's SOE restructuring almost everything, if not more, that happened in Russia.[34] Gallagher observes from China that "[t]he sequencing of reforms in urban areas placed liberalization of FDI first, the development of a domestic private industry second, and SOE reform and privatization last."[35] China ultimately initiated SOE privatization in 1997. Although the government does not formally use the term privatization, which suggests a significant shift from its official socialism-oriented ideology, the policy allows most SOEs to be sold off to private owners, merge, or go bankrupt, and large-scale layoffs were encouraged. Unlike Russia, China has been able to attract a large amount of foreign direct investment (FDI), therefore some

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[32] Merritt B. Fox, and Michael A. Heller, "Conclusion: The Unexplored Role of Initial Conditions," 391.

[33] Andrey Mikhaylenko, 2004, "Private Enterprise Owners and Corporate Governance," in Daniel J. McCarthy, Sheila M. Puffer, and Stanislav V. Shekshnia, eds. *Corporate Governance in Russia*, Cheltenham, UK, Edward Elgar, 2004, 197.

[34] Fei Fangyu, "*Kongzhi Neibu ren Kongzhi: Guo Qi Gaige zhong de Zhili Jizhi Yanjiu* (Controlling the Insider's Control: A Study of Corporate Governance of SOE Reform," Beijing, China, *Jingji Yanjiu* (Economic Research), No.6, 1996, 35-36.

[35] Mary Elizabeth Gallagher, *Contagious Capitalism: Globalization and the Politics of Labor in China*, Princeton, NJ, Princeton University Press, 2005, 136.

foreign investors have participated in the privatization, through grafted joint ventures between foreign and Chinese firms, the foreign acquisition of state firms and the renting of SOEs to foreigners on long-term leases, which often results in the loss of state assets either by selling the SOEs too cheaply or, worse, selling off the best parts of the SOEs too cheaply.[36] The same thing has happened when new owners are domestic, and more corruption has been reported. China's local governments are often the most ardent supporters of privatization, because it helps relieve them of their own social welfare burden.[37] Examining accounting information of 496 Chinese corporatized SOEs listed on stock exchanges during 1997 to 1999, Fan and Lau found that the data did not provide enough evidence to suggest that the corporate governance mechanism of the firms was effective. The two authors offered explanations: first, although the corporatized firms included some foreign and private business shareholders, and employee shareholders (about two percent) and individual shareholders (about 40 percent) as well, control by gaining ownership through the capital market had not been effective, as government offices and other SOEs remained large shareholders and their shares were not readily tradable; second, both inside and outside directors of their boards were often appointed through administrative decisions rather than recruited from a competitive labor market, and the supervisory boards did not have real authority to monitor operational and strategic firm behavior.[38]

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[36] Ibid, p.49.

[37] Ibid, p.51.

[38] Dennis K.K.Fan, Lau Chung-ming, and Wu Shukun, "Corporate Governance Mechanism," in Anne S. Tsui, and Lau Chung-ming, eds. *The Management of Enterprises in the People's Republic of China*, Boston, MA, Kluwer Academic Publishers, 2002, 211-240.

If the deviation of corporate governance in Russia and China from the Western model is not going to be corrected for a long period, one will have to consider it a normal state and could hardly expect the ideal model of corporate governance to dominate, which is assumed efficient from a long-run point of view. In other words, beyond economic theory and the ideals of good corporate governance, alternative interpretations about the behavior of managers, workers and outside owners in Russia and China are needed to understand the results of privatization.

When economists criticize the defective corporate governance of privatized enterprises in transition economies, some political scientists make efforts to analyze why patterns of corporate governance vary across countries. For example, Gourevitch and Shinn developed a theoretical framework that incorporates three key actors into the configuration of corporate governance, i.e., owners, managers and workers, for empirical observation. The authors suggest: "The three actors contend with each other over resources of the firm, each with a varying set of claims against the firm's revenue and profit stream. Each set of actors has preferences that set up a range of trade-offs, thus of possible alignments with the other players."[39] This framework helps explain how the actors may interact through their political coalitions. The authors not only broaden the narrower view of economics that believes corporate governance should converge to the pattern of owners dominating managers and workers, but also have offered political explanations for why corporate governance differs in various countries. Their research suggests that politics, not the legal system alone, determines the shape of corporate governance

[39] Gourevitch and Shinn, *Political Power and Corporate Control: the New Global Politics of Corporate Governance*, Princeton, NJ, Princeton University Press, 2005, 59.

systems.[40] While their comparative study in thirty nine countries convincingly analyzes features of different corporate governance patterns, its analysis of Russia and China is weak. The authors pay more attention to political institutions in consolidated market economies, especially the institutionalized role of labor unions, but leave aside the less-organized or unorganized labor negotiations that are typical in the privatization experiences of Russia and China. This approach weakens the capacity of the framework to interpret the formation of corporate governance in the two countries. Indeed, in-depth analysis of the Russian and Chinese cases is not part of the project, which focuses on models centered on multi-nation comparability.

Drawing lessons from advanced market economies, the literature in law and economics has contributed a great deal in analyzing features of the institutions of corporate governance in the US, Europe and Japan. "Institutions are explained by their function in orienting decision makers toward signals in financial markets… These institutions came to be seen as a transferable blueprint for economic vibrancy for economies around the world."[41] However, the literature does not include much about how the institutions influence, and are changed by, social actors. Particularly, the literature does not include cultural factors (such as social values) and patterns of social relationship between management and workers. For transition economies, studies of such issues are important for efforts to transplant the Western corporate governance system into societies where new market systems grow from different historical legacies. Thus it is understandable that some would argue the theory of corporate governance was "derived from

[40] Gerald F. Davis, "New Directions in Corporate Governance," 155.
[41] Ibid, 159.

the experiences of advanced market economies and is not necessarily applicable more generally in the world."[42]

Another problem with the literature is that introduction of corporate governance to the transition economies often assumes that privatized SOEs should be in the hands of outside owners. It is of course applicable to large enterprises, if institutional investors and financial market regulations are there ready to work. However, it might not be a feasible model for the privatization of many medium size or small SOEs. A lot of the medium size or small SOEs were loss-makers or survived at the margins of profitability with little transparency. In these cases, potential investors, private or institutional, if there are any, would feel reluctant to offer help. When these SOEs are privatized, outside owners very likely are missing from the beginning. Thus the privatization of such SOEs would necessarily become a game of insiders, having little to do with outside owners or the ideal model of good corporate governance designed for institutional investors.

In recent years a few sociologists entered the field of corporate law and corporate governance. Analyzing state action as a response to market factors, Kaufman explored the history of American corporate law and explained why the modern American corporation was traditionally run in the interest of management and shareholders, rather than of employees.[43] Fligstein traced the institutional development of the large American corporation from the early

[42] Merritt B. Fox, and Michael A. Heller, eds. *Corporate Governance Lessons from Transition Economy Reforms*, Princeton, NJ, Princeton University Press, 2006, vii.

[43] Jason Kaufman, "Corporate Law and the Sovereignty of States," *American Sociological Review*, Vol.73, June, 2008, 402- 425.

years to the 1980s and provided a four-part periodization of the history of the corporation.[44] Rather than perceive the contemporary structures of corporate governance as "self-evidently appropriate and inferring an 'efficient history'," the sociologists "document the critical historical junctures that shaped the developmental trajectory of the corporation."[45] There is also research on the dynamics of the board of directors, ownership, and change of control.[46] Among sociologists, Fligstein has tried to expand the understanding of institutions of corporate governance. He points out that the political system of a particular society (i.e., democracy versus dictatorship) and the existence of the rule of law are important preconditions for understanding corporate governance structures; the cultural tradition of the legal systems, such as whether they have civil or common law legal systems, is part of this apparatus as well. Fligstein also mentions that class struggle, defined as the conflict between owners and workers, plays out in the politics of societies; these conflicts and their resolution greatly affect the nature of ownership relations (including the rights of minority stockholders), the development of financial markets, and labor law. He also emphasizes that the religion of various societies plays into the political system in several ways; some religious traditions are more tolerant and promoting of wealth generation than others. Finally, he thinks that another source of social solidarity is the shared values and assumptions that people hold about one another; in societies that are homogeneous, people exhibit a great deal of trust, which presumably shapes the types

[44] Neil Fligstein, *The Transformation of Corporate Control*.
[45] Gerald F. Davis, "New Directions in Corporate Governance," 151.
[46] Ibid, 52-153.

of corporate governance that exist.[47] This framework suggests that necessary social and cultural factors should be brought into analysis of corporate governance.

2. Labor Relation Studies: Empirical Observations with a Weak Framework

Unlike corporate governance, the field of labor relations has a long tradition. In recent decades the study of labor relations receded in states with advanced market economies, as traditional manufactures moved away to developing countries and the number of factory workers kept declining, whereas such studies have become quite active in transition societies during the past twenty years. Not only have Western scholars published numerous books and articles about labor relations in Russia and China, but they were also echoed by Russian and Chinese scholars motivated by an interest in new and complicated labor issues in the privatization processes in their countries. A Chinese sociologist even suggests that scholars should "bring the working class back" to the center of sociological research in China, as more manufacturing jobs are transferred to the country.[48]

The terms "labor relations" and "industrial relations" are used to represent the same research field concerning "formal and informal dealings between workers and their managers

[47] Neil Fligstein, and Jennifer Choo, "Law and Corporate Governance," 70-71.

[48] Shen Yuan, "*Shehui Zhuanxing yu Gongrenjieji de Zai Xingcheng* (Social Transition and the Reformation of Working Class," Beijing, China, *Shehuixue Yanjiu* (Sociological Studies), 2005, No.2.

and/or employers with respect to wages and conditions of work, whether the workers are organized into trade unions or not, and whether they bargain collectively and freely, with the right to strike."[49] The term industrial relations, originating in Britain, refers to the world of work and the process of control over work relations more specifically.[50] Nowadays debate among scholars in the field has been heated, especially in the U.S., on whether the term industrial relations is outdated in an era of declining union membership. Some have adopted what is seen as the more neutral term "employment relations."[51]

According to Kaufman, in the early part of the last century this field emerged as an area of scholarly inquiry in the U.S. due to labor problems such as poor wages and working conditions and the lack of public policies governing labor markets or union representation.[52] Developed by several labor economists,[53] the field attracted increasing interest among social scientists during the latter part of the last century. American scholars usually take a narrower definition of the field, which just includes union- management relations; but researchers in other countries with an Anglo-Saxon tradition are inclined to use a broader definition that covers all aspects of employment relations. In the European continent a separate field of

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[49] Malcolm Warner, and Zhu Ying, "The Origins of Chinese 'Industrial Relations'," in Malcolm Warner, ed. *Changing Workplace Relations in the Chinese Economy*, New York, St. Martin's Press, 2000, 16.

[50] Ibid.

[51] George Strauss, and Keith Whitfield, "Research Methods in Industrial Relations," in Keith Whitfield, and George Strauss eds. *Researching the World of Work: Strategies and Methods in Studying Industrial Relations*, Ithaca, NY, Cornell University Press, 1998, 6-8.

[52] Bruce E. Kaufman, *The Origins and Evolution of the Field of Industrial Relations in the United States*, Ithaca, NY, ILR Press, 1993.

[53] William Form, "Comparative Industrial Sociology and the Convergence Hypothesis," *Annual Review of Sociology*, Vol.5, 1979, 2.

industrial relations did not exist until recently, where research on industrial relations was long subsumed under law and sociology. Before the 1940s industrial relations research in the U.S. concentrated on the legitimation of unions and social insurance institutions. After World War Two there was a lot of industrial unrest and the focus of research turned to strikes and inflation. During the 1960s it was race relations. Recently the dominant themes have been the decline of unions and the impact of participation schemes, such as work teams. Early British industrial relations research focused on unions and union-management relations during the 1960s, on shop-floor labor-management relations during the 1970s, and recently on the role of management and how work is organized.[54] It is often recognized that the field does not have a well-established theoretical base,[55] and is traditionally problem-centered, normative, historically oriented, and multidisciplinary. The field has also been closely connected with policy formulation. With such coverage works in the field have accumulated rich experience in terms of research strategy and methodology.

Thirkell, Petkov, and Vickerstaff think that comparative–labor-relations research is traditionally concerned with the extent to which labor relation models converge on a standard pattern according to the level of technological development of the economy of which they are an element. They notice that in recent times European integration has spawned discussion about the scope for the development of a pan-European approach to industrial relations, which minimizes differences between member states; and the collapse of the Soviet model of labor

[54] George Strauss, and Keith Whitfield, "Research Methods in Industrial Relations," 16.
[55] Ibid, 8.

relations also raises questions about the extent to which marketization and privatization of Eastern European economies will result in the convergence of labor relations models with Western European patterns over time. According to the authors, within the Western European literature there are various types of conceptualization of how to compare and classify labor relation models. For instance, Slomp uses a three-parties and three-levels approach (employer organizations, worker organizations, and the state), and then patterns of decision-making between the parties at central, sector, and enterprise levels, thus three broad clusters or models are clarified, i.e. the British, the German or Northern European, and the French. Similar distinctions are made by other authors between the "Anglo-Saxon" model and the "continental" model of collective bargaining, or between "contestation" and "corporatism."[56] Crouch provides a four varieties system: stable pluralist bargaining or contestation, unstable pluralist bargaining or contestation, neo-corporatism with strong labor and neo-corporatism with weak labor.[57] Such models may provide a starting point for analysis of the changes in transition societies such as Russia and China, but too much attention in searching for models may lead to a neglect of what are historically specific patterns of development in these countries.[58]

When research on industrial relations emphasizes the functioning of the formal features of employment, labor relations, and collective bargaining, industrial sociologists often use

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[56] John E.M. Thirkell, Krastyu Petkov, and Sarah Vickerstaff, *The Transformation of Labour Relations: Restructuring and Privatization in Eastern Europe and Russia*, Oxford University Press, 1998, 5-6.

[57] Colin Crouch, *Industrial Relations and European State Traditions*, New York, Oxford University Press, 1993, 43.

[58] John E.M. Thirkell, et al. *The Transformation of Labour Relations: Restructuring and Privatization in Eastern Europe and Russia*, 6.

different conceptual tools that emphasize the interrelationships among individuals and the formal and informal features of workplace organizations, while labor sociologists address issues such as comparative labor movement structure, temporal variations in strikes and labor unrest, the impact of organized labor on the degree of inequality in income and life chances, and the determinants of union democracy and oligarchy.[59] In sociological views, bureaucratic work organizations are embedded in a web of laws, formal agreements and culturally defined societal norms about informal inter-group relations.

Kochan points out that the primary feature distinguishing the field from its counterparts lies in the normative assumptions and perspectives that underlie our conceptualization of the employment relations. Industrial relations theory starts from an assumption that an enduring conflict of interests exists between workers and employers in employment relationship."[60] He thinks that the pluralist school of thought views the sources of conflict as embedded in the structure of authority relations and the separation of economic interests of workers and employers, thus perceives the parties to the employment relationship tied together in an enduring web of partially conflicting and partially common interests or objectives; on the other hand, the Marxist or neo-Marxist perspective views the source of conflict as embedded in the separation of workers from the ownership of the means of production, and considers conflict as

[59] Daniel B. Cornfield, and Melinda D. Kane, "Sociological Approaches to Employment Research," in Keith Whitfield, and George Strauss, eds. *Researching the World of Work: Strategies and Methods in Studying Industrial Relations*, Ithaca, NY, Cornell University Press, 1998, 240.

[60] Thomas A. Kochan, "What is Distinctive about Industrial Relations Research?" in Keith Whitfield, and George Strauss, eds. *Researching the World of Work: Strategies and Methods in Studying Industrial Relations*, Ithaca, NY, Cornell University Press, 1998, 37.

more all-encompassing than partial.[61] The different assumptions lead to debate between the two schools over the approach to research, the definitions of problems of interests, and the type of data viewed as valid.

The studies of labor relations did not exist for decades in the Soviet Union and China. In the Stalin era, sociological research was banned, as Stalin equated it with bourgeois influences and declared it to be "hostile to Marxist ideology."[62] In the Mao era, the situation was the same. Most scholars credit the birth of modern empirical sociology in the Soviet Union to the post-Stalin era.[63] Beginning in the late 1950s, the research on work was the first field of empirical sociology permitted by the Soviet regime. In the Khrushchev and Brezhnev era of the Soviet Union, "the sociology of work is one of the few branches of Soviet sociology which has enjoyed a relatively large degree of autonomy from direct political control."[64] Rich accumulated materials since then may help researchers today to understand the workplace in the Soviet Union/Russia. In China sociological research and teaching were resumed in the 1980s after Mao's policies were partly altered. Since the 1990s Chinese sociologists have done a lot of research on work and labor relations. The political background of the research in the Soviet Union was quite similar to that in China: on the one hand, the leadership needed an accurate

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[61] Ibid.

[62] Vladimir Shlapentokh, *The Politics of Sociology in the Soviet Union*, Delphic Monograph Series, Boulder, CO, Westview Press, 1987, 13-14.

[63] Elena I. Bashkirova, and Vicki L. Hesli, "Polling and Perestroika," in Arthur H. Miller, William M. Reisinger, and Vicki L. Hesli, eds, *Public Opinion and Regime Change: the New Politics of Post-Soviet Studies*, Boulder, CO, Westview Press, 1993, 21.

[64] Vladimir Shlapentokh, "Evolution in the Soviet Sociology of Work: From Ideology to Pragmatism," The Carl Beck Papers in Russian and Eastern European Studies, No.404, University of Pittsburgh, 1985, 3.

and objective understanding of reality in order to make effective decisions on various issues; on the other hand, the leadership wanted to suggest to the population that the Soviet or Chinese society functioned in accord with the official interpretation of social reality, and sociologists were called upon to provide "evidence" of that.[65] However, the weakness of such a direction was obvious. In 1987, a Soviet Academician, Mrs. Tatyana Zaslavskaya, who authored the Novosibirsk Report in 1985 which challenged the whole structure of the organization of the Soviet economy,[66] published critical evaluations of the official sociological establishment[67] and helped the reform regime draft the 1987 official decision to re-establish sociology as an academic discipline.[68]

Commenting on the Soviet sociological research on work motivation and attitudes in large enterprises, Clarke mentioned that one of the primary purposes of the research was to identify the causes of anti-social behavior in order to provide remedies. The work was carried out usually at the local level, through hundreds of sociology departments attached to large industrial enterprises and to regional communist party offices and that of the communist youth league schools. The vast majority of its results were not published. He pointed out that this research had a predominantly social-psychological character, and the defects of the system of production were attributed to the psychological and moral characteristics of individual workers and managers and specific deficiencies in their education and social environment. Clarke

[65] Ibid, 4.

[66] Teodor Shanin, "Foreword," in Tatyana Zaslavskaya, *The Second Socialist Revolution: An Alternative Soviet Strategy*, London, I.B. Tauris & Co. Ltd, 1990, xiii..

[67] Elena Bashkirova, and Vicki L. Hesli, "Polling and Perestroika," 25.

[68] Teodor Shanin, "Foreword," xiv.

thought that this research produced innumerable indices and correlations of satisfaction, social cohesion, labor motivation, the moral-psychological climate, and leadership qualities, and was used primarily in the attempt to improve the training and social organization of labor, as well as to identify candidates for recruitment to leadership positions.[69]

The reform in the mid 1980s created new conditions for Soviet sociological research, but many of the leading industrial sociologists turned to political issues while many enterprise sociology departments were cut back or closed; thus there was a massive decline in research and publication in the field. Clarke noted in 1995 that in post-Soviet Russia researchers did not publish any book or article that contained detailed description of analysis or was based on a detailed description of the real life of Russian industrial enterprises. During those years, the majority of publications either contained abstract theoretical analysis or were devoted to macro-economic processes in the country, using federal statistics, the results of public opinion surveys touching on industrial issues, and occasionally interviews with enterprise directors.[70]

For scholars outside the Soviet Union, studies of the organization of labor in Soviet enterprises had been severely constrained and conditioned by the sources on which they had been forced to rely. Clarke pointed out that the foundation of the Western understanding of the Soviet enterprise was laid by the classic studies of Granick, which were primarily based on press reports, and that of Berliner, based on interviews with émigrés, which focused on the management structures that developed in the 1930s. He notices that more recent studies have

[69] Simon Clarke, "Formal and Informal Relations in Soviet Industrial Production," in Simon Clarke, ed. *Management and Industry in Russia*, Aldershot, UK, Edward Elgar Publishing Ltd., 1995, 3.
[70] Ibid.

built on these classics, using the same type of sources, without modifying their essential features. The main focus of the classic studies was the horizontal and vertical connection of enterprises with other supplier and customer enterprises, state bodies and Party organizations; analysis of the internal functioning of the enterprise was sketchy.[71] On the other hand, Filtzer used an extensive range of newspaper sources, official reports and research data, and indicated that Soviet workers resisted the imposition of work and production discipline, expressed in high levels of inefficiency and lack of coordination.[72] Clarke thinks that "while Filtzer's work has been pioneering in establishing the barriers that confront central control of management and managerial control of the labour process, his interpretation is strongly influenced by the sources on which he has relied, which have primarily been those which report disciplinary violations and the negative features of worker behavior, bemoaning low levels of discipline as part of orchestrated campaigns."[73]

Since the early 1990s Clarke and his colleagues did extensive work on internal relations in Russian enterprises and published a series of books that enriched our understanding of the Russian workplace before and during the transition.[74] The books include in-depth analysis about

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[71] Ibid, 4.

[72] Don Filtzer, *Soviet Workers and Stalinist Industrialization*, London, Pluto, 1986; *Soviet Workers and Destalinisation*, Cambridge, UK, Cambridge University Press, 1992; *Soviet Workers and Perestroika*, Cambridge, UK, Cambridge University Press, 1994.

[73] Simon Clarke, "Formal and Informal Relations in Soviet Industrial Production," 4.

[74] Simon Clarke, Peter Fairbrother, Michael Burawoy, and Peter Krotov, *What About the Workers: Workers and the Transition to Capitalism in Russia*, London, UK, Verso, 1993; Simon Clarke, ed., *Management and Industry in Russia*, Aldershot, UK, Edward Elgar Publishing Ltd., 1995; Simon Clarke, ed., *Conflict and Change in the Russian Industrial Enterprise*, Aldershot, UK, Edward Elgar Publishing Ltd., 1996; Simon Clarke, ed. *Labour Relations in Transition: Wages, Employment and Industrial Conflict in Russia*,

workplace relations by Clarke and his colleagues, as well as work by Russian scholars, many of whom built their conclusions on case studies.[75] The series compliments the generalized findings from discussion on policy and formal rules, opinion surveys and media reports, revealing the informal relations and detailed stories about negotiations and conflict at the shop-floor level, an arena that was barely explored before. For example, unlike what the formal Soviet workplace relations showed, Clarke notices: "[N]ot only do managers have few sanctions and limited incentives to induce the workers to work, they also appear to have enjoyed very little authority in the eyes of the workers."[76] This turned out to be true in China's enterprises during the pre- and early reform period.

On the other hand, as the Samala Research Group in Russia maintains, in Soviet enterprises "excessively exaggerated admiration for the power of the leading person is one of the features of the psychology of Soviet workers and employees," although "charisma does not necessarily presuppose that the Director has a high degree of authority, a universal recognition of his unlimited power to determine the fate of the factory."[77] Although the Soviet model of social relations at the workplace has its national characteristics, its generalized features are more or less reflected in other societies under communist regimes. It could be said that understanding the Soviet model is a necessary starting point for comparative studies of labor

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Cheltenham, UK, Edward Elgar Publishing Ltd., 1996; Simon Clarke, *The Russian Enterprise in Transition: Case Studies*, Cheltenham, UK, Edward Elgar Publishing Ltd., 1996.

[75] Saul Estrin, Josef C. Brada, Alan Gelb, and Inderjit Singh, *Restructuring and Privatization in Central Eastern Europe: Case Studies of Firms in Transition*, Armonk, NY, M.E. Sharpe, 1995.

[76] Simon Clarke, "Formal and Informal Relations in Soviet Industrial Production," 7.

[77] The Samala Research Group, "Paternalism in Russian Enterprises: Our Understanding," in Simon Clarke, ed. *Management and Industry in Russia*, Aldershot, UK, Edward Elgar Publishing Ltd., 1995, 134.

relations in these societies, as well as for workplace studies in a single communist country. Methods employed by earlier Soviet scholars in the field have also influenced studies of the topic in other countries. For example, Walder did his well-known work about China's industrial workplace by interviewing immigrants from the Mainland China to Hong Kong in the early 1980s.[78]

The communist industrial relations system was usually dominated by leadership of the communist party, government and official labor unions, and at the workplace by the director, party secretaries and enterprise labor union officials. The labor unions were subordinated to the party and were expected to implement assigned tasks such as promotion of production, indoctrination, fringe benefits distribution and organization of participation by working people in managerial issues. Therefore the unions were not allowed to define workers' interests, nor were they supposed to protect them against the administrations at any level. In Soviet studies the role of the labor union was often interpreted as a dual function, i.e., the union represented both the workers and the policies of the party-state, though there was a tension between the two functions.[79] Clarke argued that the union was an instrument of the party-state, but in practice it was dominated by enterprise administration, thus the dual function was actually the function for the enterprise administration and that for the party-state, and the tension was between them.[80]

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[78] Andrew Walder, *Communist Neo-Traditionalism, Work and Authority in Chinese Industry*, Berkeley, CA, University of California Press, 1986.

[79] Blair Ruble, *Soviet Trade Unions*, Cambridge, UK, Cambridge University Press, 1981.

[80] Simon Clarke, "The Unions and the Working Class," in Simon Clarke, Peter Fairbrother, Michael Burawoy, and Peter Krotov, eds. *What About the Workers: Workers and the Transition to Capitalism in Russia*, London, UK, Verso, 1993, 96.

Some Russian scholars thought that paternalism was the most important feature of state management under socialism. For example, in a paper contributed by the Samala Research Group, Russian scholars emphasized the importance of paternalism: "In our opinion this concept most fully and accurately characterizes many features of the life of Russian enterprises: the strategy carried out by management, inter-relationships within the labour collective and the stereotypical expectations of workers."[81] Bizyukov so reviewed the history of paternalism: the weakening of state coercion, beginning from the 1960s, led to the strengthening of paternalistic policy both in the state as a whole and at the level of enterprise; from the 1970s this policy assumed the form of social planning; the social development plan of an enterprise was considered as the plan for the guardianship of the leader of the enterprise over the labor collective; it combined a collective agreement with a plan for the development of the personnel of the factory, covering all aspects of their work, health, welfare, housing and leisure activities; these plans were not an innovation of the enterprise administration, but a part of state policy and were financed out of the state budget. The enterprise administration was responsible to the state organs for their fulfillment.[82] Clarke depicted the details of the paternalistic practices: the Soviet enterprise was not just a unit of production, it also had extensive social and welfare functions in relation to the labor force; large enterprises provided kindergartens, nurseries, sporting and cultural facilities, housing, education and training; in the late 1980s enterprises

[81] The Samala Research Group, "Paternalism in Russian Enterprises: Our Understanding," 128.

[82] Betr Bizyukov, "The Mechanism of Paternalistic Management of the Enterprise: The Limits of Paternalism," in Simon Clarke, ed. *Management and Industry in Russia*, Aldershot, UK, Edward Elgar Publishing Ltd., 1995, 105.

increasingly provided subsidized consumer goods, food and clothing, and distributed land for allotment; thus, social benefits and entitlements, rest and holidays, sporting and cultural activities, access to consumer durables, clothing and footware, housing, health care, education, and even food, were all linked to the workplace.[83] But the social plan had the same shortages as other parts of the central planning system. As Bizyukov indicated, "Very often fewer goods were received, and their quality was worse, than that which was proclaimed… The feeling became widespread that 'the bosses provide us less and pay less for it than was agreed.'"[84] Since the 1990s many Chinese social scientists and some China scholars have analyzed the same features in Chinese work units (*danwei*) and discussed the organizational paternalism and its implications for social control and reform in China.

In contrast to the traditional three-party approach, the state, managers and labor unions, in Western industrial relations research, Clarke emphasized the importance of bringing the labor collective into the study. He emphasizes that a distinct form of the Soviet enterprise was reflected in its ideological representation, which characterized it not as an economic unit but as a "labor collective"; it was in the name of the labor collective that Soviet managers ruled the enterprise, pressed their interests against higher authorities, and subjected individual workers to managerial authority; the interests of workers in the shop were represented within the system primarily by their line managers and their demands were channeled through administrative

[83] Simon Clarke, "The Contradiction of 'State Socialism'," in Simon Clarke, Peter Fairbrother, Michael Burawoy and Peter Krotov, eds. *What about the Workers: Workers and the Transition to Capitalism in Russia*, London, UK, Verso, 1993, 24.

[84] Petr Bizyukov, "The Mechanism of Paternalistic Management of the Enterprise: The Limits of Paternalism," 106.

structures. He thought that in this way conflict between workers and management was expressed within the administration of the enterprise. Clark perceives the Soviet workplace as essentially a bureaucratic-paternalist system of conflict resolution, based on the exclusion of any forms of independent worker representation.[85] As a center-piece of the Soviet reform strategy in the early 1980s, the Labor Collective Council (*STK*) was introduced into enterprises. The 1987 Law on State Enterprise sought to generalize some of the more radical experiments in workers' representation. "These reforms had not been designed to increase workers' power, but to encourage workers to show more initiative in production, and to respond more positively to material incentives."[86] Frustration at the failure of the reforms to respond to the aspirations that they had aroused was an important factor in leading workers to take independent action, outside all institutional channels, and was a major source of the discontent that exploded in the miners' strikes in 1989.[87]

The incentive system was a key area for researchers of the Soviet labor relations. Briefly reviewing the pre-reform payment system and its limited changes during *perestroika* (reform), Vadeneeva mentioned that traditionally managerial authority was supposed to be imposed in the Soviet system by piece-rate systems of payment of wages and bonuses; until the 1970s these systems were primarily individual, but from the late 1970s there was a rapid shift to collective

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[85] Simon Clarke, "The Contradiction of 'State Socialism'," 25-27.

[86] Simon Clarke, and Peter Fairbrother, "The Origins of the Independent Workers' Movement and the 1989 Miners' Strike," in Simon Clarke, Peter Fairbrother, Michael Burawoy, and Peter Krotov, eds. *What About the Workers: Workers and the Transition to Capitalism in Russia*, London, UK, Verso, 1993, 123.

[87] Theodore Friedgut and Lewis Siegelbaum, "Perestroika from Below: The Soviet Miners' Strike and Its Aftermath," London, UK, *New Left Review*, No.181, 1990, 13.

piece-rates with the move to the brigade system. The author emphasized that in practice there was a considerable gulf between the formal payment system and its practical implementation. In practice the system tended to be subverted by line managers who had to make substantial concessions to the workers under their command, individually and collectively, in order to retain their collaboration in the battle for the plan; and, on the other hand, workers tended to receive the normal wage regardless of their individual productivity. The outcome was that there was only a weak relationship between effort and reward. According to him, the program of *perestroika* was linked from the very beginning to proposals to improve production discipline and to replace the principles of "leveling" by principles of "social justice" in the system of wage payment; however, there had been few effective attempts to introduce new payment systems.[88]

Substantial changes occurred after communist regimes collapsed in the former Soviet bloc. Thirkell, Scase and Vickerstaff summarized some common features of the changes in Russia and Eastern Europe: the post-communist governments viewed the development of new institutions of labor relations as secondary to economic reform, and the emerging patterns of labor relations were shaped by the legacies of the communist past, domestic political and economic processes, and the West European models of labor–management relations.[89] In January 1992, the Russian Federation's trilateral commission (government, business, and labor)

[88] Valentina Vedenneva, "Payment Systems and the Restructuring of Production Relations in Russia," in Simon Clarke, ed. *Management and Industry in Russia*, Aldershot, UK, Edward Elgar Publishing Ltd., 1995, 224-225.

[89] John E. M. Thirkell, Richard Scase, and Sarah Vickerstaff, eds. *Labour Relations and Political Change in Eastern Europe: A Comparative Perspective*, London, UK, UCL Press, 1995.

for the regulation of social-labor problems began operations. This was a corporatist design of a Western European social-democratic model. Ultimately, "the commission became a venue for huge concessions on the wages for militant workers in critical industries, rather than a regulator of their demands…and [there was] no evidence that labor become united".[90] By the end of the year, it turned out that trilateral corporatism had failed. Scholars of labor relations in transition societies often focus on labor politics, i.e., what policy is adopted concerning labor and how workers respond, at a nationwide level with generalized descriptions and conclusions, often supported by media information. While workers' positions dramatically changed during the privatization, such a focus often underestimates the role of change of property rights in labor politics. Moreover, the role varies in different enterprises, as situations and nominal and real privatization schemes differ.

Only a few researchers have done case studies on labor relations. According to the observation of Clarke in 1993 at the workplace in Russia, directors of the enterprises had to look to the support of the labour collective, exploiting his traditional position as its paternalist representative; directors did everything in their power to preserve the existing social relations of production on which their power was based and in which their authority was embedded. Clarke noted that the existing form of social relations of production within the enterprise determined both the form and the limits of independent worker organization in the breakdown of the Soviet system, and there was a constant tendency for emerging class conflict to be displaced and

[90] Walter D. Connor, "Labor Politics in Post-communist Russia: A Preliminary Assessment," in James R. Millar, and Sharon L. Wolchik, eds. *The Social Legacy of Communism*, New York, the Woodrow Wilson Center Press and Cambridge University Press, 1994, 344.

re-absorbed into the existing structures of power, as foremen, shop chiefs, directors or outside political figures proclaimed themselves patrons of the workers, representing their just demands within the framework of the existing structures of power. The author thought that this was a major obstacle to any attempt to develop independent working class organization. On the other hand, he emphasized that such patterns of conflict equally tended to set strict limits to the activities of the industrial *nomenklatura* to transform itself into a capitalist class, as any direct confrontation with the labour force immediately undermined the foundation of managerial authority, leading to the emergence of competitors for power within the hierarchy, who represented themselves as defenders of the collective interest.[91] Somewhat different from the observation of Clarke, when analyzing strikes in the early 1990s, a Russian scholar pointed out that Russian managers had an obvious interest in the success of such strikes, during which demands to increase the resources granted to enterprises were put forward. "This is very clear in all the material on the miners' movement, where the enterprise directors participate in the strikers' negotiations with the government, helping to work out their packages of demands."[92] Moreover, when privatization was introduced in Russia, the common interest of managers and workers often prevailed over their opposition.

Later, in 1996, Clarke concluded from case study materials that the collapse of the party and the disintegration of ministerial structures removed the external constraints on managers,

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[91] Simon Clarke, "The Contradiction of 'State Socialism'," 27-28.

[92] Vladimir, Iiyin, "Social Contradictions and Conflicts in State Enterprises in the Transition Period," in Simon Clarke, ed. *Conflict and Change in the Russian Industrial Enterprise*, Aldershot, UK, Edward Elgar Publishing Ltd., 1996, 39-40.

and their power did not increase much though no effective trade unionism emerged. Having lost the support to their authority from the Party and state bodies, the managers worked on restoring their power during the enterprise restructuring process, at the same time on securing financial resources to allow them to survive.[93] Holding down and not paying wages, encouraged by tax and redundancy legislation which gave enterprises a strong incentive to keep low-paid workers on the books to reduce the enterprise's liability to the excess wage tax and to avoid the obligation to pay compensation for redundancy, managers had to deal with an increase in labor turnover as the skilled and younger workers left for better paying positions.[94]

Clarke and his Western and Russian colleagues pointed out the complexity of strategies both managers and workers adopted during privatization; but they did not make efforts to understand how the behavior of managers and workers affected the privatization process and its outcomes. Obviously, the post-Soviet worker-management relationship is significantly different from the expectation of many Western labor relation scholars who believed that removing the power of the party-state would soon lead to the emergence of the Western European model of labor relations. The paternalism function of enterprises, the legacy of the Soviet workplace culture, the common interests and possible tension between managers and workers, and many other factors as well, twisted together and shaped the course of privatization.

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[93] Simon Clarke, "Labor Relations and Class Formation," in Simon Clarke ed. *Labour Relations in Transition: Wages, Employment and Industrial Conflict in Russia,* Cheltenham, UK, Edward Elgar Publishing Ltd., 1996, 6-7.

[94] Ibid, 10.

The pre-reform worker-state relationship in China is well categorized by Walder as organized dependence on the workplace.[95] Since the mid 1980s, China's SOE managers who were still largely integrated into the party-state apparatus had been gradually offered a kind of management autonomy, which gave them more power at the expense of workers. From 1993 employment reform had been accelerated in China and SOE employees were shifted into a kind of work contract system. At the same time, selected large SOEs were restructured into corporations with a variety of new ownership patterns, but the labor unions and the Workers' Congress in the enterprises maintained the Soviet role of transmission-belts and rubber-stamps.[96] From 1997 the government carried out the widespread privatization of SOEs. Before and after the privatization campaign was implemented, the developmentalist managerial ideology in China justified the contractualization and commodification of SOE workers and asked them to make sacrifices for the survival of their enterprises, while official media repeated the message that workers were no longer protected from the market and those who continued to wait passively for the state to distribute new jobs would lose out in the new economy.[97]

As privatization policy caused increasing workplace conflicts and protests, workplace studies in contemporary China have become a recent heated topic for sociologists outside and inside the country. More Chinese sociologists (including those in Hong Kong and Taiwan) are now involved in international collaboration with their outside colleagues, and their knowledge

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[95] Andrew Walder, *Communist Neo-Traditionalism, Work and Authority in Chinese Industry*.

[96] Malcolm Warner, and Zhu Ying, "The Origins of Chinese 'Industrial Relations'," 24-28.

[97] Mary Elizabeth Gallagher, *Contagious Capitalism: Globalization and the Politics of Labor in China*, 148-149.

and access to the workplace contributes greatly to the understanding of the changing labor relations in China. Lee has so described the latest development in the research field: the Chinese workplace is now treated as an organizational arena, where employment relations, labor processes, occupational culture, and identities are formed, and not merely as a political site for state-sponsored clientelism and ideological and political control; now broad questions of workplace practices, alienation and exploitation, professional autonomy, managerial strategies, workplace culture, contestation over the labor process, and the constitution of interests and identities related to class, community, ethnicity, and gender have been addressed.[98] Among the research issues, labor relations studies in privatized SOEs often focus on two dimensions: how economic reforms eroded the iron rice bowl system of employment and changed the Chinese workplace (*danwei*), and how labor conflicts cause workers' resistance and protests. Unlike some economists who tend to explain how successful China's transition is, sociologists and political scientists in the field pay more attention to changes in the legal environment at the workplace and workers' response to state policies and managerial mistreatment.

Lee points out that in the reform period labor discontent and workplace tensions were primarily the product of layoffs, bankruptcies, insecurity of jobs and rewards, the failure of enterprises to pay wages over months and even years, the non-payment of benefits accumulated over a lifetime of labor, and the unsettled nature of legal and organizational frameworks regulating work relations and workers' rights; on the other hand, there was a shift from state to

[98] Lee Ching Kwan, "Mapping the Terrain of Chinese Labor Ethnography," in Lee ed. *Working in China: Ethnographies of Labor and Workplace Transformation*, London and New York, Routledge, 2007, 1-2.

enterprise responsibility for securing welfare and wage payment. She thinks that both trends deepened workers' sense of powerlessness, particularly when China's legal system has proven to be quite ineffective in defending workers' legal rights.[99] Gallagher emphasizes that the basic characteristics of contemporary labor relations in China include substantial managerial control and autonomy, the atomization and fragmentation of the workforce through the individual contract system, and management domination or suppression of worker organization.[100]

Gallagher have analyzed the legal environment of China's contemporary labor relations: in practice institutions designed to protect workers are instead used against them; local enforcement of the labor law and other regulations is extremely weak and compromised by the need to attract and retain investment and grow the local economy; implementation of China's legal framework for labor has mainly succeeded in fulfilling the needs of enterprise managers—by shortening and attenuating the employment relationship, rather than increasing the rights of workers; cozy government-business relations and deep-seated corruption further weaken the state's capacity to provide legal institutions and a regulatory framework that can adequately protect the weaker signatory of the labor contract: individual workers.[101]

A lot of studies on the changing industrial relations in SOEs suggest that Chinese workers in labor conflict are often not engaged in collective mobilization; instead, they tend to join protests individually without a well organized plan or a responsible leader, and in so doing protect themselves from possible political repression. In a few cases where protests did produce

[99] Lee Ching Kwan, "Mapping the Terrain of Chinese Labor Ethnography," 4-5.
[100] Mary Elizabeth Gallagher, *Contagious Capitalism: Globalization and the Politics of Labor in China*, 64.
[101] Ibid, 77-78.

their leaders, the government compromised first with the protesters, then, when the workers were dismissed, arrested the leaders and charged them, leading to long sentences.[102]

The role of labor unions in China's privatization is hotly debated. When Chan and some Chinese scholars maintain that official labor unions and the Workers' Congress in China could play an active role in improving the workers' situation,[103] some observers like Gallagher and Lee emphasize the weak independent role of these institutions. Gallagher suggests that SOE unions are increasingly incorporated into the enterprise management structure, and this incorporation process, often coinciding with a period of restructuring, can grant the union an official position within a reformed firm, but it remains a weak junior partner vis-à-vis management.[104] She cites Yasumuro's observation that most union officials in foreign invested enterprises and SOEs now jointly serve in management positions, most often in human resources and personnel,[105] and concluded that the practice of joint positing dilutes the power of the union.[106] Moreover, many large multinationals seem to welcome the role played not only by the firm's branch of the official All-China Federation of Trade Union (ACFTU) but also by the communist party: these organizations employ traditional Chinese socialist methods (thought

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[102] In her book *Against Law: Labor Protests in China's Rustbelt and Sunbelt* (Berkeley, CA: University of California Press, 2007), Lee mentioned the fate of two workers' leaders in Liaoyang City. The case was widely reported in the media of the West.

[103] Feng Tongqing, ed. *Zhongguo Jingyan: Zhuanxing Shehui de Qiye Zhili yu Zhigong Minzhu Canyu* (China's Experience: Workplace Governance and Workers Democratic Participation in Transitional Economy), Beijing, China, Social Science Academy Press, 2005, 2.

[104] Mary Elizabeth Gallagher, *Contagious Capitalism: Globalization and the Politics of Labor in China*, 89.

[105] Yasumuro Kenichi, ed. *China's Labor-Capital Relations and on the Ground Management*, Tokyo, Japan, Hakutoshobo, 1999, 56.

[106] Mary Elizabeth Gallagher, *Contagious Capitalism: Globalization and the Politics of Labor in China*, 90.

work, propaganda, tight organization) to train the workforce to accept their role in the factory as loyal employees of a foreign company that often has extremely high demands and an exhausting work schedule. Gallagher thinks that this is an ironic marriage of neoliberal capitalism with socialist tools of control.[107] Lee finds that, rather than working with official labor unions or the Workers' Congress, self-mobilized "workers are testing old and new cognitive, moral and action frames inadvertently provided by state ideologies, to find out which ones work under what conditions at a time when institutions are in relative flux."[108] She also points out that "ever cautious of the heavy hand of a repressive state authority, workers rarely dare to pursue lateral mobilization across factories, limiting themselves instead to localized disruption that they hope can generate social and political pressure on local officials."[109] A lot of labor disputes during China's privatization are implicitly addressed at a core issue: "Who ought or ought not to be profiting from the wealth accumulated under socialism—the former managers of state firms? Foreigners? The general public?"[110] The issue is very important because it refers to the guidelines of privatization. However, it turns out that the Chinese government is reluctant to make the answer clear.

In most labor relation studies, what Chinese workers expect can be found from interviews and opinion survey data, but what managers think about it and what they have done remain

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[107] Ibid, 92.

[108] Lee Ching Kwan Lee, *Against Law: Labor Protests in China's Rustbelt and Sunbelt*, Berkeley, CA, University of California Press, 2007, 26.

[109] Ibid, 28.

[110] Katherine Verdery, *The Vanishing Hectare: Property and Value in Post-Socialist Transylvania*, Ithaca, NY, Cornell University Press, 2003, 74-75.

ambiguous. Exploration of answers to these questions has to do with in-depth analysis of managers' responses to the privatization policy. An interesting difference between the protests of Russian workers and that of their Chinese counterpart is that the latter more often blames their managers than the former does, which also suggests a focus for studying managerial behavior. In contrast to Russia and Russian scholars, China and Chinese scholars working on workplace issues conduct interviews more often with workers, but less with managers, while managers' strategies are often taken for granted as a generalized pattern. On the other hand, China and Chinese scholars pay more attention to workers' appeals to government, but less to the relations between workers and management during privatization, as if the privatization process in each enterprise is simply a result of state policy with little variation or deviation. In other words, in the studies of the Chinese workplace the role and behavior of managers is often interpreted as an abstract formality, if not missing. There are two reasons for this feature. First, the labor issue is the primary concern of their research. Second, investigation of managers' attitudes and activities is more difficult in China than in Russia, especially where worker discontent originates from the corruption of managers. Labor disputes are a result of the interaction between workers and managers. When pointing out the sources of workers' grievances, such as nonpayment of wages, pensions and other welfare, the scholars of China's labor relations often do not develop a detailed analysis of managers' activities, nor do they explain why Chinese workers do not reach a consensus with managers, even though some indicate that "when workers protest, their targets have always been enterprise managerial cadres

and their superior officials in local labor bureaus."[111] Without interpreting what is going on at the workplace before labor disputes take place, one may miss a key part of the whole story at the enterprise level.

3. Understanding the Attitudes of Workers and Managers: A Missing Mission

A large-scale privatization process in a short period involves hundreds of millions of participants from policy makers, government officials, investors, to workers and managers. No matter whether workers have opportunities to make their decisions in the process, their attitudes reflect their positive or negative evaluations about the process and results of privatization. If workers and managers are given options in a privatization process, their attitudes towards the privatization may largely shape their actions. In order to understand their attitudes, we have to learn the relationship between the attitudes and the long existing SOE system under state socialism. Although one's attitude may flow to a certain degree from his values and may shift in reaction to changing events, values and beliefs about the world stem from an individual's most basic socialization and psychological orientations; they are the least malleable of the components of people's opinions.[112] Melville points out that the dominant Soviet political culture has very deep Russian roots and demonstrates some continuity with basic traditional

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[111] Lee Ching Kwan, *Against Law: Labor Protests in China's Rustbelt and Sunbelt*, 21.

[112] William M. Reisinger, "Conclusion: Mass Public Opinion and the Study of Post-Soviet Societies," in Arthur H. Miller, William M. Reisinger, and Vicki L. Hesli, eds, *Public Opinion and Regime Change: the New Politics of Post-Soviet Studies*, Boulder, CO, Westview Press, 272.

values and beliefs: individual and community tend to delegate their interests and rights to the state; and individuals tend to seek spiritual freedom rather than legal rights protected by law.[113] Such phenomena can be found in China as well. The observation suggests that workers' beliefs and values may be of more or less systematic characters shaped by the sociopolitical structure, and their interests and means for the realization of their objectives may have some common features in privatization. Obviously, analysis of the attitudes of workers and managers in privatization should be a central task.

In the field of employment relationship studies, employee attitude surveys have been widely adopted in the West.[114] By designing questionnaire to measure values, attitudes and opinions of employees, researchers identify individual attitudes, aspirations, motivations and needs. Kaufman suggests that since industrial relations is concerned with human behavior in the context of the world of work, all industrial relations research that seeks to deduce a test "if A then B" must contain or be based on an underlying model of human psychology.[115] The application of psychology to studies of the workplace results in a wide diversity of important research issues such as inequality, injustice, job dissatisfaction, alienation, and resistance to

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[113] Andrei Yu. Melville, "An Emerging Civic Culture? Ideology, Public Attitudes, and Political Culture in the early 1990s," in Arthur H. Miller, William M. Reisinger, and Vicki L. Hesli, eds, *Public Opinion and Regime Change: the New Politics of Post-Soviet Studies*, 59.

[114] John Hartley, and Julian Barling, "Employee Attitude Surveys," in Keith Whitfield, and George Strauss, eds. *Researching the World of Work: Strategies and Methods in Studying Industrial Relations*, Ithaca, NY, Cornell University Press, 1998, 157.

[115] Bruce Kaufman, "Models of Man in Industrial Relations Research," *Industrial and Labor Relations Review*, Vol.43, No.1, 1989, 73-74.

control.[116] This approach has also been used by some scholars to analyze the attitudes of workers in Eastern European countries.[117] However, in the literature about the privatization in Russia and China, study of the attitudes and opinions of workers and managers is seemingly missing. Many of the researchers pay a lot of attention to the ideas and decisions of policy makers in privatization; occasionally they mention the attitudes of managers obtained from individual interviews, but rarely do they take workers' attitudes and opinions into consideration. Without analyzing the patterns of the attitudes and opinions of workers and managers towards privatization schemes, the research is much less effective in explaining what workers and managers like and want in privatization, and how they evaluate the results of privatization. Understanding the patterns of the attitudes of workers and managers is no doubt a necessary step to analyze the roles of workers and managers in privatization, and a precondition to propound how privatization is actually operated and why the results of privatization are often different from the designated policy goals.

Organizing nationwide attitude surveys is usually very expensive and difficult. The researchers of privatization in Russia and China usually rely upon case studies, mainly based on interviewed managers. Such case studies provide rich materials for in-depth analysis, particularly helpful for foreign researchers who know little about the minds of workers and managers in the countries. If the researchers want to claim typicality or respresentativeness of

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[116] Stephen M. Hills, *Employment Relations and the Social Sciences*, Columbia, SC, University of South Carolina Press, 1995, 126.

[117] Duncan Gallie, Dobrinka Kostova, and Pavel Kuchar, "Employment Experience and Organizational Commitment: An East-West European Comparison," *Work, Employment and Society*, Vol.13, No.4, 1999, 621-641.

their findings from case studies, they may benefit from employing analysis of workers' attitudes. However, in the literature of privatization in the two countries researchers often do not discuss workers' attitudes, nor do they pay enough attention to workers' attitudes towards the changes and lack of change at the workplace. Actually, public opinion surveys conducted both in Russia and China have offered rich data about the attitudes of workers and managers before, during and after privatization. However, scholars who studied the privatizations have not utilized the available data. Probably the complicated background of opinion data in the two countries has made them hesitant to conduct data analysis. Indeed, without tracing back to the history of the public opinion studies in the two countries, one may find himself often confused with the purposes, quality and usability of the survey data.

Both the Soviet Union/Russia and China had developed public opinion surveys after the Stalin or Mao era. The appearance of public opinion survey was actually a result of the intelligentsia's efforts and the need for pragmatic consideration by the regime. After totalitarian rule was loosened, the regimes realized the necessity to know what people thought in response to various polices. When the intelligentsia tried to increase the transparency of society, the regime was interested in improving its rule by reading people's real thinking. The political atmosphere in the last years of the Soviet Union and the new era of the democratizing Russia had been very beneficial for the development of public opinion surveys and studies; however, the atmosphere in China has created a lot of difficulties for investigators and researchers.

One of the great pioneers of public opinion research in the Soviet Union is Boris Grushin.[118] He started research in late 1950s. With his tireless efforts, the first organization for the study of public opinion in the Soviet Union, the Institute of Public Opinion, was established in May 1960, under the newspaper of the communist youth league, *Komsomol'skaya Pravda (The Communist Youth Truth)*, and Grushin was its director. The first survey was carried out in May of the year with a subject "Will Mankind be able to Prevent a World War." The institute existed about eight years, during which period it took 20 national surveys and an international survey.[119] But the results of the surveys were not allowed to be published, as the information obtained from the surveys, according to Grushin, "either tended toward anti-propaganda because it focused not so much on the successes of Soviet society but on its failures and chronic ailments, or else it suggested solutions to problems that fit in poorly or not at all with the dominating ideology in society."[120] Two years after the first organization for public opinion study was closed down, Grushin organized another one, the Center for the Study of Public Opinion in 1969, under the Institute for Concrete Social Research of the Soviet Academy of

[118] The papers of Dr. Boris Andreevich Grushin written during the period from 1960 to 1974 in Russian are reserved at the Hoover Institution Archives of Stanford University. From Sept. 1996 to Jan. 1997, he had been invited to the Dept. of Sociology of Princeton University to offer a lecture about the Soviet/Russia public opinion surveys.

[119] V. Z. Doktorov, "He Studied People's Opinions 'Without Mercy, in Spite of Everything', to the Memory of Boris Andreevich Grushin (1929-2007)," Moscow, Russia, *Sotsiologicheskii Zhurnal* (The Journal of Sociology), No.4, 2007, cited from its English translation in *Sociological Research*, Vol.48, No.2, March-April, 2009, 15.

[120] Boris Andreevich Grushin, "*Chetyoe Zhizni Rossii v Zerkale Oprosov Obshchestvennogo Mneniia: Zhizn' 2-ia, Epokha Brezhneva* (Four Lives of Russia in the Mirror of Public Opinion Surveys: Life Two, The Brezhnev Era)," Moscow, Russia, Progress-Traditsiia, Part 1, 27; cited from V. Z. Doktorov, "He Studied People's Opinions 'Without Mercy, in Spite of Everything,' to the Memory of Boris Andreevich Grushin (1929-2007)," *Sociological Research*, Vol.48, No.2, March-April, 2009, 15-16.

Sciences. The second organization for public opinion studies survived for three years. During this period, it conducted 23 questionnaire surveys, nearly 10,000 personal interviews, and 18 studies of the content of the press and radio broadcasts. In the spring of 1971, it carried out its first nationwide representative opinion survey with a sample of 2,000 interviewees. Once again, due to financial, cadre and organizational difficulties, the institute was closed and its data was not published.[121] Grushin's doctoral dissertation titled "Problems of the Methodology of Public Opinion Research" defended in January 1967, served as an introduction to the study of public opinion in the Soviet Union for many years. "This book could have become a standard textbook, but it never did; the authorities did not deem it necessary to train specialists in that field."[122] For the communist regime, public opinion studies were supposed to be used for improving the ruling methods of the party-state, but not for the interests of the public. During the 1970s, the results of sociological research in the Soviet Union were published mainly in specialized scientific journals with a narrow circulation, and very rarely in the public press; parts of the data were used by political authorities in various state and communist party documents, including official reports and speeches by political figures, but the data characterizing negative attitudes towards Soviet society were not incorporated into the official documents.[123] "The rare published findings of these early studies either did not report responses related to political

[121] V. Z. Doktorov, "He Studied People's Opinions 'Without Mercy, in Spite of Everything', to the Memory of Boris Andreevich Grushin (1929-2007)," 17.

[122] Ibid, 18.

[123] Elena I. Bashkirova, and Vicki L. Hesli, "Polling and Perestroika," in Arthur H. Miller, William M. Reisinger, and Vicki L. Hesli, eds, *Public Opinion and Regime Change: the New Politics of Post-Soviet Studies*, Boulder, CO, Westview Press, 1993, 23.

issues or else they were presented in such vague terms that it was difficult to draw meaningful conclusions."[124]

Gorbachev's policies of *perestroika* (reform) and *glasnost* (transparency) ushered in an entirely new phase for the study of public opinion: "With the onset of *perestroika* and the introduction of the goal of democratizing all aspects of political, economic and social life, public opinion became a crucial instrument of political power and rule by the people."[125] As the media regularly reported the results of public opinion polls, such surveys provided feedback to the regime and to public organizations, while shaping the attitudes of the people.[126] In 1988 foreign researchers finally got access to the public opinion data generated by Soviet sociologists, as the Institute of Applied Sociological Research of the Soviet Academy of Sciences began to assist joint USSR-Western polling projects.[127] At the same time Grushin helped create the largest and most successful organization for the study of public opinion surveys in the Soviet Union/Russia, the All-Union Center for the Study of Public Opinions. In 1993 it was renamed the Russian Center for Public Opinion Research (*Vsyarossiskii Tsentr Izuchenya Obshestvennogo Mnenya, VCIOM*)). In 2007 Grushin reviewed the difficult process to establish such an organization. One of the difficulties, which he could not overcome personally, was that, even though his project was taken into consideration, he had to wait for the decision of the

[124] Ibid, 24.
[125] Ibid, 17.
[126] Ibid, 18.
[127] Ibid, 24.

party-state apparatus to select an official roof (or nanny) for the organization.[128] The communist regime never allowed an independent civil organization to conduct public opinion survey without supervision by governmental organizations or institutions affiliated with the government. Finally, the Soviet party-state apparatus chose a roof for the Center, the All-Union Central Council of Trade Union, which, according to Grushin, was "full of holes."[129] On the insistent recommendation of Grushin, Academician Tatyana Zaslavskaya was appointed as the first director of the VCIOM; she enjoyed enormous scientific and moral authority not only among social scientists but also in the community of the country's intelligentsia as a whole.[130] Later, more such organizations grew out in Russia, such as the Levada Center, the Public Opinion Foundation, and many regional research firms and organizations. Zaslavskaya devoted a lot of her time to the VCIOM,[131] and led the organization through the difficult transition period from the Soviet empire to the democratizing Russia. It must be understood that getting survey workers, performing data processing and analysis, and obtaining sufficient financial

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[128] Boris Andreevich Grushin, "On the Distant and Near Approaches to the Creation of VCIOM," Moscow, Russia, the Iurii Levada Analytical Center and the Interdisciplinary Academic Center for Social Sciences, *Vestnik Obshchestvennogo mneniia. Dannye, Analiz, Discussii* (Bulletin of Social Opinion: Data, Analysis and Discussion), 2007, No.5, 55-64; cited from its English translation in *Sociological Research*, Vol.48, No.2, March-April, 2009, 37.

[129] Ibid, 39.

[130] When Zaslavskaya was asked to organize the country's first specialized system to measure public opinion, she agreed, "but on the condition that Boris Grushin be appointed deputy director." Grushin worked there for just two years. During the sad days when she bade him farewell Zaslavskaya said, "he is the one to credit for the creation of VCIOM as a modern organization for the study of public opinion." See V. Z. Doktorov, "He Studied People's Opinions 'Without Mercy, in Spite of Everything', to the Memory of Boris Andreevich Grushin (1929-2007)," 17-18.

[131] Tatyana Zaslavskaya, *The Second Socialist Revolution: An Alternative Soviet Strategy*, London, UK, I.B. Tauris & Co. Ltd, 1990, 222.

resources to maintain its operation were very difficult jobs for Zaslavskaya and her colleagues when Russia was experiencing the transitional economic recession.[132] But they succeeded.

During the last years of the Soviet Union from 1989 to 1991, the survey results of the VCIOM had been circulated among Russian sociologists and were often reported in the media. "Censorship became the exception rather than the rule, even when the data revealed public pessimism or declining trust in the Communist Party or the government. Practically no limitation existed on the publication of the results of any sort of public opinion poll."[133] It was only after 1993 that the VCIOM began to publish its survey results systematically and periodically, while the VCIOM and another non-profit organization, the Interdisciplinary Academic Center for Social Sciences (InterCentre), carried out a program of regular public opinion survey and data analysis. The purpose of the program is to "provide the Russian public, the scientific community, institutions of power and mass media with full and continuously renovated information about changes in the social-economic situation, opinions, interests, orientations and behavior of the most important social, demographical, regional, economic and other population groups."[134]

The aggregate data from VCIOM surveys and some brief analyses about the data were periodically published in an informative bulletin *Economic and Social Change: The Monitoring of Pubic Opinion (Monitoring Obshchestvennego Mneniia)*, a bimonthly publication. Since then, the publication has never been interrupted, though after 2004 it includes less and less data but

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[132] In summer of 1995, when the author interviewed Tatyana Zaslavskaya in Moscow, the problems were discussed.

[133] Elena I. Bashkirova, and Vicki L. Hesli, "Polling and Perestroika," 26.

[134] The Interdisciplinary Academic Centre for Social Sciences, Moscow, Russia, *InterCentre*, 1994, 22.

more analytical essays. The collection of the periodical, particularly those issues from 1993 to 2003, provides rich materials for analyzing public opinions on various issues. The aggregated data are often sorted by several categories such as age, education, job, sectors of industries, and region. A lot of Russian scholars use the data for their research on public attitudes towards democratization, marketization and social changes; but it seems that few Western scholars have noticed the data, and rarely have they used it in their work. An advantage of the VCIOM opinion survey data for researchers is that it periodically lists the same questions in the questionnaires, so the time series of the data provide an opportunity for dynamic comparison. Following the tradition of Soviet sociological research, the VCIOM has paid a lot of attention to employee attitudes about various issues at the workplace. In November of 1989 and December of 1990, it conducted surveys on privatization, and from 1992 to 1995 it repeated a set of questions in its surveys about the attitudes of SOE managers and employees towards privatization. It also asked questions in terms of issues at the workplace from 1992 to 2003, thus making it possible for scholars who are interested in the topics to conduct their own studies.

Most researchers of public opinion in the West hold that public opinion can only exist in a public sphere. It is certainly true that in a free society people are more likely to say what they think and believe. But in a communist country or a democratizing former communist country, political intervention may restrict the range and content of opinion surveys, and interviewees may withhold reporting some opinions. In such a political environment, bias of the opinion data may mislead researchers. Lubrano identifies four factors that limited the effectiveness of opinion survey research in the Soviet Union: the politicization of the profession, which limited

both the choice of research questions and the dissemination of results; the limitation of most studies to regional samples, e.g. often in Moscow and Leningrad area, not representing opinions of other areas; the potential distortion of responses because of poorly worded questions or fear of reprisal; and the unevenness in the quality of data analysis.[135] The first factor reflects how political intervention affects the arena of public opinion survey, and other three factors refer to problems of survey methods. Shpapentokh also mentions that the Soviet sociologists often presented "their research as related to economic and divorced from politics and ideology."[136] In the last years of the Soviet Union the political intervention in public opinion survey organization gradually reduced, and then eventually receded after Russia began its democratization. But Shpapentokh points out that, even right before the Soviet Union collapsed, "although the state no longer determined the topics to be analyzed, or the way in which the results were presented," "questions which were extremely controversial or questions which were likely to 'offend superiors' could be excluded from the interview schedule."[137]

In democratic societies, researchers of public opinion are always careful with how well respondents are motivated to participate and to give honest answers, and how they can be made to communicate their inner world.[138] This concern is often expressed when opinion surveys are

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[135] Linda Lubrano, Wesley Fisher, Janet Schwartz, and Kate Tomlinson, "The Soviet Union," in William A. Welsh ed. *Survey Research and Public Attitudes in Eastern Europe and the Soviet Union*, New York, Russell Sage Foundation, 1981, 14.

[136] Vladimir Shlapentokh, *The Politics of Sociology in the Soviet Union*, Delphic Monograph Series, Boulder, CO, Westview Press, 1987, 18.

[137] Ibid, 204.

[138] John Hartley, and Julian Barling, "Employee Attitude Surveys", in Keith Whitfield, and George Strauss, eds. *Researching the World of Work: Strategies and Methods in Studying Industrial Relations*, 158-159.

conducted in a communist country, because "the government controlled press exploited the ignorance of the citizenry by stressing the 'unity of socialist society' and its 'solidarity in supporting the Party'"[139] and dissident voices were frequently punished, while people were used to engaging in public discourse that was officially acceptable. In the Soviet Union/Russia, political liberalization in the latter half of the 1980s and the collapse of the communist regime gradually removed the political pressure against free speech and released people from the worries about being punished for free expression; thus "people now are more willing to participate in public opinion polling, to talk frankly, and to express themselves."[140] Hahn described his observation: when he accompanied his Soviet colleagues to verify the interviews results they had done, his impression was that most respondents welcomed the opportunity to be interviewed and it was often difficult to get the respondents to stop giving their opinions; "The 'fear' factor, according to which Soviets would be reluctant to share their political views because of past danger to those doing so, may be overestimated in some Western analysis."[141]

Beyond the issue of political intervention in public opinion survey, researchers in this field should be reminded that Russian respondents may have a desire to "give a good performance, please the interviewer, or demonstrate political, national or cultural loyalty."[142] A Russian sociologist so explains: this attitude is deeply rooted in Russian culture, and Russians

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[139] Timur Kuran, *Private Truths, Public Lies: The Social Consequences of Preference Falsification*, Cambridge, MA, Harvard University Press, 1995, 125.

[140] Elena I. Bashkirova, and Vicki L. Hesli, "Polling and Perestroika", 26.

[141] Jeffrey W. Hahn, "Public Opinion Research in the Soviet Union: Problems and Possibilities," in Arthur H. Miller, William M. Reisinger, and Vicki L. Hesli, eds, *Public Opinion and Regime Change: the New Politics of Post-Soviet Studies*, Boulder, CO, Westview Press, 40.

[142] Elena I. Bashkirova, and Vicki L. Hesli, "Polling and Perestroika", 27.

have a special proverb for this, "do not carry our rubbish from your home."[143]

China's first public opinion poll was carried out in 1942[144] before the communist party took power. However, public opinion surveys were banned during the Mao era, as they were in the Stalin years of the Soviet Union. After economic reform was initiated in post-Mao China, various opinion polls were conducted, "not so much by professional survey institutions as by *ad hoc* groups in official research institutions."[145] Among them was the Institute of Journalism of the Chinese Academy of Social Sciences, which carried out a survey in 1982 with a sample of 2,629 urban residents,[146] "to gauge propaganda effect while seeking respondents' opinions on how to modify media practices in order to salvage media credibility."[147] Another institution, the China Institute for Economic Reform under the State Commission for Economic Reform,[148] in collaboration with the Sociology Department of Beijing University, conducted its first public opinion survey at the end of 1984, and another 13 surveys in the next two years. At the beginning of 1987, the institute established the first nationwide social survey system in China,

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[143] Marina Kiblitskaya, "We Did not Make the Plan," in Simon Clarke, ed., *Management and Industry in Russia*, Aldershot, UK, Edward Elgar Publishing Ltd., 1995, 208.

[144] Sam Schreiner Jr., "China's First Public Opinion Poll," *Public Opinion Quarterly*, Vol.7, No.1, 1943, 145.

[145] Li Dong, "Growth of Chinese public opinion polling," in Chapter 2, "Origin and Development of Chinese Opinion Survey Research" of his dissertation *Public Opinion Polls and Political Attitudes in China, 1979-1989*, Dept. of Political Science, Columbia University, 1994.

[146] Everett M. Rogers, Zhao Xiaoyan, Pan Zhongdang, Milton Chen, and the Beijing Journalists Association, "The Beijing Audience Study," *Communication Research*, Vol.12, No.2, 1984, 179-208.

[147] Zhang Yong, "Public Opinion without Public? State Democracy, Middle-Class Consumerism, and Opinion Surveys in Post-Mao China," paper submitted to the International and Development Division, the 53rd Annual Conference of the International Communication Association, May 23-27, 2002, San Diego, California (http://www.allacademic.com//meta/p_mla_apa_research_citation/1/1/2/3/2/).

[148] The history of the institute is introduced in Catherine Kayser's *Professionalizing Research in Post-Mao China: The System Reform Institute and Policy Making*, Armonk, NY, M.E. Sharpe, 2003.

"The China Social Survey System," headed by Yang Guansan. With its nationwide network, it conducted semiannual social survey from 1987 to 1991. The China Social Survey System included two nationwide opinion survey networks: the rural opinion survey network jointly administrated by the Rural Department of China's State Statistics Bureau, and the urban opinion survey network. The System used multi-stage cluster sampling technique and conducted dozens of opinion surveys. The institute was one of the main reform think tanks in China, and the task of the social survey system was to provide information on social reactions to reform policies for reform leader Zhao Ziyang.[149] The questionnaires were policy oriented and carefully selected in order not to conflict with official ideology. Some sensitive findings from the surveys were directly reported to Zhao Ziyang, and only select information was released to the public. The project lasted only about five years and was terminated when the think tank was shut down after the political persecution against many of the research fellows at the institute, following the Beijing massacre. The researchers could no longer publish all the data they had collected.

In China there has never appeared an organization like the VCIOM of Russia, working as an independent institution, regularly conducting nationwide public opinion surveys on various issues from political to economic and social topics, and publishing survey results periodically. However, a lot of Chinese scholars and organizations have made efforts to develop public

[149] I was the director of the Dept. of Interdisciplinary Studies of the institute from 1987-1988, and was responsible for policy discussion with Zhao Ziyang during the period. A detailed history about the Social Survey System was introduced in Li Dong's dissertation *Public Opinion Polls and Political Attitudes in China, 1979-1989* (Dept. of Political Science, Columbia University, 1994). The contribution of the institute to public opinion survey in China has also been mentioned both by Zhang Yong (see Note 147) and Tang Wenfang *(Public Opinion and Political Change in China,* Stanford University Press, 2005, 35 & 37).

opinion studies. For example, in 1986 the first academic institute for public opinion studies, the Public Opinion Research Institute, was established at the Renmin University of China. It conducted many surveys; some collaborations with U.S.- based Chinese scholars.[150] Other institutions, including China's State Statistics Bureau, the All China Federation of Trade Union (ACFTU), the Institute of Sociology of Chinese Academy of Social Sciences and provincial academies of social sciences, departments of sociology in various universities, and commercial polling companies, have been involved in fieldwork. Among them, ACFTU has carried out the largest nationwide survey on the workplace. It conducted two national polls on workers' attitudes in 1986 and 1988, each based on a large random sample with more than 64,000 interviewees[151] on topics such as workers' satisfaction and motivation, labor relations and worker participation in factory management. The ACFTU has continued this large-scale survey project every five years since 1997 and published volumes of aggregate data, which are helpful for the researches of China's employment relationship.

Generally speaking, from 1978 to 1997, public opinion surveys in China experienced a relatively loose political atmosphere, and many foreign scholars enjoyed the opportunity by conducting opinion surveys for their researches in collaboration with their Chinese colleagues. However, things changed in 1998. This year has turned out to be a turning point for scholars outside Mainland China, who are interested in doing social surveys in the country. Alerted to

[150] Zhu Jianhua, Zhao Xinshu, and Li Hairong, "Public Political Consciousness in China: An Empirical Profile," *Asian Survey*, Vol.XXX, No.10, Oct. 1990, 992-1006.

[151] Li Dong, "Growth of Chinese public opinion polling," in Chapter 2, "Origin and Development of Chinese Opinion Survey Research" of his dissertation *Public Opinion Polls and Political Attitudes in China, 1979-1989*.

some politically sensitive content in the questionnaires of some U.S.-based scholars, the Chinese regime began to ban the independent public opinion surveys sponsored and organized by foreign researchers or organizations. The Office of the State Council and that of the Chinese Communist Party (CCP) ordered the restriction of such social investigations in China in the No. 40 internal document from the two offices in 1998. Later, more regulations were announced. China's State Statistics Bureau was assigned the task of supervising and approving social surveys, backed up by the Ministry of State Security, though the latter is not mentioned in the regulations. In 1999 the State Statistics Bureau of China issued a regulation ordering all overseas-funded survey institutions or domestic survey agencies employed by foreigners to receive approval from national or provincial statistics bureaus, and that such surveys results be checked by statistical authorities before being released.[152] In 2000 the Bureau issued licenses to the first group of Chinese and foreign-funded companies that are eligible to carry out researches for overseas organizations and individuals.[153] In March 20, 2000, the Bureau announced the Declaration Guide of Application for Social Investigation Projects Involving Foreign Nationals (*shewai shehui diaocha xiangmu shenbao xuzhi),* then on March 15, 2001, the Temporary Method for the Administration of Social Investigation Activities Involving Foreigners (*shewai shehui diaocha huodong guanli zanxing banfa*),[154] and finally the Regulation for the

[152] The State Statistics Bureau of China, "*Shehui Diaocha Xin Guiding* (New Regulations on Social Surveys)," Beijing, China, *Zhonghua Gongshang Shibao* (China Industry and Commerce Daily), Aug. 2, 1999.

[153] *China Daily*, Beijing, China, July 28, 2000.

[154] He Qinglian, *The Fog of Censorship: Media Control in China*, New York, Human Rights in China, 2008, 227.

Administration of Social Investigation Involving Foreigners (*shewai diaocha guanli banfa*) on November 18, 2004.[155] According to the regulations, all social surveys involving non-residents of the People's Republic of China, including China-born graduate students studying abroad, must be conducted by the organizations assigned by the Bureau, and the domestic collaborators of the foreign investigators have to report to the local state security bureaus to receive approval and supervision; their questionnaires are checked before being approved, and the sampled data will be filtered before being available to foreign investigators.

As a result, recently researchers residing outside mainland China often chose politically and socially less sensitive issues, e.g., the village elections if they want to study democratization in China, as research topics. At the same time, most of their survey samples are purposely selected within a certain locality or localities. Moreover, their "mainland partners remain unspecified for a high proportion" of the surveys. "[T]he lack of transparency is unfortunate… As anonymity provides protection, identification provides accountability."[156] Unfortunately, the rising labor disputes and conflicts have left the workplace in China politically sensitive terrain to be investigated. It implies that, after 1998, foreign researchers in this field may have to use the opinion data published by official organizations that have the privilege to touch on sensitive questions.

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[155] The Department of Politics and Law, the State Statistics Bureau of China, "*Shewai diaocha Guanli Banfa* (Regulation for the Administration of Social Investigation Involving Foreigners)," Nov. 18, 2004, 15:02:40 (http://www.stats.gov.cn/tjgl/swdcglgg/xgfg/t20041118_402209105.htm).

[156] Melanie Manion, "An Introduction to Survey Research on Chinese Politics," *China Quarterly*, 196, December 2008, 755-758.

Political intervention remains a key concern for scholars of public opinion in China. "Even with all these marketization changes, the Party's political manipulation has remained almost the same, especially in the field of the public opinion polling. Academic surveys are still under the tight control of the Party and most of them remain to be harnessed for political propaganda."[157] Zhang depicts three mechanisms that the Chinese regime employs to control public opinion surveys, i.e., privileging, disciplining and punishing,[158] which well reflect the old and new approaches of the regime. The third mechanism involves punishing survey organizers who violate rules and is easy to understand; the first two mechanisms are not familiar to scholars who do not work in the field of China studies.

The mechanism of privileging refers to the organizational and financial resources and the legitimate venues to design sensitive questions and to publish survey results. One of the advantages of governmental and quasi-governmental organizations in conducting such surveys is that they have their own nationwide vertical organizational structures and bureaucratic authority to carry out public opinion surveys. Once the central office of any of these organizations decides to conduct a survey, this decision can be carried out as an administrative order and a budget then provided. "Although these organizations are concerned about political sensitivity, they do have a certain degree of legitimacy (which other types of organizations lack) that gives them the authority to ask sensitive questions."[159] Academic organizations in China are

[157] Zhang Yong, "Public Opinion without Public? State Democracy, Middle-Class Consumerism, and Opinion Surveys in Post-Mao China."
[158] Ibid.
[159] Tang Wenfang, *Public Opinion and Political Change in China*, Palo Aldo, CA, Stanford University Press,

actually better equipped with knowledge of sampling techniques and of theories for analyzing data, and may be more flexible in selecting topics and designing questionnaires, but "they have neither the authority to compel people to cooperate nor adequate financial resources to carry out complex surveys."[160] Foreign organizations are also labeled by the Chinese government, and their chances to get a privilege for collaborative research in China vary. For example, when the British Broadcasting Company (BBC) approached the Journalism Institute of the Chinese Academy of Social Sciences for collaboration on a project in 1995, it was turned down by the government for "ideological considerations." Compared with the BBC, the United Nations Educational, Scientific and Cultural Organization (UNESCO) and other non-government international organizations are often considered "ideologically safer" and more acceptable.[161]

In terms of the mechanism of disciple, Zhang points out that the regime explicitly established formal regulations and licensing rules to govern survey practices. "Various Party and government authorities issued executive directives—both in written form and in verbal instructions—to restrict how surveys could be conducted. For example, no data related to 'state secrets' should be made public; surveys should not be used as a tool to solicit anti-Party opinions; no collaborating surveys could be done with foreign agencies, and so on."[162] Consequently, it becomes an open secret that Chinese pollsters with official affiliations have to

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2005, 37.

[160] Ibid, 37-38.

[161] Zhang Yong, "Public Opinion without Public? State Democracy, Middle-Class Consumerism, and Opinion Surveys in Post-Mao China."

[162] Ibid.

guarantee the political safety of questions.[163] In order to have their opinion surveys go through, investigators in China usually have to be self-disciplined in survey designing. Tang points out, "[I]n China, people are often afraid of the political consequences of speaking the truth. One way to deal with this problem is to avoid asking politically sensitive questions and instead focus on various aspects of people's daily lives."[164] It is a common practice that public opinion survey organizers in China have carefully prevented from addressing sensitive political questions. According to Tang, social and economic questions are generally perceived as less threatening than political issues in China; among political issues, more general questions related to the rule of law, voting and other forms of political participation, expressing dissatisfaction, attitudes toward marketization and socialism, and foreign policy issues are seen as "safer" than questions directly related to the evaluation of the current regime and leadership.[165] Actually, the political sensitivity of questioning in public opinion surveys varies when political atmosphere changes, and when some non-political issues are politicized by policies. Therefore, an implicit tactic for researchers of opinion surveys in China is to find out what is not sensitive at the moment when their survey are conducted, and evaluate which risks to take by addressing some valuable questions at the margins of the current political sensitivity.

The fear of being punished for free expression in Chinese society has gradually receded during the last two decades. Since the late 1990s, Chinese people began to openly express their

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[163] Li Dong, Chapter 3, "Methodological Problems of Chinese Opinion Polls" of his dissertation *Public Opinion Polls and Political Attitudes in China, 1979-1989*.

[164] Tang Wenfang, *Public Opinion and Political Change in China*, 47.

[165] Ibid, 41.

discontent in public spaces such as in buses, cabs and restaurants, and the regime eventually stopped punishing such opinion expression as it is so widely practiced, and "it became increasingly safe to express ideas contrary to official canons."[166] Moreover, after the internet was introduced into China, criticism of the regime with real or anonymous name has become more and more popular. However, as opinion survey organizers in China remain self-disciplined, the published opinion survey data usually do not contain politically sensitive questions and answers. Some China scholars working in the field of public opinion and political change in China have made efforts to identify if respondents could frankly tell their opinions. For instance, Tang suggests that "a way to tell whether people are telling truth is to deliberately ask politically sensitive questions, such as whether 'the CCP is corrupt,' 'the government is inefficient,' or 'market reform is going too fast.' If the majority of the respondents say yes, we can be more confident that people are telling the truth and are not afraid of political retribution."[167]

The author finds two problems in the literature of public opinion research in Russia and China. The first problem is found in Russia, but is not necessarily limited to Russian scholars, and it is the predominance of researchers' preferences. A Russian scholar wrote in 1992: "Almost all serious researchers are now enamored of the liberal point of view, which is very far from that of working people. Scholars are concerned with how to make a rapid transition to the

[166] Timur Kuran, *Private Truths, Public Lies: The Social Consequences of Preference Falsification*, 219.
[167] Tang Wenfang, *Public Opinion and Political Change in China*, 47.

Western model of capitalism, but workers are not dreaming of anything of the sort."[168] When reading the literature from Russia published from 1986 to 1995, I find that this bias among Russian liberal scholars sometimes leads their research towards a direction more focused on justifying the applicability of the Western model to Russian society, a more or less intelligentsia-oriented concern rather than an academic one. Another case can be found from the views of some Marxist researchers of labor relations. From a normative position, they may distrust or discount results of opinion surveys on workers, because they believe that such surveys can not get beyond individual false consciousness shaped by the authority and control structures under which people work. They instead prefer in-depth studies of the labor process that document the ongoing struggle for control over power and resources in employment relationships.[169] Maybe the issue of false consciousness is overemphasized to meet the class conflict orientation in framing the research agenda and approaches. If one's purpose of studying the workplace is to find various patterns of management-labor relations, rather than the conflict shaping process only, workers' attitudes surveys should be a usable data source, and the value of the survey data should not be underestimated or neglected.

The second problem refers to researchers' possible manipulated questioning. In 1990, Shiller, Boycko and Korobov conducted a survey with 36 questions in Moscow and New York City. Their comparative study of public opinions in the two cities leads to such a conclusion: Soviets

[168] Boris Rakitskii, "The Struggle for the Interests of Working People with the Transition from a Totalitarian to a Democratic (Market) Economy," *Sociological Research*, No.1, 1992, 78.

[169] Thomas A. Kochan, "What is Distinctive about Industrial Relations Research?" in Keith Whitfield, and George Strauss, eds. *Researching the World of Work: Strategies and Methods in Studying Industrial Relations*, 39.

appear to be no more concerned with fairness of prices than United States citizens; they appear to be no more concerned with income inequality; and Soviets appear to have the same understanding of the importance of incentives. The authors then suggest that, because the opinion differences between the USSR and the USA are often small or nonexistent, perhaps too much prominence has been given in discussions of the transition to a market system in the Soviet Union today to the differences between Soviets and people in market economies.[170] Carefully using terms without ideological implication in their questionnaire, limiting questions to the field of economic activities, and making questions practical with no institutional background, they try to convince readers that the views of the Soviet and American respondents were basically similar in most respects. However, the well-designed "in-lab" survey has tactically isolated economic actions from the institutional environment, thus the answers of the respondents in the two countries seemingly become indifferent. The survey result by no means suggests that institutional factors do not matter. Even within the field of economic actions, many issues have to involve institutional factors such as values, beliefs and ideology. This example reminds us that researchers should carefully keep themselves away from inappropriate question wording and survey design driven by a pre-determined conclusion, particularly when the researchers are foreign and do not understand much of the cultural and social differences between the investigated country and their own.

[170] Robert J. Shleifer, Maxim Boycko, and Vladimir Korobov, "Popular Attitudes towards Free Markets: The Soviet Union and the United States," Washington, DC, *NBER Working Papers Series* No. 3453, Sept. 1990. This paper was later published on *American Economic Review*, No.81, 1991, 385-400. Maxim Boycko was a young Russian economist and served as economic adviser to the Russian government in the early 1990s; he was the director of the Russian Center for Privatization, an agency of the Russian government under the State Property Management Committee headed by Chubais (see Lynn Nelson, and Irina Y. Kuzes, *Radical Reform in Yeltsin's Russia: Political, Economic, and Social Dimensions*, Armonk, NY, M.E. Sharpe, 1995, 48).

In both Russia and China, usually, if a researcher could get access to the opinion data he needs from the two countries, and well understands the background of the data and the potential problems he has to care about, he may use the data to find patterns of the attitudes for various research purposes. But he may not employ statistical inference to analyze the data. Unlike the GSS data in the US, the original social survey databanks of Russia and China are not available to the public or the researchers outside the survey organizations. What one could read from the published materials is only the aggregate data. Certainly, aggregate data are not really a satisfactory source for statistical analysis, and the averaged figures from the data do not reflect the intra-group differences. However, if one's purpose is to find the general patterns of the attitudes and opinions, he may still utilize the data by comparing the data from the same survey organizations dynamically, or the data from different surveys on the same issue.

Contrasting the studies of public opinion in Russia to that of China, one may find some differences. First, while Russian sociologists have played a key role in the enterprise of the Soviet Union/Russia, their Chinese colleagues haven't shown a dominant influence in the field while a lot of opinion surveys done in China were organized by scholars of other disciplines or by specialists of commercial polling companies for non-sociological purposes. This implies that, as the Soviet/Russian researchers have been able to develop more sophisticated techniques, train more specialists and accumulate more experiences than their Chinese colleagues, sociologists outside the two countries may get more desirable and satisfactory data from Russia than from China, and that the enterprise in Russia would be more uniform along a consistent sociological direction than in China. Second, the implementation of nationwide opinion

sampling survey in China still relies upon the legitimacy and privilege of governmental or quasi-governmental institutions, whereas in Russia it is more likely to be carried out by independent organizations. Usually sponsored by governmental institutions, the available financial resources for such surveys in China are often much larger than that in Russia; and, as a result, China's national surveys have much larger samples, so, statistically, the samples in China are more representative. Third, since political liberalization in the Gorbachev era and the democratization that followed, public opinion studies in Russia encountered far fewer political restraints, whereas in China the researchers still work in a political environment similar to that of the Brezhnev era. This difference suggests that it is often not easy to contrast the questions being asked, and thus the answers, of opinion surveys taken in democratizing Russia and authoritarian China. Some questions frequently asked in Russia remain politically sensitive in China.

4. Privatization in the Cradles of State Socialism: Why is the Picture Fuzzy?

It might not be so surprising that the privatization in Russia and China where state socialism was rooted for many decades could differ from that in other transition societies. The peculiarity of privatization in the two countries may imply that their privatization processes deserve more in-depth analysis for better understanding of the transition paths from state socialism. It has already been a decade or longer since privatization was carried out in both countries, but there are still many aspects of the processes we do not really know. Why did

privatization in Russia and China depart from the ideal model? Is the result a fault of the state, the managers, or the workers, or is it not a fault at all? What lessons might we learn from an academic analysis? The above review of the literature from the two main schools on privatization suggests that this research field remains inadequately explored, and a lot of key questions remained unanswered. Among the questions, a core one is how the state, managers, outside investors, and workers shape privatization, with what motivations, and what their real interactions are. Only starting from here may one further analyze why the insider privatization took place in Russia and why the majority of shares workers held did not produce a model of worker self-management, and how the alliance of managers and local officials in China prevailed in privatization, and why workplace conflicts differ between the two countries.

A key problem of why privatization has not been properly explored may be the methodological weaknesses of previous studies. Many researchers of both schools treat the privatization process as a black box, and focus on consequences only; they thus are unable to provide an explanatory framework to interpret the consequences. Many of them do not really aim at understanding the process. For example, they did not try to find out what workers and managers thought before privatization was launched, and what they did when they were given options, and why. In other words, when privatization is taken as a research objective, it should not be treated as an independent variable that determines the structure of ownership, management authority and labor relations. If we recognize that actors in enterprises may shape the process through their interactions, that privatization can be a dependent variable, and that norms and values are also variables that explain the behavior and choices of managers and

workers, then the management-worker relationship becomes an important explanatory factor to be considered.

The second problem refers to the pre-determined dimensions and assumptions of research. Economists from the point of view of corporate governance often pay too much attention to the role of outside investors. In their analysis a key actor, the workers, is missing or only mentioned symbolically. On the contrary, in the literature of labor relations, workers and labor unions are central but attention is placed on workers' grievances, whereas their influence, positive or negative, on privatization is underevaluated. Moreover, both schools are dominated by certain pre-determined positions: economists believe that workers are not supposed to hold dominant shares, and many labor relation scholars think that workers are not supposed to cooperate with managers. Restricted by their approaches, a lot of researchers ignore the critical role of managers and workers in the privatization process. Actually, managers and workers are not simply passive puppets manipulated by outside investors or the state during privatization; insiders may become the dominant forces that participate in and shape the privatization process, therefore determining what kind of privatization scheme is adopted. In China managers have played a key role in privatization and workers are often involved in resistance; Russian managers and workers decisively shape the process together. The different formations of management-worker relations during privatization in the two countries warrant much more attention. This is a research task that the two schools have left aside. The meaning and content of the management-worker relationship in the privatization process could be quite different from the traditional labor-management relationship in the West. This difference suggests the

necessity of developing a unique framework.

The third problem is related to the weakness of the single country study. Not employing a comparative approach, scholars of Russia and China have seemingly adopted different standards to measure the privatization in their own works. For example, many scholars of Russia charge that privatization failed because of the fragile legal infrastructure, hostile business environment and corruption. But for a lot of China scholars, while all three elements are present, the Chinese version of privatization is perceived as acceptable, having attracted little criticism. A comparative study of the lessons from both Russia and China may offer a chance to reevaluate conclusions drawn from single country study.

This research project on the privatization of SOEs in Russia and China employs economic sociology and organization theory and develops a framework that fills part of the gap left in the literatures of law, economics and employment relations. With this framework the author interprets how the relations of owners (both outsider and insider), managers and workers are shaped during privatization, and how they shape formal and informal institutions of the privatized enterprises in the two countries.

Chapter 3

Analytical Framework and Data Sources

Western scholars usually believe that privatization brings about proper corporate governance, and thus improves the performance of privatized enterprises; however, observations of the privatization experience in Russia and China have revealed quite puzzling consequences, i.e. the ideal type of corporate governance is often not established in privatized enterprises, conflicts frequently occur at the workplace under China's authoritarian regime but less so in a democratizing Russia, and the performance of the enterprises is not satisfactory. This research project aims at understanding the privatization process in Russia and China, tries to solve the puzzles, and explores how the lessons learned from Russia and China may contribute to sociological thinking about the transition from state socialism to market economy.

1, How to Better Understand Privatization in Russia and China?

Privatization refers to both ownership change and enterprise restructuring. The two aspects are intertwined. After the state's hand manipulating the daily operation of SOEs withdrew during the privatization, who sought and actually gained control of the enterprises and their properties is a central concern of all participants including the state, managers, and workers. Large scale privatization of industrial SOEs in big countries like Russia and China inevitably encounters a

problem: shortage of private capital for taking over the enterprises. Therefore, managerial ownership and worker ownership become two possible options; in other words, insiders of SOEs may play a crucial role in privatization. Managers and workers may cooperate with outside investors, or make efforts to prevent the take-over of outsiders. Moreover, even though workers have become shareholders, managers may reduce the rights of employee shareholders. How managers and workers influenced the privatization process and how their interactions restructured owner-employee relations and management-worker relations is an unexplored research area with wide-ranging implications.

Indeed, a lot of questions in this arena have yet to be answered. First of all, in the empirical sphere, researchers may want to know many basic issues which so far remain fuzzy. First, how do managers and workers perceive their new positions in the transformation process? Second, how do the two key parties identify their interests at any given time, especially given the degree of uncertainty during transitions? Third, how do policies, laws and political culture affect their actions? Fourth, how do managers gain authority over former worker-comrades? Fifth, how do workers influence the restructuring of management-labor relations? Sixth, how does the new management establish a system of rewards and punishments for workers? Seventh, how does the progress of marketization of the economy influence the actions of the two parties, especially in light of the fact that China has made greater progress than Russia has? Eighth, if the pre-reform management-worker relationship is characterized as paternalistic,[1] is it replaced during the

[1] Iraida Belyaeva, and Nikolai Malafeyev, "*Ot Paternalisma k Sotsal'nomu Partnerstvu* (From Paternalism to Social Partnership)" Moscow, Russia, *Problemyn Teoryi i Praktyky Upravlenya* (Theoretical and Practical

transformation by a kind of partnership between managers and workers, a confrontation between them, or neither of those two patterns? Ninth, is the restructured management-worker relationship more like that of early capitalism, or that of the social market economy in Western Europe, or something else? Tenth, how does the restructured management-worker relationship affect performance of the firms? These questions are all addressed from a sociological perspective.

This observational dimension implies that the privatized enterprises or corporations are studied as a social institution, and change of ownership and restructuring of the enterprises are not perceived simply as an issue of investing, financial control and legal procedure. Such research touches some core themes in economic sociology and organization theory: reconfiguration of the power within the enterprises, the role of culture in organizational structure, and the social relations that shape intra-organizational structure. Concepts and approaches derived from discussions of these themes play an essential part in this study.

Only after the above basic issues have been analyzed, can we move further to discuss how the lessons of privatization in Russia and China may help us get a deeper understanding of the transition from state socialism to capitalism. From the view of comparative study of the transition, the following questions are worth exploring. First, does democracy matter in privatization, and how is privatization shaped by political institutions with or without democracy? Second, what shapes the perceptions of managers and workers on property rights, managerial power and their own positions, and what is the relationship between their perceptions and

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Aspects of Management), No.2, 1995, 92-97; Andrew Walder, *Communist Neo-Traditionalism, Work and Authority in Chinese Industry*, Berkeley, CA, University of California Press, 1986.

choices in privatization? Third, in the transition how is managerial power reconfigured, and how does the role of workers influence the reconfiguration of managerial power? When workers actively participate in privatization, does the interaction between managers and workers differ from when workers are unable to participate? Fourth, how may we assess the role of the state in privatization, and which goals of the state might be positively evaluated?

2. The Features of SOEs in Russia and China: Background of the Research Project

In Russia and China, the cradles of state socialism, social relations in SOEs exhibit a series of unique features. Such features mean that privatization in the two countries encounters quite different questions than those present in a market economy.

First, before privatization both managers and workers were state employees. Their relationship was not that of the employer-employee in a market economy; instead, they both were defined by the Constitution, administrative regulations and official ideology as the masters of the country. Behind the nominal concept, in practice, managers were perceived as administrative “leaders” (in Russian *rukovoditeli*, in Chinese *lingdao*), and employees not in leading positions were staff or workers. The party-state apparatus appointed leaders, thus offering them power within the enterprises; it also provided workers permanent employment. Thereafter, the leaders were removed only when the governmental organizations did not reappoint them; at the same time, the number of employees did not fluctuate according to changing labor demands and wages and employment conditions were not subject to formal

bargaining but were set by the government. Job change without official authorization was restricted, and the residence registration system (in Russian *propiska*, and in Chinese *hukou*) worked as a barrier to prevent labor mobility. It was under such social relations that bureaucratic control of management was conducted.

Second, the authority in an enterprise was not simply an economic function for production; it was also allocated by the party-state a role in political and social control. The leaders were authorized to instruct workers' behavior and political consciousness, and any informal political or non-political associations of workers were suppressed. Therefore, the leaders were both managers and political supervisors. Official organizations within the enterprises, such as the Congress of Staff and Workers, labor unions and Communist Youth League, all served as administrative branches to help the leaders achieve full control from productive to social activities. Shop-floor directors worked as brokers that mediated between the factory administration and workers. The administrative power in the enterprises not only employed incentives of promotions, wage raises and the distribution of benefits, but also used political mobilization and political honor (such as the "model" or "hero of labor") as an approach to run the workplace. As an implicit rule of the administration, political loyalty or acquiescence to the regime (in Chinese the term is political *biaoxian*) was a precondition for workers to receive a promotion or a wage increase. Realizing that any expression of political doubt or disloyalty could jeopardize their living conditions, workers often declined to criticize their leaders at the workplace and tended not to present their real political views. The workplace in the Soviet Union and China was like a place of socialization rather than simply a place of work. On the other hand,

as SOE workers could hardly be dismissed, managers often felt helpless when workers were reluctant to work hard.

Third, facilities necessary for living were often not available outside the workplace, and SOEs provided them to their employees. It was particularly true in towns with only a few large industrial enterprises. The enterprises provided their employees all or most of the following: an apartment, land for building a dacha and raising vegetables (in the Soviet Union), medical care, schools including nursery school and kindergarten, subsidized cafeterias and dining halls, recreation facilities including movie theaters, and access to vacation spas (not applicable in China).[2] So the workplace played a crucial role in welfare distribution for the state by delivering public goods and social services. In such a system, workers depended heavily on their enterprises, as their daily needs for living could only be satisfied at the workplace. In China, workers were not only supervised at the workplace, their off-work life was also controlled as their residential community was usually established and managed by their enterprises. Such a system contributed a great deal to the stability of SOE and industrial system; it produced a dependency of workers on the workplace as well. On the one hand, workers' socioeconomic status was eventually determined by the accumulation of years of service, and the increase of wages, bonuses and fringe benefits from their workplace; on the other, they did not really have a lot of alternatives if they wanted to change jobs. They might enjoy a stable life if staying in an enterprise in compliance with their leaders. In 1986, based upon analysis of China's workplace, Walder

[2] James R. Millar, "From Utopian Socialism to Utopian Capitalism: The Failure of Revolution and Reform in Post-Soviet Russia," *Problems of Post-Communism*, May/June, 1995, 10.

indicated that such organized dependence was effective for political control, but was harmful to and responsible for poor economic performance.[3] In the Soviet Union scholars called the phenomenon the state patronage,[4] or state-dependent workers, and reached similar conclusions. For example, Zaslavsky wrote that the psychology of state-dependent workers could be related to a complex of specific work habits and to a production ethic based more on the avoidance of work than on discipline and productivity, on a general scorn for work in the state sector, and on the inability and reluctance to take risks and display initiative. Workers always valued guarantees more greatly than success, and viewed guarantees more as the absence of a threat than as the existence of a prospect for the satisfaction of a need.[5]

Certainly, the above features of SOEs would make privatization in Russia and China somewhat different from that in Eastern European countries. The long job tenure of SOE employees, the loose work disciplines and the dependency of workers on the welfare facilities of the workplace may all reduce workers' enthusiasm and capability to find jobs and work in the private sector. At the same time, when privatization was initiated, if a large amount of SOE employees wanted to find jobs in the private sector simultaneously, they found that the employment opportunities were not available. This also greatly influenced workers' expectations to and attitudes towards the privatization scheme in their own enterprise. In other words, very

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[3] Andrew Walder, *Communist Neo-Traditionalism, Work and Authority in Chinese Industry*, 190.

[4] Victor Grigor'evivh Britvin, "Strikes at Enterprises from the Standpoint of Working People," *Soviet Sociology*, May-June, 1991, 56.

[5] Victor Zaslavsky, "*Rossiia na Puti k Rynku: Gosudarstvenno-Zavisimye Rabotnikii Populism* (Russia on the Path toward a Ring: State-Dependent Workers' Populism)", Moscow, Russia, *Polis*, 1991, No.5, p.67; cited from Vladimir E. Gimpel'son, "Economic Consciousness and Reform of the Employment Sphere," *Sociological Research*, Sept.-Oct., 1992, 16.

likely, they may want to retain their jobs at the current workplace during privatization, thus resisting any form of outsider takeover which may lead to large scale lay-offs, and they may support the managers who promised keeping jobs for workers.

Given that labor was more mobile in the Soviet Union than in China and the shortage of blue-color jobs was more apparent in the former than in the latter, Russian workers may have been less dependent on their workplaces than their Chinese counterparts. Besides, SOEs in Russia less emphasized *Biaoxian* than in China, and political control over SOE employees was looser in the Soviet Union. It could thus be expected that Russian workers may be more active as an organized labor force in the privatization process than their Chinese fellows. Moreover, Russia's democratization started before privatization, and Russian workers therefore were able to enjoy political freedom to present their interests and to participate in demonstrations and strikes, whereas Chinese workers did not have such fortune. These features imply that Russian workers might be less restrained by their workplace, and be more enthusiastic and capable in influencing the privatization process than Chinese workers. In other words, Chinese workers may be more compliant to privatization policies of the Chinese government and to decisions of their managers. Whether such differences would be an advantage or a disadvantage for privatization in each country will be analyzed in the following chapters.

Generally speaking, what kind of role the members of SOEs, particularly workers, would play during privatization may largely be shaped by the organized dependence and the ideological dogma of masters of production. Although workers did not really believe that they were awarded the social position described by the dogma, they might still use the official cult of the proletariat

to defend their interests. This is particularly true in China where economic reform was carried out under the communist rule. "Under the old system, workers were the 'masters', and managers and bureaucrats were to be the 'servants' of the socialist firm. Workers complained that during reform the 'servants' were penalizing the 'masters'."[6] As Gimpel'son pointed out before Russia's privatization, "behind these roles is a definite system of values, a type of culture, and a work ethic whose origins go back into history, into the social memory of preceding generations."[7] Chinese scholars also expressed the same concern when China began its industrial reform in the mid 1980s. In order to overcome the influence of a workplace culture hostile to economic reform, the Chinese government even initiated in early 1990s a campaign called "change of mind" targeting SOE employees, emphasizing the necessity of reducing redundant labor. The Russian government did not do much regarding the issue prior to privatization, as it encountered too many troubles in the early stage of the transition. How workers were prepared to play a new role in privatization, either from a state-employee to a wage laborer or from a rank-and-file worker to a proprietor, remains almost untouched in the literature about privatization in the two countries.[8]

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[6] Tang Wenfang, and William L. Parish, *Chinese Urban Life under Reform: The Changing Social Contract*, Cambridge, UK, Cambridge University Press, 2000, 139.

[7] Vladimir E. Gimpel'son, and A. K. Nazimova, "'Master of Production', Dogma and Reality," *Sociological Research*, July-Aug. 1993, 61-74.

[8] In the chapter "Labor-Management Relations" published in their 2000 book, Tang and Parish touched the topic a little bit, but they did not focus on the change of property rights in China's SOEs and used an outdated data collected in 1991 and 1992, thus were unable to explore workers' opinions during the privatization period starting in 1997. See Tang Wenfang, and William L. Parish, *Chinese Urban Life under Reform: The Changing Social Contract*, Cambridge, UK, Cambridge University Press, 2000, 128-162.

3. Analytical Framework and Orienting Propositions

A nationwide large-scale privatization is a state-induced process, but it should not be conceived simply as a result of the teleological and rationalistic designs of bureaucrats. The central government may prepare uniform privatization schemes for SOEs and the rules to regulate asset appraisal and transactions of SOE properties, but it can not directly control the privatization process through centralized leadership, as many decisions and arrangements have to be negotiated in each enterprise by privatization stakeholders and other participants. In enterprises, privatization is not simply an economic decision making and legal arrangement; it is also a social process shaped by participants pursuing self-interested goals. Therefore, research on the transition from state socialism should not only analyze how privatization policies are formulated, but also try to understand how interactions among participants and their responses to privatization policies are shaped by the past and present state-society relationship and the old and changing social relations among participants, and by the sociopolitical and economic conditions before privatization. Furthermore, after privatization, both managers and workers may become owners, so how they reconfigure their relations and how the new relationship between the two parties affects performance of the privatized enterprises are also a central concern. Privatization not only yields economic outcome, but also results in social and political consequences. Evaluation of privatization should not only be grounded in economic analysis; social and political concerns must be included.

The framework of this research project identifies four key actors in privatization and three types of social relations to be analyzed. The state, managers, workers, and outsider investors are

perceived as four key actors in privatization. Among them managers, workers and outside investors are possible participants or game players, whereas the state plays the role of policy maker and rule maker, and arbitrator as well. Three types of relations are considered crucial for the understanding of the privatization process, i.e. state-society relations, the interaction among the players and the interaction between managers and workers. The backgrounds of the relations, the motivation of the state and the players, the value orientations of the players, their attitudes towards privatization, and their actions, and the results of their actions, will all be discussed. Based on the discussion the author will be able to evaluate the process and outcome of the privatization in Russia and China from a sociological perspective.

As SOE institutions under state socialism in Russia and China shared many commonalities, the beliefs and values of workers and managers and their perceptions about the relations between each other may be similar. Traditionally, in cultural analysis beliefs and values are considered long existing perceptions and are used as external factors to interpret subjective experience. In the transition from state socialism, the beliefs and values of workers and managers not only shape their attitudes and actions in privatization, they themselves are subject to change, not only because reform policymakers seek change, but also for the reason that organizational reconfiguration of privatized enterprises result in such a change. Therefore, in this research the author will not only analyze how the old values, beliefs and social relations at the workplace influence the actions of managers and workers, but also analyze how privatization alters the attitudes of one party towards another at the workplace.

In this framework, privatization in the two countries is viewed as an interactive process among participants with different interests, options and powers. It is assumed that, when managers' authority rooted in state socialism and the tenure status of workers are weakened in privatization, both parties may engage in struggles with available approaches provided by government policies and the power drawn from the pre-reform values and social relations; managers could employ their power as the current leader, and workers may rely upon their symbolically defined social position as the master of the enterprises; when workers' active involvement in the privatization is encouraged by the state, they might cooperate with managers for insider privatization; if workers' participation in the privatization is denied, managers might arrange various spontaneous privatizations; workers may enjoy far more power under a democratizing regime than under an authoritarian communist reform regime; no matter which party, the managers or workers, wins more in the privatization, the interactive process could affect the social relations at the workplace between the managers and workers. This analytical framework includes four sets of orienting propositions as presented below.

a. The Role of Government

Under different sociopolitical and economic preconditions, and with different goals and guidelines of privatization, not all the possible players will naturally participate in privatization; some players may be missing in the process, voluntarily or involuntarily. Government may stand on the side of one player against the other, and its goals may be in conflict with the public interest.

When government prepares privatization policies, its goals and the guidelines for privatization are shaped by sociopolitical and economic preconditions, the legacies of the pre-reform state-society relationship, and the interaction between the state and the players. Government may play the role of an arbitrator between managers and workers, or simply stand on one side. The state may try to balance the interests of different social groups, or bring the collective interest of *nomenklatura* into privatization policy making, and ignore the interests of other social groups. A democratic regime needs workers' votes and political support, so it may care more about the concern of workers than a communist authoritarian reform regime does. The latter may ignore the survival concern of workers, if it perceives such a concern a trouble to the state.

The state may prepare privatization schemes and set up rules for privatization, but players in enterprises can manipulate the privatization process for their interest. If the state does not function properly in setting guidelines and rules for privatization, the process may be poorly organized and directed towards spontaneous privatization. When privatization is poorly organized and regulated but officials of government offices are given the power to manipulate privatization, they may become players in privatization for personal interest.

b. The Struggle for Individual Survival

Both managers and workers consider individual survival a priority in the privatization process. Whether workers are able to defend their interests is determined by the nature of the political institutions.

Managers (directors and section managers of factories) have a strong willingness to retain their social status and power, and perceive the maintenance of prestigious social and economic status as a

necessary part of their individual survival. Since their positions can no longer rely on governmental appointment, they have to rebuild their power by a new arrangement through the privatization of the property rights of their enterprise. Although there is an option to develop a new business by leaving their enterprises, managers may not be much interested in quitting their current jobs, so their personal survival largely depends upon the efforts to maintain control.

While over-employment in SOEs is a common problem, the majority of workers (including clerks and technicians) tie individual survival to job security. Workers do not necessarily oppose marketization and privatization, but they are not quiet followers either. Their attitudes towards the process are shaped by the priority of survival and their values and beliefs. No matter whether workers are allowed to actively participate in privatization, they may justify their rights to defend their job security at the current workplace with the idea of being master of their enterprise, even though they realize that their status as masters is simply symbolic. Their common interests lead to collective consciousness in supporting insider privatization or another approach that best guarantees their jobs. Their capability of shaping the privatization of their own enterprise is decided by the privatization policies and political environment. Whether workers' participation in the privatization is required or excluded by the state determines if their struggles for individual survival are successful.

c. The Selection of Allies

Insider privatization and an alliance between managers and workers are more likely to take place if workers are able to participate in the privatization process; managers may form an alliance with outside investors at the cost of workers if workers are not allowed to participate in privatization.

Struggling for individual survival, the managers may select allies in order to control the privatization process. Both an alliance between managers and workers in an enterprise and one between the managers and outside investors are possible. The former may result in an insider privatization against outside investors, and the latter may lead to a privatization at the expense of workers.

If workers are offered by the state or managers opportunities to choose the new ownership structure of their enterprise, they may want to obtain a dominant portion of the shares of their own enterprise. While doing so, they may become allies of the managers, working together against outside investors who might want to lay off workers or replace managers for profit maximization. At the same time, managers would count on the cooperation of workers for their own survival.

In a political environment where worker's participation in privatization is excluded, if managers find that an alliance with possible outside investors could consolidate one's own power or transfer more properties from the enterprise into their own hands, they may work on forming an alliance with outside investors become their agents. Such an alliance could result in arrangements of privatization detrimental to workers at least in the short run, as both the outside investors and managers may want to reduce the redundant labor and benefits burden. When in a weaker position, workers can only express their opinions by collective negotiations, street protests, or some other means. In such activities, the workers may raise the claim of justice grounded on their beliefs and values. The managers and outside investors may need the support of the state in order to weaken the resistance of workers. The state could buy off the redundant workers, take over the responsibilities of large-scale layoffs, or simply leave the responsibilities on the shoulder of the managers.

d. Bolstering Managers' Authority and Changes in Management-Worker Relations

Whether managers obtain their own interests at the sacrifice of workers greatly shapes the post-privatization management-worker relationship and worker morale.

In a privatization, if managers want to retain their position and power, the source of their authority has to be changed. When privatization is implemented without a regime change, managers may still enjoy the old authority backed up by the communist state, but they may also need the legal authority based on a new arrangement of property rights. If a privatization takes place after a regime change, they may only count on the latter.

An insider privatization would result in a majority ownership by workers, as managers' personal investment will not be large enough to gain a dominant holding. In order to bolster their authority, managers may employ various strategies such as collecting shares of their enterprise into their own hands from the workers with the resources of the enterprise or with bank loans. If workers are not allowed to participate in the privatization process, managers may still ask workers to invest in the enterprise as a condition of keeping their jobs, but the employee-investors may not have the rights of shareholders. The managers may also deal with outside investors by providing the properties of their enterprise with a fair or favorable price to the investors in exchange for retaining management power. A portion or most of the workers may keep their jobs, but management-worker relations may be damaged. The workers may not challenge the authority or power of the managers, but they may question the moral aspect of their behaviors. When managers personally benefit from the deals by taking bribes from the investors or by selling part of the properties, workers are naturally offended or angered. Workers' attitudes towards privatization under these circumstances can affect

management-worker relations and the morale of employees.

After privatization management-worker relations at the workplace are reconfigured. At a workplace that has experienced an insider privatization, there might be less tension, whereas in the enterprises privatized without workers' participation, the management-worker relationship may largely be shaped by the behavior of managers. In the latter case, if the managerial behavior goes much beyond what workers perceive to be right, tensions may be aggravated.

4. Data Sources

In this study, the author will use the aggregate data from published public opinion survey results, his survey data in Russia, his interview materials in Russia and China, and media reports from the two countries to analyze the attitudes of participants of privatization, their behavior, and interactions.[9] The aggregate data of public opinion and media reports are secondary sources, and his survey data and interview materials are first-hand sources.

4.1 The Data from Russia

a. The Data of the Russian Center for Public Opinion Research (VCIOM)

The Russian Center for Public Opinion Research (VCIOM) conducts periodic interviews and its sample includes about 3,000 people in 105 cities and villages of 28 regions and republics

[9] In the privatization process managers may engage in various forms of asset stripping, making participatory observation inapplicable to the research project.

in Russia. When Russia began privatization, the center collected opinions from managers and the rank-and-file employees of enterprises in industrial, construction, transportation and service sectors. The Center identifies the samples as opinions of the working population. The samples of working population are drawn from regions and populated areas of Russia. For instance, the survey in Mar.-Apr. 1993 was conducted in 28 regions and 92 populated areas of Russia; the size was between 1,700 and 2,000 respondents. The questionnaires for the working population include 18 questions about working attitudes, 35 questions about management-worker relations, six questions about social relations among workers, 29 questions about perceptions of privatization, 16 questions about norms and values, 13 questions about social acceptance and trust, and eight questions about the business environment.[10] Results to each question in the surveys are reported in tables, broken down by age, education, job type (managers, technicians, clerical workers, skilled workers and unskilled workers), industrial sectors, and regions. But the surveyors did not design any questions in terms of the ownership composition of privatized enterprises. The time-series of the data from 1993 to 2001[11] provide a unique opportunity to analyze the attitudes of workers and managers during and after the privatization in Russia. The weakness of the published data is that they are not cross-tabulated; thus, researcher's data analysis is more or less restrained.

[10] From 1994 to 1996, the questions were frequently asked in surveys.

[11] After 2001, the VCIOM excluded the questions mentioned above. Its focus has moved to other issues.

b. Interview Data

In 1995 the author conducted 13 interviews in St. Petersburg from July to September in selected enterprises of different industries, to obtain basic information about the situation at the workplace before and after privatization. Among the interviewees, five are directors of enterprises (three worked in privatized enterprises in the garment, food and machinery industries; one was the director of a private bank, the former district secretary of the communist party, and one was the director of a private trading company), two are sector managers (one worked for a ship-building factory and one for a machine-building factory), and one is an engineer in a factory of military industry. The author also interviewed four unemployed people and a director of a Women's Retraining Center. The average time for each interview was about 2 hours. The interviews provide rich information about perceptions of the people in privatization. The author tried to interview workers of the enterprises where the interviewed directors worked, but all the directors were reluctant to offer help.

When planning more interviews with a properly designed questionnaire, the author visited several research institutions in Moscow[12] and discussed the privatization process in Russia with

[12] The institutions include the InterCentre (an organization supports the operation of the VCIOM, which is introduced in Chapter 2), the Labor Sociology Dept. of the Institute of Sociology of the Russian Academy of Sciences, the Labor Relations Dept. of the Institute of Economics of the Russian Academy of Sciences, the Institute of World Economy and International Relations of the Russian Academy of Sciences, the Dept. of Labor Problems and Social Development of the Institute of Socioeconomic Problems of the St. Petersburg Branch of the Russian Academy of Sciences, the Dept. of Labor Relations of the Institute of Labor of the Federal Ministry of Labor, and the Academy of Labor of the Labor Union of Russia. The author also attended an international symposium, "Labor Relations and Employment in Enterprises of the Industrial Centers," organized by the Institute of Economics of the Russian Academy of Sciences and the Employment Center of Moscow District, and a symposium about "Self-Management in Industrial Production" organized by the

many Russian scholars. The discussions enriched understanding of privatization in Russia.

In autumn 1997, with the help of the *Vox Populi* Opinion Survey Company headed by Professor Grushin,[13] the author arranged interviews in twelve industrial enterprises. As a professional public opinion survey organization, *Vox Populi* uses an enterprise list for sampling when conducting its regular surveys on various issues. Upon the suggestions of the author, *Vox Populi* randomly selected eleven privatized industrial enterprises and an SOE in Moscow *Oblasti* (Moscow Administrative District, which is much larger than Moscow city) from its enterprise list, then interviewees from the employee list of each enterprise for research of this project. Interviewers from *Vox Populi* visited the enterprises and interviewed a director and three workers at each workplace during the period from September 22 to October 4.[14] All together 48 people were interviewed, of whom twelve were directors and 36 were the rank-and-file workers. The questionnaires used for the interviews were designed by the author and revised by the opinion survey specialists of *Vox Populi*.[15] Four different types of questionnaires were used in the interviews: one for the directors of privatized enterprises, one for the workers of the enterprises, one for the director of the SOE, and one for the SOE workers. The questionnaires included five parts: individual data (eleven questions), job and career (23 questions), organizational change (the

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institute.

[13] The *Vox Populi* Opinion Survey Co. is based in Moscow and has about 10 employees working for contracted public opinion surveys. Professor Grushin was a leading scholar of public opinion survey in Russia and the founder of VCIOM. His contribution is introduced in chapter two.

[14] Only one worker was sick and absent on the planned interview day, so the interview with him was done at his home.

[15] The sequence of questions in the questionnaires and the phrases used in the questions were revised by the opinion survey specialists of *Vox Populi*, so interviewees would feel more comfortable to answer. Then the questionnaires were translated from English into Russian by the specialists.

questions about privatization are included in this part) and leadership (55 questions for managers, 49 questions for workers), work motivation (27 questions), and open-ended questions (seven questions). Interviewees were asked to answer the questions for both the pre- and post-privatization periods. A lot of questions in the questionnaires were similar to that in the VCIOM surveys, so the data from these interviews could be compared with VCIOM data. When asked questions in the questionnaires, interviewers also asked respondents to give answers with a numerical scaling, where the approach was applicable. On average an interview with a 16-page questionnaire took about two hours. After all the completed questionnaires were collected, the author double checked with selected interviewees through telephone interviews.

4.2 The Data from China

In 1996 before privatization was initiated in China, the author conducted twenty one personal interviews with workers and managers. However, in 1998 after privatization started, the Chinese government reinforced its supervision of independent social surveys conducted by scholars from outside China. The author was thus unable to organize independent opinion surveys about the privatization process as this issue is too sensitive to gain government approval. Instead, the author use published opinion survey data about the attitudes of managers and workers, and other materials such as research articles, books and media reports for this research.

a. The Opinion Data of the Chinese Entrepreneurs Survey System (CESS)

The opinion data published by the Chinese Entrepreneurs Survey System (CESS) is a valuable, and the only, source of managers' opinions in China. Reading annual research reports

published by the system, one may analyze the opinions of Chinese managers from various dimensions. The CESS is an official research group in charge of organizing opinion surveys among entrepreneurs annually. It was founded in 1993 by the Research Center for Development under the State Council, the Research Department of the State Council, the State Assets Supervision and Administration Commission, the State Bureau of Statistics and the Chinese Association of Enterprises. The CESS is supported by about 40 ministries and official organizations. Most members of the CESS are the research fellows of the Research Center for Development under the State Council. Every year the CESS selects goals of each annual survey based on government's policy priorities, designs questionnaires, and mails it to managers of 10,000 to 15,000 sampled enterprises in China. After receiving the questionnaires, managers of the selected enterprises may choose to fill out and return them, or not reply. In each survey about 28 to 38 percent of the distributed questionnaires are collected for analysis. Usually, in the collected questionnaires about 68 to 77 percent are from manufacturing, mining and power supply enterprises, the rest from service industries. After data analysis the survey organizers draft an annual survey report for policy makers and publish it in the journal *Management World* (*guanli shijie*) sponsored by the Research Center for Development under the State Council. During the past 18 years the CESS has published more than 40 survey reports about managers' opinions with different focuses. Before China initiated privatization in 1997 the main goal of the survey system was to find urgent problems encountered in SOEs and other private companies; since 1997 the system has served for promoting transformation of SOEs and the development of entrepreneurship in China.

The CESS never releases the original survey data it has collected, so outside researchers can only use the aggregate data published in the report series. Within limited pages, each survey report contains only 20 to 30 tables with tabulated data. When some questions are repeated in the surveys of different years and answers are provided in the reports, one may collect the data to observe opinion changes over time. Although the data are not entirely satisfactory, they are useful for understanding the attitudes of managers.

b. Opinion Data from the All-China Federation of Trade Union (ACFTU) and Other Organizations

Before and after privatization, China's official labor union, the All-China Federation of Trade Union (ACFTU), conducted nationwide opinion surveys of workers and managers in 1997, 2002 and 2007. Its 1997 survey selected 2,335 enterprises by random sampling in 81 cities and counties, and in the selected enterprises 54,000 respondents were interviewed. The aggregate data of the 1997 survey were published in a volume with 1,859 pages.[16] This survey includes four types of questionnaires: one for workers, one for the work unit, one for directors (including the secretaries of the communist party, top managers and labor union chief officers) and one for laid-off workers. The questionnaire for workers has 130 questions that can be divided into eleven categories: basic information (nineteen questions), income and living conditions (seventeen questions), job and career (22 questions), social security (including medical insurance and pensions, nine questions), labor contracts and labor disputes (thirteen questions), work morale

[16] The Research Department of the All-China Federation of Trade Union, *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: the Data Volume), Beijing, China, Xiyuan Press, 1999.

(five questions), attitudes towards the Workers' Congress (eight questions), enterprise reform (eight questions), evaluations of social life (six questions), attitudes towards official labor union (ten questions), and labor relations (thirteen questions). The questionnaire for work units has 110 questions that can be divided into eight categories: basic information (nineteen questions), unemployment (five questions), income and social security (32 questions), the role of labor unions (nineteen questions), the role of the Workers' Congress (four questions), labor contracts and labor disputes (twenty questions), working conditions (two questions), and corporate governance (nine questions). The questionnaire for managers has 51 questions that can be divided into five categories: basic information (nine questions), attitudes towards the Workers' Congress (eight questions), attitudes towards enterprise reform (seven questions), evaluations of income distribution (one question), and evaluations of the labor unions (26 questions). The questionnaire for laid-off workers has seventeen questions that can be divided into four categories: basic information (three questions), the time and reason for the lay-off (three questions), income and living after the lay-off (five questions), and job seeking (six questions).

The results of the ACFTU's 2002 survey were published in a volume of 1,283 pages.[17] According to the publication, 20,854 interviewees of 14,036 enterprises were selected by random sampling in all 31 provinces and metropolitan areas. The volume listed 107 questions that can be divided into twelve categories: fifteen questions are about basic information, eighteen refer to employment, thirteen are about income and living conditions, one for shareholding, twelve about

[17] The Research Department of the All-China Federation of Labor Union, *2002 Zhongguo Zhigong Zhuangkuang Diaocha: Di Liu Pian, Diaocha Shuju* (The Survey of the Status of Chinese Staff and Workers in 2002: Volume 6, the Survey Data), Beijing: Chinese Workers' Press, 2006.

social security, seven about working conditions and training, nine about the Workers' Congress, fourteen refer to management-worker relations and labor disputes, twelve are on attitudes to social issues and reform policies, two are about leisure life, one refers to evaluation of workers' status, and three are about the role of labor union. Many of them are similar to those in the 1997 survey.

In the published data volumes, results of each question in the surveys are reported in tables, broken down by age, education, job and ownership (privatized, private or state-owned). The Research Department of the ACFTU has to consider the requirements and needs of the government; therefore it selects only politically safe questions.

The ACFTU conducted a similar survey in 2007 and published its survey reports in August 2008 in an internally circulated journal,[18] then as a book for the public in March 2010.[19] But, it did not publish the data volume of the 2007 survey, as it usually did before, because the survey found workers' discontent significantly increased. According to a research fellow of a government office, who read the report, 70 percent of the interviewed workers were unsatisfied with their

[18] The Research Department of the All-China Federation of Labor Union, "*Quanmian Jianshe Xiaokang Shehui Xin Zhengcheng Zhong de Zhongguo Zhigong Duiwu: Di Liu Ci Quanguo Zhigong Duiwu Zhuangkuang Diaocha Zong Baogao* (The Development of China's Workers and Staff: The General Report of the Sixth Survey of the Status of Chinese Staff and Workers)," and other Six Reports, Beijing, China, the Research Department of the All-China Federation of Labor Union, *Gongyun Yanjiu* (Studies of Labor Movement), No.16, 2008, 3-65.

[19] The Research Department of the All-China Federation of Labor Union, *Di Liu Ci Zhongguo Zhigong Zhuangkuang Diaocha* (The Sixth Survey of the Status of Chinese Staff and Workers), Beijing, Chinese Workers' Press, 2010.

socioeconomic status, and, when labor disputes took place, 61 percent of the workers tended to participate in protests.[20]

Other opinion data from surveys conducted by research institutes such as the Institute of Sociology of the Chinese Academy of Social Sciences and the Chinese Institute of Labor Movement can be found from their research reports. The Institute of Sociology of the Chinese Academy of Social Sciences, together with the Institute of Philosophy and Sociology of the Hebei Provincial Academy of Social Sciences organized a project "Research on Working Attitudes of Enterprise Workers and Staff" in 1987. The project carried out a nationwide opinion survey. This was the first survey in China aimed at collecting opinions on worker attitudes. Based on a random stratified sample, investigators selected 47 enterprises in 21 cities. 20,000 questionnaires were distributed, and 15,472 effective questionnaires were received and analyzed. Among the respondents, 52 percent were workers, fifteen percent were foremen, sixteen percent were administrative staff, fifteen percent were technicians, and two percent were managers. Results of the research were published as a volume of aggregate data with very brief discussion.[21] This survey focused on the self-evaluation of workers about their morale. The questionnaire included various questions about efforts workers made, factors that influenced their working attitudes, workers' value orientations, how they perceived their managers and

[20] Xia Xiaolin, "*Jiedu Quanguo Zhigong Duiwu Zhuangkuang Diaocha Zong Baogao* (Interpreting the Report of the Survey of the Status of Chinese Staff and Workers in 2007)," Feb. 19, 2009 (www.chinavalue.net/blog/BlogThread.aspx?EntryID=127552).

[21] "Research Group about Working Attitudes of Enterprise Workers and Staff", *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers*)*, Beijing, China, the Ocean Publishing House, 1991.

enterprises, inter-group working relations, and their interest in participation and workplace democracy. The data revealed the attitudes and values of Chinese workers after China's economic reform entered its primary stage.

The Chinese Institute of Labor Movement, a training college of the ACFTU, carried out a research project about worker-management relations and relations among groups of workers from November 1991 to January 1992. Investigators of the project selected 100 enterprises in ten cities of seven provinces by stratified sampling with proportional allocation. About 9,800 questionnaires were distributed and 8,419 were returned. The questionnaire contained 64 questions. Of them, thirteen were questions about basic information, fifteen referred to employment history and career choice, two were related to employee shareholding, three were about housing, two about job training, two about workplace democracy, eight about income and wage determination, four about hiring and promotion, one about inter-worker relations, two about management, ten about working morale and individual behavior, and two about social issues. Some aggregate data were published in 1993.[22] The data provided an opportunity to explore worker-management relations just before large-scale layoffs were initiated.

Another attitude survey done by the Institute of Economics of the Chinese Academy of Social Sciences in 1990, titled "Problems of the Workers and Staff in the Reform of SOEs", also provided valuable information about workers' attitudes. The researchers particularly explored why monetary incentives implemented in the first stage of SOE reform in China eventually failed

[22] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), Beijing, China, the Chinese Press for Social Sciences, 1993, 91.

to work.[23] Their survey was conducted in 57 SOEs in six cities, 3,000 questionnaires were distributed and 2,899 returned.

Although the analytical framework of the Chinese researchers is restrained by official ideology-for example, they have to emphasize that their research design falls into the discourse of classical Marxism-a lot of their data are still useful for this research project. As the surveys often ask similar questions, comparing their data may help to discover patterns in the attitudes of workers and managers in China.

c. Interview Materials

The interviews by the author with workers and managers in China were conducted in the summer of 1996 before the privatization started. Altogether, twenty one workers and managers were interviewed; the average interview time was 90 minutes. All the interviewees were selected through the network of the author, so they were more likely to feel free to tell the author their opinions. Among the interviewees, two were in Shanghai, four were in Nanjing city, eight were in Beijing, two were in Tianjin city, one was in Suzhou city of Jiangsu Province, one worked in Chongqing city, one worked in Shandong Province, one worked in Ningbo city of Zhejiang Province, and one was the research designer for the survey of the Chinese Institute of Labor Movement, a sociology professor of Beijing University. Most of the interviewees worked in SOEs. They include three workers (two of them worked in Capital Iron and Steel Co. in Beijing), four top-managers, three section managers and six clerks. The author also interviewed a senior

[23] Du Haiyan, ed. *Guanli Xiaolu de Jichu: Zhigong Xintai yu Xingwei* (The Foundation of Management Efficiency: The Psychology and Behavior of Workers and Staff), Shanghai, China, the Shanghai People's Press, 1994.

manager of a shareholding company, and two managers and a worker of a private enterprise. The interview materials help the author better understand the situation of SOEs before China's privatization was initiated in 1997.

d. Media Reports

The materials for case studies of the privatization in China are mainly collected from media reports.[24] As in the former Soviet Union before the Gorbachev era, the main official newspapers published by China's central government and its ministries and by provincial governments are full of propaganda, policy interpretation and good news, whereas negative news such the cases of spontaneous privatization rarely appear in the media, as the cases reveal the dark side of the privatization and the press in China is often instructed not to report on them. Precisely as Liu points out: "As the agent of the political authority responsible for shaping public opinion, the mass media in the PRC, as a rule, do not comment on events damaging to the communist system…"[25] However, media control in China has been weakened by efforts of reporters and editors who have tried very hard to break up media control. Since the late 1990s

[24] When cases of privatization involve corruption, in a democratic society civil and criminal court files might be used as a source for researchers; however, in China when claims referring to such issues are submitted, local courts, under the instruction of governments, often refuse to take the cases, and, if cases are accepted by the courts and put into legal procedure, their files are usually confidential for government use only and are not available to the public. In November 2011, the author checked the largest litigation case database in China developed by Beijing University (http://www.lawyee.net/) and found only seven such cases recorded.

[25] Alan P. L. Liu, "The Politics of Corruption in the People's Republic of China," *American Political Science Review*, No. 77, 1983, 602.

more and more locally based newspapers and periodicals were commercialized in China[26] and from such media a researcher might occasionally find reported cases of spontaneous privatization.

In order to make case studies of China's privatization, the author has collected a lot of Chinese newspapers and periodicals and also used search engines on the internet to review newspapers and periodicals.[27] From various newspapers and journals the author finds that several periodicals[28] and local newspapers published in China are useful sources that sometimes report cases of privatization, most of them referring to practices of spontaneous privatization. After reviewing about five thousand search engine pages[29] and reading all the relevant news reports, the author selected about 130 cases from 30 out of China's 31 provinces and municipalities. The cases are selected according to time, place and source reliability. Only those that took place during the privatization process at the privatized SOEs and were reported by newspaper and periodicals are selected. Due to strict media control and internet censorship in China, only a very small number of such cases have been reported in the media, thus the number of the cases collected from every

[26] Such newspapers or journals could no longer receive full financial support from the fiscal budgets, thus have to rely on revenues from sales and subscriptions; at the same time they have obtained some autonomy from government offices. The limited autonomy and market pressure have led the reporters and editors of the media to do more independent news reports, though punishment from the propaganda departments of the communist party often follows. A recent research report has introduced the tough situation the reporters and editors in China encounter (see He Qinglian, *The Fog of Censorship: Media Control in China*, published by Human Rights in China, NYC, NY, 2008).

[27] Both the U.S.-based search engine Google and China's largest search engine Baidu were used. The two have their different limitations. Google does not have the full freedom to carry out its job in China; Baidu has to conduct internet censorship for the government and a huge amount of links, in particular negative news items, are not accessible via the search engine. Another problem is that most media in China set up their web sites after 2002 and do not provide files of back issues; therefore, information prior to 2002 is often not available.

[28] Such periodicals include *Caijing (*Finance and Economy Magazine*)*, and *Nanfengchuang (*The Window for the Wind form the South*)*, and several others.

[29] Each search page contains about 10 news titles with links.

province could not be used to estimate the frequency of the events in each area. The observed cases might only serve for understanding the types of practices in privatization.

e. The Validity of the Public Opinion Data collected in China

Since this research will use a lot of public opinion data collected by officially approved organizations (see chapter 2), the validity of the data should be discussed here. When most questions in the published opinion survey results are not politically sensitive, as a result of self-disciplining of the survey organizers, the validity issue actually refers to understanding people's thinking and modes of expression in a communist system. Russian sociologist Shlapentokh described the thinking of Russian people: the individual citizen's mind was divided into two layers, one "pragmatic" and the other "ideological"; the former layer contained the practical information necessary to get things done, derived mostly from experience; and the latter consisted of abstract information, drawn primarily from public discourse.[30] This description could also be applied to the thinking of Chinese. Public discourse in a communist country is manipulated by indoctrination, and propaganda through media serving as the mouthpiece of the regime. It usually refers to, but is not limited to, built-in perceptions about the socialism system, the legitimacy of the regime, and the authority of the leadership. Shlapentokh's point implies that the answers in public opinion surveys to non-ideological pragmatic issues, most likely referring to socioeconomic activities, are not much influenced by public discourse and would more

[30] Vladimir Shlapentokh, *Soviet Public Opinion and Ideology: Mythology and Pragmatism in Interaction*, New York, Praeger, 1986; *Public and Private Life of the Soviet People: Changing Values in Post-Stalin Russia*, New York, Oxford University Press, 1989. Cited from Timur Kuran, *Private Truths, Public Lies: The Social Consequences of Preference Falsification*, Cambridge, MA, Harvard University Press, 1995, 218.

possibly reflect respondents' free expressions although behind the expressions the values and belief of the interviewees are still influenced by public discourse. Reforms in communist countries often lead to an attenuation of control over public discourse. For example, discussion of the market, civil society, and Western culture were prohibited before reform, but were gradually removed from the list of highly sensitive issues. Thus public discourse under the reform-oriented communist regimes can be divided into two parts: the restricted and unrestricted. A lot of issues in unrestricted public discourse are perceived by interviewers and interviewees as politically non-sensitive or less sensitive. It is the expansion of the unrestricted public discourse that makes it possible for public opinion researchers to explore people's changing attitudes.

Based on Shlapentokh's concept of pragmatic and ideological discourse and the discussion above, the author would suggest that questions in China's public opinion surveys may be divided into three categories: the questions in unrestricted public discourse, questions in restricted public discourse, and non-ideological questions. While the third type of questions are usually not addressed within the discourse of the official ideology and are more likely related to people's daily life, the first two types of questions both have ideological implications, and differences arise if free expression in answering the questions results in political risk. To check if people freely express their opinions in the domain of unrestricted public discourse, a researcher may verify whether the answers of the majority respondents are significantly different with or opposite to the official versions of the standardized interpretation to the issues. The method may help him make a judgment about the political sensitivity of questions for interviewees.

The transition from state socialism may reformulate people's values and beliefs, but, one

should not use public opinion in democratic societies as references to evaluate the validity of opinion data in a reforming communist country like China, even though the survey questions are in the domain of unrestricted public discourse. “It is one thing to recognize the failures of one’s own system, another to understand the underlying problems.”[31] The author would like to emphasize that values and belief are usually formulated through socialization, and prior indoctrination in the socialization process may still have enduring effects on thinking. Therefore, interviewees’ answers in opinion surveys may reflect their new understanding of the changing socioeconomic institutions, and the old value and beliefs they hold. Therefore, free expression in unrestricted public discourse does not necessarily means that public opinion on various issues in China will become similar to what one would expect to find in democratic societies.

[31] Timur Kuran, *Private Truths, Public Lies: The Social Consequences of Preference Falsification*, 214.

Chapter 4

The State, Managers, and Workers:

The Road towards Privatization in Russia and China

Both the Soviet Union and China initiated economic reforms before finally beginning the process of privatization. Until the start of the 1990s, economic reform without privatization in Russia and China had offered little autonomy to managers in economic decision making and profit distribution, and little material incentives to workers. Different sociopolitical policies of the reform regime in the Soviet Union and China greatly influenced the daily life of SOE workers and their attitudes. Political liberalization in the Soviet Union under Gorbachev's leadership in the late 1980s provided not only limited press freedom and freedom of speech, but also opportunities for workers to organize independent labor unions and strikes. In China, the crackdown on the 1989 democratic movement shocked the Chinese people and ended the economic reforms that had been pursued with a "soft hand" under the leadership of Zhao Ziyang. In such circumstances, what did the workers and managers in the Soviet Union and China expect from the reforms in the next stage? What were their perceptions of a market economy and management-worker relations in the near future? Nowadays, evaluations of privatization in Russia and China often ignore the background and its implications. Yet, it is exactly the attitudes and actions of the workers and managers before privatization that affected the policies of privatization. In Russia the nationwide labor movements for democracy and against the spontaneous privatization activities of *nomenklatura* put great pressure on the new democratic

regime for initiating a rapid privatization program, and workers' positive attitudes towards the idea of being masters of production-reinforced by Gorbachev's policy of workplace democracy-became a factor that policy makers could hardly ignore. In China, as the political suppression after the Beijing massacre largely frightened the workers, their low work morale and attitude towards earlier enterprise reform clearly showed that the incentive-oriented enterprise reform that was started in the mid 1980s had reached a dead end. More and more Chinese SOEs became loss makers in the first half of the 1990s, and the Chinese government worried about the dangerous financial burden produced by SOEs to the state budget and banking system. In an attempt to get rid off this burden, while preventing workers from active participation in SOE restructuring, the Chinese government handed over the fate of most SOEs to their managers.

Privatization in a country that has been through a communist revolution is obviously different from one in a society which has never experienced the rule of totalitarianism and the full-range planned economy. A key aspect of the differences is rooted in the attitudes of SOE workers toward the changing socioeconomic life in their own country. Moreover, different political developments before privatization was put on agenda in the two countries had largely changed the sociopolitical atmosphere and the balance of power among the social forces that would participate in privatization. This chapter focuses on the socioeconomic and political changes in the Soviet Union and China and workers' attitudes prior to privatization.

1. Management-Worker Relations in the Pre-reform Workplace

In former socialist countries, the administrative-command economy was established through a highly centralized hierarchy, in which the managerial structure of the state-owned enterprises was simply an extension of the administrative apparatus. These enterprises dominated industries, providing the bulk of jobs for urban dwellers and of taxes for the state budget. Although the regimes repeated a dogma that workers were the master of production, the industrial organizations were actually an intermediary between state and society for political and social control by the party-state. In this hierarchical social structure, positions of individuals are determined by state power, and social mobility is organized from above. At the same time, the regime indoctrinated a mentality among the masses: "a feeling of total dependence on the state's authority structure, intolerance of dissent and free-thinking, the constant feeling of being threatened by external and internal enemies, the predominance of consumerist orientations coupled with modest demands, and the affirmation of the values of social justice as synonymous with egalitarian distribution."[1] As a latecomer to the Stalinist state socialism, China copied the Soviet model of industrial management system,[2] although experimenting with some variations during Mao's Cultural Revolution, featuring far greater politicization. The Chinese version of the Soviet industrial enterprise management model was based on the Chinese Communist Party's

[1] Vladimir Iadov, "The Formation of Working-Class Consciousness under Conditions of Social Crisis and the Developing Market Economy in Russia," *Sociological Research,* Sept.-Oct. 1992, 8.

[2] Deborah A. Kaple, *Dream of a Red Factory: The Legacy of High Stalinism in China,* New York and Oxford, Oxford University Press, 1994, 58-65.

reading of the Soviet literature and regulations, and reflected its primary goal of political control.[3]

In both the Soviet Union and China, restrictions or prohibitions were placed on workers selecting their occupations and residences, though the situations in the two countries were a little different. After WWII the labor shortage became acute in the Soviet Union, so workers had the opportunity to switch jobs and had access to enterprise-based benefits;[4] though, according to the interviews of the author, job switches were restricted by the residence registration system, particularly if one wanted to move to a large city such as Moscow or Leningrad. In China the situation was much worse. During the great famine caused by Mao's Great Leap Forward, population and labor migration was completely prohibited. Afterwards, workers were assigned by government offices to factories, and job switching was almost impossible. For example, during the Cultural Revolution from 1966 to 1976 and in the next years, only those whose spouse lived in another city were allowed to personally arrange a job switch based upon a one-to-one exchange between cities. Moreover, most urban housing was owned by enterprises in China, whereas in the Soviet Union municipalities owned and operated urban dwellings.[5] In both countries, workers were closely tied to their work organizations, and Chinese workers experienced more restrictions than their Soviet counterparts.

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[3] Ibid, 109-110.

[4] Mark W. Frazier, *The Making of the Chinese Industrial Workplace: State, Revolution, and Labor Management*, Cambridge, UK, Cambridge University Press, 2002, 240.

[5] Peter Rutland, "Firms Trapped between the Past and the Future," *Transition*, March, 22, 1996, 30.

In such an environment, workers had to be accustomed to behaving passively and obediently toward their managers.[6] Ironically, the survival strategy was officially painted with a myth about workers' social roles at the workplace. An ideological dogma indoctrinated for decades insisted that public property, though actually belonging to the state, made every citizen its master. It was assumed that workers exercised their function as masters of production in two ways: on the one hand, working with full effort at their jobs; and on the other, participating in the management of production. According to the data in opinion surveys, the reality in the Soviet Union was that, for many workers, the so-called masters of production were simply passive executors of someone else's will, while most workers felt their influence was restrained within the confines of their job functions. The portion of workers who thought themselves "masters of production" sharply declined from the mid 1970s to 1990s.[7] Actual labor morale was far away from the officially proclaimed work ethic, and workers were unwilling to sacrifice their personal interest to the state's needs under the banner of the public good.[8] Moreover, unsatisfactory work environments often resulted in a range of malaise: alienation, boredom, discontent, absenteeism, production slow-downs, and poor job performance. Therefore, the primary distinguishing characteristics of the post-Stalin and post-Mao shop-floor working process are workers holding back output and putting in low effort as a concealed expression of discontent. To obtain workers' cooperation,

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[6] Boris Rakitskii, "New Buyers and New Sellers in Russia's Labor Market," *Sociological Research,* Sept.-Oct. 1992, 43-54.

[7] Vladimir Efimovich Gimpel'son, and Alla Konstantinovna Nazimova, "'Master of Production': Dogma and Reality," *Sociological Research,*July-Aug. 1992, 61-74; Vladimir Magun, "Job Values and Labor Ethics in Socialist and Post-socialist Russia," the Institute of Sociology and the Institute of the World Economy and International Relations of Russian Academy of Sciences, Moscow, Russia, 1994, 15.

[8] Vladimir Magun, "Job Values and Labor Ethics in Socialist and Post-socialist Russia," 12-15.

managers were unwilling to impose tighter labor discipline, and so an informal bargain between workers and management was found.[9] Workers were fired only for either gross violation of the political or labor disciplinary code or for making trouble for managers. Thus, hidden unemployment coexisted with a labor shortage.

Two seemingly opposite images of relations between managers and workers in communist countries like the Soviet Union and China are often cited: a long-term tension between the two parties due to the anti-management sentiments, expressed in work discipline and productivity,[10] and a family-like interaction between them under a paternalistic culture.[11] Neither are untrue or contradictory. The images reflect the double faceted management-labor relationship under state socialism. The tension was partly caused by the violation of worker expectations that had been raised by the state. The paternalistic relationship between workers and managers was produced by structured, organizational dependence. Right before the reform (*perestroika*), many Russians still thought that the state was obligated to provide people with their living necessities, with 42 percent of respondents to a survey believing that "it is primarily the state that should be responsible for people's success and well-being."[12] The paternalistic relationship also led to the normalization of an ethic of

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[9] Donald Filtzer, "Economic Reform and Production Relations in Soviet Industry, 1986-1990," in Chris Smith and Paul Thompson, eds. *Labor in Transition: The Labor Processes in Eastern Europe and China*, London, UK, Routledge, 1992, 110-148.

[10] Vladimir Efimovich Gimpel'son, and Alla Konstantinovna Nazimova, "'Master of Production': Dogma and Reality," 61-74.

[11] Andrew Walder, *Communist Neo-Traditionalism, Work and Authority in Chinese Industry*, Berkeley, CA, University of California Press, 1986.

[12] Nikolai P. Popov, "Labor Relations in Soviet Public Opinion," *Sociological Research,* Sept.-Oct. 1992, 34-35.

consensus to avoid frequent confrontations between workers and managers.[13] However, conflicts at workplaces still stemmed from poor working conditions, unjustified reduction of piece rates, arbitrary management, and difficulties with food supplies. In the Soviet Union sometimes the hopelessness of attempts to obtain justice through appeals to officials prompted workers to strike. According to unofficial information in the *samizdat* literature, about twenty strikes were noted in the 1960s and 1970s in the Soviet Union. Workers even created the first independent labor union in 1977 and 1978, though it was very small, held minor influence, and existed for only a short time.[14] However, in the official discourse any conflict was declared a "chance event" and a purely intra-organizational problem, representing a clash between workers, caused by a divergence of interests, values, or norms of behavior.[15]

2. How Did the Early Reforms in the Soviet Union Shape the Attitudes of Workers and Managers?

Perestroika in the Gorbachev-era brought about large political changes and rapidly reshaped people's values and attitudes towards the reform. According to Tatyana Zaslavskaya, *perestroika* can be seen in two stages. From 1985 to 1988, the *nomenklatura* initiated the movement which

[13] Brantly Womack, "Review Essay: Transfigured Community: Neo-Traditionalism and Work Units Socialism in China," *China Quarterly*, No.126 (June), 1991, 313-339.
[14] V. Kabalina, and A. K. Nazimova, "Labor Conflict Today: Features and Dynamics," *Sociological Research*, No.1, 1992, 9-10.
[15] Viktor G. Britvin, "Strikes at Enterprises from the Standpoint of Working People," *Soviet Sociology*, Vol.30, No.3 (May-June), 1991, 49.

stimulated people's interest in politics, increased social involvement and planted in them the hope of the democratization of society. As most of the *nomenklatura* realized that the command-repressive system of the Soviet Union had outlived itself and that there could be no return to the past, their main concern became how to survive, at least as one of the prestigious, influential, materially secured, and socially-protected groups.[16] Taking party properties with it, the younger and more energetic and educated portion of the *nomenklatura* began to switch from the administrative apparatus to business; and the managers of SOEs tried to change their status from officials to factory owners. Although many people in managerial positions at enterprises "prove to be not only redundant but also demonstrate their total incompetence and lack of readiness to work under conditions of economic independence,"[17] they were able to transform their possession of power into the possession of private property by appropriating state assets. This process began in 1987 and 1988,[18] much earlier than when the post-Soviet regime initiated a privatization program. It implies that reform policies of the government could be manipulated to favor the elite, and that a spontaneous privatization could very easily take place. As the Russian communist elite were steeped in their personal transition, the younger generations of the elite dreamed of becoming businessmen, stockbrokers and corrupt deputies; "Get rich" were words that resounded throughout Russia.[19] The same slogan attracted the Chinese communist elite and their children who began profiteering by selling quotas of raw

[16] Tatyana Zaslavskaya, "Socialism, *Perestroika*, and Public Opinion," *Sociological Research*, July-Aug. 1992, 15-20.

[17] Vladimir E. Gimpel'son, "Economic Consciousness and Reform of the Employment Sphere," *Sociological Research*, July-Aug. 1992, 22.

[18] Ovsei Shkaratan, "The Old and The New Masters of Russia: From Power Relations to Proprietary Relations," *Sociological Research*, Sept.-Oct., 1992, 64.

[19] Boris Rakitskii, "New Buyers and New Sellers in Russia's Labor Market," 51.

materials and consumer goods in shortage from 1985 onwards. The corruption of the Chinese elite finally angered the masses to a sufficient degree as to enable the 1989 democratic movement in China.

The actions of Soviet *nomenklatura* to expropriate state assets reinforced the stubborn, long-existing anti-bureaucratic and anti-management sentiments of workers, and the already firm image that the managers were simply the enemy of *perestroika*.[20] The central committee of the communist party of the Soviet Union adopted a resolution on July 25, 1986, in which a proposal to establish a network of scientific and technical centers from the Communist Youth League for the benefits of its members was approved. The centers were allowed to engage in the manufacture and sale of consumer goods, including computers, and to develop economic relations with foreign firms.[21] The first *nomenklatura* commercial organizations were established by Communist Youth League officials with the funds from the budget of the League. One such cooperative, the Intersectoral Center of Scientific Technical Progress, was made up of a group of the Communist Young League officials in December 1987; after having made a lot of money from selling computers and designing software, they set up the Interbank Organization for Scientific Technical Progress in August 1988; many directors of SOEs joined the bank-creation frenzy.[22] Such commercial activities run by the *nomenklatura* were called the *Komsomol* economy (Communist Youth League economy).

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[20] Vladimir E. Gimpel'son, "Economic Consciousness and Reform of the Employment Sphere," 22.

[21] Olga Kryshtanovskaya, and Stephen White, "From Soviet *nomenklatura* to Russian Elite," *Europe-Asia Studies*, Vol.48, No.5, 1996, 711-733.

[22] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, London, Routledge, 2003, 85.

Zaslavskaya pointed out that, in the second stage of *perestroika* from 1989 to 1990, social forces opposing the *nomenklatura* were activated, while labor, ethnic, ecological and political movements rapidly expanded. Their main object of struggle was the redistribution of power and property among different social groups.[23] Responding to the increasing pressure and attempting to calm down the upset populace, from 1989 to 1991 Gorbachev simply increased wages and social benefits. This measure, together with others, expanded the state budget deficit and brought about inflation; at the same time the foreign reserve of the Soviet Union shrank to a dangerous low of about $100 million.[24]

With the disintegration of the Soviet system of industrial and collective farming, a shortage of goods, and price increases influencing daily life, most people found it increasingly difficult to make ends meet. According to Iadov, public opinion surveys showed that at the end of the 1980s up, to 90 percent of the Soviet populace thought they were "basically satisfied with their material well-being"; however, at the beginning of 1990 about 40 percent of the population indicated that they were worse off than before-at the beginning of 1992 that figure stood at over 90 percent.[25] Thus, paternalism and egalitarianism were nurtured by poverty and economic depression. The key concern of workers was in achieving a more just distribution of income and consumer goods, having the assets that were unlawfully appropriated by the *nomenklatura* returned, and gaining

[23] Tatyana Zaslavskaya, "Socialism, *Perestroika*, and Public Opinion," 15-20.

[24] Joseph R. Blasi, Maya Kroumova, and Douglas Kruse, *Kremlin Capitalism: The Privatization of the Russian Economy*, Ithaca, NY, Cornell University Press, 1997, 28-29.

[25] Vladimir Iadov, "The Formation of Working-Class Consciousness under Conditions of Social Crisis and the Developing Market Economy in Russia," 10.

reliable social guarantees for sickness, old age, disability, and unemployment.[26] In 1988 unemployment began to be a more and more serious problem in the Soviet Union, particularly among the groups of intellectuals and engineering-technical personnel.[27] People's expectations that the state would play an active role in solving problems of job placement became high.[28] The uncertain labor market and increased likelihood of layoffs increased the worries of workers. At the same time, workers were more disciplined at workplaces.[29] At an All-Union Meeting of Managers of the USSR State Enterprises, an appeal to the highest legislative bodies and the President of the USSR was adopted. In it the managers presented a virtual ultimatum demanding that tighter restrictions be imposed on workers and a moratorium on democratization be declared.[30]

One step in *perestroika* greatly shaped the attitudes of workers and managers towards privatization in the post-Soviet transition. In 1987 Gorbachev proposed a reform plan related to workplace democracy in his talk at the London School of Economics. This plan was considered a "new mechanism to revive old ideas of 'worker self-management' and 'industrial democracy' as part of *perestroika.*"[31] According to the plan, supervision of ministries over managers was reduced, workers were given the right to elect their managers, and the Council of Labor Collective (*Soiuz trudovogo kollektiva (STK*) would be established, so that workers could have their voice in management and decision-making and might lease their enterprise to the workers collective of the

[26] Tatyana Zaslavskaya, "Socialism, *Perestroika*, and Public Opinion," 29.
[27] Vladimir E. Gimpel'son, "Economic Consciousness and Reform of the Employment Sphere," 19.
[28] Nikolai P. Popov, "Labor Relations in Soviet Public Opinion," 35-36.
[29] Vladimir Magun, "Job Values and Labor Ethics in Socialist and Post-socialist Russia," 29.
[30] Boris Rakitskii, "New Buyers and New Sellers in Russia's Labor Market," 50.
[31] Paul Christensen, *Russia's Workers in Transition: Labor Management, and the State under Gorbachev and Yeltsi*n, DeKalb, IL, Northern Illinois University Press, 1999, 37.

factory. The plan was adopted by the Supreme Soviet of the USSR on June 30, 1987 as the "Law on State Enterprise" and went into effect in January 1988. The resistance of industrial ministries, the party apparatus and managers made the law flawed. Its provisions were contradictory and its language vague. In particular, the law did not clearly address who had ultimate control over industrial properties.[32] As a result, managers backed up by the industrial ministries and party apparatus used various methods to prevent workers from getting involved in management or decision-making. But the Enterprise Law reaffirmed some elements of communist ideology that stood against a free economy and free enterprise, and strengthened the belief of workers that they ought to claim a collective ownership of their enterprise, as shown by workers' attitudes in later opinion surveys (more details will be discussed in the next chapter).

At the same time, before the collapse of the Soviet Union the attitudes of Russian people towards marketization and privatization were ambivalent. They cared about who benefited from privatization, and most people did not want public assets falling into the hands of the *nomenklatura*. According to the VCIOM opinion surveys in 1990, only seventeen percent of respondents declared themselves unconditionally in favor of the transition to a market economy, while roughly one-fourth of the respondents had a basically positive attitude but expressed certain doubts; seventeen percent of respondents declared themselves unconditionally opposed to the market, and approximately an additional one-quarter were negatively disposed toward it. "Many consider the affirmation of a market economy inadmissible because it carries with it private property, which generates the

[32] Ibid, pp.37-38.

exploitation of working people."[33] In October 1990, a nationwide opinion survey by the Bureau of Sociological Research of the USSR State Committee on Statistics showed that more respondents favored the principle of private ownership than the specific policy of selling off state assets to private individuals. At that time, several early examples of denationalization in the Soviet Union revealed a kind of party-state privatization, as the lion's share of stock went to the ministries to which the enterprises were subordinated. This opinion survey found that the majority of respondents opposed the privatization approach of selling stocks of SOEs. The negative attitude reflected the suspicion toward the party-state apparatus and its attempt to preserve the old power structure under a new name.[34]

It has to be pointed out that people's attitude towards privatization is not merely value-oriented, but is also influenced by their practical considerations. For example, in the Soviet Union--a largely urbanized country--urban attitudes towards land privatization were more positive than views in rural areas. From the VCIOM data, a Russian sociologist found that the purchase and sale of land was supported by more than two-thirds of Russia's urban inhabitants, whereas the rural population was less enthusiastic, because they had been used to life on the collective and state farms and saw land privatization as a frightening process.[35] On the contrary, Chinese peasants warmly embraced the reform to lease land to individual peasants from 1978 to 1981,[36] because they

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[33] Iu. Volkov, "The Transition to a Mixed Economy and the Prospects for the Labor and Trade Union Movement in the USSR," *Sociological Research*, No. 1, 1992, 61-62.

[34] Darrell Slider, Vladimir Magun, and Vladimir Gimpel'son, "Public Opinion on Privatization: Republic Differences," *Soviet Economy*, 1991, 7, 3, 256-275.

[35] Nikolai P. Popov, "Labor Relations in Soviet Public Opinion," *Sociological Research*, Sept.-Oct., 1992, 39-40.

[36] Tang Yingwu, *Jueze: 1978 Nian yilai de Zhongguo Gaige Licheng* (Options: The Road of Reform in China

had never experienced the kind of stable life enjoyed by Soviet farmers on collective and state farms, where wages were paid no matter what portion of crops were collected. The land leasing system brought Chinese peasants benefits without any losses.

3. The Attitudes of Chinese SOE Employees towards Reform Programs, and the Limited Progresses of Enterprise Reform in China before 1989

China began its economic reform in the late 1970s by rural land leasing arrangements and the liberalization of agricultural product sales and small businesses. However, the reform of SOEs did not make much progress for several reasons. First of all, price reform was made the priority. Second, when reform leader Zhao Ziyang realized the urgent need for enterprise reform, his position had already been weakened, and he was unable to overcome the resistance of conservatives in policy circles.[37] Third, restrained by communist ideology and the conservative *nomenklatura*, privatization was not considered politically acceptable. Therefore, enterprise reform became a tough task without any clear goal. Control over the press and the academy, as well as over freedom of speech, was softened from 1978 to May 1989. But China's political atmosphere during the period, compared to that of the Gorbachev-era, was much more rigorous.

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since 1978), Beijing, China, Press of Economic Daily, 1998, 218.

[37] Cheng Xiaonong, "Decision and Miscarriage: Radical Price Reform in the Summer of 1998," in Carol Lee Hamrin, and Zhao Suisheng, eds., *Decision-Making in Deng's China: Perspectives from Insiders*, Armonk, NY, M.E. Sharpe, 1995, 189-206.

According to opinion surveys by the China institute for Economic Reform, as the living standards of almost everyone in society improved significantly from 1978 to 1984, the Chinese people were more supportive of economic reform than their counterparts in the Soviet Union.[38] During the years when prices increased quite fast, price changes did not significantly reduce support for the reform policies.[39] However, the higher expectations were for the reform program, the lower were their evaluations of some reform policies,[40] because the reform program brought not only opportunities and higher income, but also increased prices and unequal opportunities. Moreover, reform policy makers encountered challenges from members of the *nomenklatura* and often could not select or implement the necessary measures. It seems that Zhao Ziyang and Gorbachev had the same problems. The two reform leaders were both bothered by the corruption of the *nomenklatura* who seized on reforms to benefit themselves. In a survey of twenty Chinese cities in February 1986, it was found that, among thirteen items that caused social discontent, such as corruption, price increases, and income inequality, corruption was listed by respondents as the

[38] For example, 78 percent of respondents in an opinion survey of 1985 thought that "as long as the reform would improve our system, we could even afford a temporary downturn in living standards"; and 78 percent of respondents agreed that "it might be necessary for individuals to take certain risks in terms of a decrease in personal living standard, if the reform measures benefit socioeconomic development." Yang Guansan, Yang Xiaodong, and Xuan Mingdong, "*Jiage Gaige de Shehui Xinli Fanying* (The Social Psychological Responses to Price Reform)," in Gao Shangquan ed. *Zhongguo: Fazhan yu Gaige* (China: Development and Reform), Beijing, China, the China Institute for Economic Reform, 1987, 538.

[39] Yang Guansan, Qian Jianghong, Zhang Jie, and Yan Yan, "*Shehui Baozhang Zhidu Gaige de Shehui Xinli Fanying* (The Social Psychological Responses to the Reform of Social Security System)," in Gao Shangquan ed. *Zhongguo: Fazhan yu Gaige* (China: Development and Reform), Beijing, China, the Institute for Economic Reform, 1987, 737.

[40] Department of Sociology, the China Institute for Economic Reform, "*Gaige de shehui huanjing: Bianqian yu Xuanze* (The Social Environment of the Reform: Changes and Options)", Beijing, China, the China Institute for Economic Reform, *Jingji Tizhi Gaige Yanjiu Baogao* (Research Report for Economic Reform), No.39, Dec.20, 1987, 5.

first.[41] When corruption grew more widespread in the following years, social discontent against it rose further. As a result, in the 1989 democratic movement in Beijing and other cities, anti-corruption turned out to be one of the banners that mobilized people to participate in demonstrations.

The reform of the SOE system requires a series of other reforms of the employment and social security system, i.e. abolishing the iron rice bowl of the permanent employment system and establishing a social security system as in a market economy; however, the needed reforms were not largely supported by SOE employees in China. Although they expressed dissatisfaction with the state socialist system, and wanted reform, they worried about losing the vested interests sustained by the system. In a survey conducted by the China Institute for Economic Reform in about a hundred enterprises in six cities from July to August of 1985, 48 percent of the employees asserted that they would rather live with the old *danwei* (work unit) system which did not allow them to select jobs freely and provided only low wages; the respondents also expected that the state could continue to assign jobs for workers.[42] Later, in another survey in 94 enterprises selected from 6 cities in December 1986, the responses of managers suggest that 70 percent felt the need to reduce redundant labor but hesitated to do so for three reasons. The first was that, without reforms of the whole employment system and social security system, the laid-off workers could hardly make ends meet or find new jobs. The other two reasons were the fear that managers' personal safety might be

[41] Ibid, 3-4. The sample size of the survey in the 20 cities was 2,555 respondents.

[42] Yang Guansan, Qian Jianghong, Zhang Jie, and Yan Yan, "*Shehui Baozhang Zhidu Gaige de Shehui Xinli Fanying* (The Social Psychological Responses to the Reform of Social Security System)," in Gao Shangquan ed. *Zhongguo: Fazhan yu Gaige* (China: Development and Reform), Beijing, China, the Institute for Economic Reform, 1987, 737.

under threat from the laid-off workers, and that government offices might not provide full support to the managers.[43] The reform leaders such as Zhao Ziyang who relied on public support could hardly find back-up forces, whether from SOE employees or the *nomenklatura*, to overcome the institutional obstacles. That's why the enterprise reform in the 1980s never moved forward substantially.

Besides opinion data from the reform think tank mentioned above, another source revealed more details about workers' self-evaluation and attitudes in China before 1989, introducing results of a nationwide opinion survey conducted in enterprises in 1987.[44] Firstly, exactly as in the enterprises of the Soviet Union, the ideological "masters of production" or "masters of enterprise" was stamped on the minds of workers in China, though they were confused about their real role in enterprises, as a lot of their Soviet counterparts were. A typical sign of the confusion was expressed by a respondent, the representative of the workers' council in his enterprise, in an interview: "What kind of role do we workers play? Are we masters of the enterprise, or simply wage earners, the employees as labor sellers? This is really a question to which we workers have never had a clear answer for many years."[45] No matter whether they felt themselves real masters,[46] about half of the

[43] Department of Interdisciplinary Studies of the China Institute for Economic Reform, "*Gaige: Zai Qianjin zhong Sisuo* (The Reforms: The Thinking in Moving Forward)," Beijing, China, the China Institute for Economic Reform, *Zhongguo: Fazhan yu Gaige* (China: Development and Reform), No.1, July 1987, 23.

[44] "*Qiye Zhigong Gongzuo Jijixing Diaochzu* (The Investigation Group of Working Motivation of Staff and Workers in Enterprises)," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), Beijing, China, the Ocean Publishing House, April, 1991.

[45] When answering a question "Do you feel that you are the master of your own enterprise", 47 percent of the respondents selected the answer "I really am" or "maybe I am", but 24 percent of them selected the answer "I do not think I am a master of my enterprise" and 29 percent selected "I'm not sure." "The Investigation Group

Chinese workers did care about workplace democracy; in other words, they believed that they were supposed to have rights to supervise their managers and to express their opinions in the decision making of their enterprise.[47] Chinese workers were particularly concerned with whether their managers behaved democratically.[48] The strong desire of Chinese workers for democratic participation in their own enterprise suggests that, although they did not have political rights in China, they did want to have their voices heard and their interests protected at the workplace.

Secondly, as in the Soviet Union, the working motivation of Chinese workers was not high.[49] The economic reforms in China increased workers' wages with bonuses, but did not improve that.

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of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 165.

[46] Only 36 percent of the respondents felt that they were satisfied or relatively satisfied with their role as master of enterprise, while 21 percent felt unsatisfied and 44 percent selected the answer "any way, I do not care." "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 53.

[47] 12 percent and 39 percent of the respondents "cared about very much" or "cared about" the "democratic management and democratic supervision" of their enterprise, while only sixteen percent "did not care" and 28 percent felt "indifferent if there is such workplace democracy." "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 226.

[48] In the survey, nine percent of the worker interviewees were "very unsatisfied" with that and 26 percent were "not satisfied," while 39 percent were "satisfied" and 26 percent "did not care." "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 274.

[49] According to the survey, among manual laborers, only twelve percent of the respondents used 100 percent of their physical capacity, while 47 percent used 80 percent of that, 30 percent used 60 percent, nine percent used 40 percent and three percent used only twenty percent of that. "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 3.

In the meantime, the widespread corruption undermined workers' working enthusiasm.[50] And thirdly, workers began to worry about their job security and benefits.[51]

Within the institutional framework of the communist rule, two steps for enterprise reform were taken from 1987 to 1988, but both did not really move forward. Zhao Ziyang tried a policy called "separating political control from business administration (*zheng qi fenkai*)" to reduce the control of the communist party over the workplace by arrogating to managers power independent from that of the factory party leaders. However, his efforts were limited to paperwork and did not amount to real progresses. In April 1988, an Enterprise Law was issued.[52] It was nominally a Chinese version of the workplace democracy advocated by Gorbachev. According to the law, workers were supposed to democratically elect the members of the Staff and Workers' Representative Congress (SWRC) which was the supreme decision-making body, the official labor union was supposed to act as its executive organ, and the party secretary was relegated to an overseer's position. Above all, the SWRC was entrusted with the power to appraise and fire managers. However, the law was not really implemented.[53] "Often the SWRC has been reduced

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[50] 52 percent of the respondents felt lacking in working motivation, 25 percent felt the motivation reduced significantly, and seventeen percent questioned if they should work hard. "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 97.

[51] 26 percent of the respondents worried that they might lose their jobs, 27 percent said that "I'm not sure if my job is safe," and only 47 percent did not worry about that. "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, Human Relations and Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 162.

[52] *Renmin Ribao* (the People's Daily), Beijing, China, April 16, 1988.

[53] Anita Chan, "Chinese Trade Union and Workplace Relations in State-owned and Joint-venture Enterprises,"

to a formalistic institution, while in some firms they do not even exist."[54] In most cases, managers of the SOEs where the SWRC was established became the SWRC representatives, with their power and status dominating the organization, while the official labor unions continued to function merely as departments of the management.[55] Generally speaking, the Chinese enterprise reform of the 1980s was unable to improve or alter the power structure at the workplace.

4. Democratization in the Soviet Union and the June 4th Massacre in China: Opposite Movements and their Different Impacts on Privatization

Unexpectedly for Gorbachev, his experiment of *perestroika* and workplace democracy opened up the door for workers' collective struggle which, together with other factors, finally buried the Soviet empire. From 1987 informal associations began to form in various cities with the character of semi-labor-unions.[56] In April 1989, miners began to make efforts to resolve the problems directly affecting their work collectives: improvement of facilities, special work clothing and safety equipment, additional pay for evening and night work. In a number of cases, they expressed mistrust of managers, officers of the work collective councils and official labor unions. At the same time, tension between workers and engineering and technical personnel was

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in Malcolm Warner, ed., *Changing Workplace Relations in the Chinese Economy*, New York, NY, St. Martin's Press, 2000, 39.

[54] Ibid.

[55] Ibid.

[56] I. G. Shablinskii, "Where is Our Labor Movement Going to," *Soviet Sociology*, Vol.30, No.4 (July-Aug.), 59.

at a peak, and turned into confrontations.[57] In June 8 and 9 of 1989, a strike took place as an expression of discontent, resentment, and moral dissatisfaction that had been building up among workers for quite a long time. After the strike, an organizing committee was formed in Moscow for holding a congress of independent workers' movements and organizations. After July 10, the center of workers' activities shifted from Moscow to the coal regions. July 1989 was literally the month of the labor movement's resurrection in the Soviet Union.[58] About half a million workers participated.[59] The strikes changed the local power structure and strike committees gained the trust of workers.[60] For example, in Kuzbass region, the strike committees began to exercise complete control over cities and towns. The local government signed an agreement with the strike committees to satisfy most of their concerns, so that the conflict could be quelled quickly.[61] After workers were mobilized, their actions led to a nationwide workers' movement. In the first four and a half months of 1990, there were strikes in 124 cities involving about 1.5 million workers.[62] In the summer of 1990, workers demonstrated their capacity for political struggle in a one day strike demanding the resignation of the government. In April 1991 the workers' movement went beyond the mine gates. More than 30 million people participated in protest actions in response to the appeal of the Russian Federation of Independent Labor Unions.

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[57] L. L. Mal'tseva, and O.N. Puliaeva, "What Led to the Strike," *Soviet Sociology*, Vol.30, No.3, May-June, 1991, 46-47.

[58] I. G. Shablinskii, "Where is Our Labor Movement Going to," 53-70.

[59] V. Kabalina, and A. K. Nazimova, "Labor Conflict Today: Features and Dynamics," *Sociological Research*, No.1, 1992, 12.

[60] Viktor G. Britvin, "Strikes at Enterprises from the Standpoint of Working People," 54-55.

[61] V. Kubas Galina, "Workers' Committees in the Kuzbass," *Soviet Sociology*, Vol.30, No.3 (May-June), 1991, 60-61.

[62] V. Kabalina, and A. K. Nazimova, "Labor Conflict Today: Features and Dynamics," 12.

This time the workers, following the miners' experiences, immediately organized large regional strike committees and formulated both economic and political demands.[63]

Because of the nature of the official labor unions and their total financial dependence on enterprise management, the labor unions either took the side of management or remained apart from the workers participating in the strikes.[64] Thus the distrust of the official labor unions became widespread among the workers. In order to survive, the center of official labor unions, the Council of the General Confederation of Labor Unions, took practical measures to reform itself and its position.[65] Workers began to organize an inter-regional organization of independent labor unions. The first such organization, the United Workers' Front, appeared in the fall of 1989; in the spring of 1990, the second, the Confederation of Labor, was formed; in the fall of 1990, the all-USSR organization of the independent labor unions, the Union of Labor Collectives, was organized. These labor organizations are sociopolitical in character, both in the content of their programs and in their actions. They all participated in political struggle, striving not only for the improvement of labor conditions, but also for the path of sociopolitical development favored by their leaders. The majority of independent labor unions belonged to the Confederation of Labor which stood for democracy and a market economy, while the United Workers' Front advanced the defense of socialism by connecting this with the ideas of Russian nationalism, and the Union

[63] Leonid A. Gorden, and E.V. Klopov, "The Workers' Movement in a Possible Postsocialist Perspective," *Sociological Research,* No.1, 1992, 31-32.

[64] V. Kabalina, and A. K. Nazimova, "Labor Conflict Today: Features and Dynamics", 15.

[65] Leonid A. Gorden, and E.V. Klopov, "The Workers' Movement in a Possible Postsocialist Perspective," 36-37.

of Labor Collectives took an intermediate position.[66]

Observing the demands of strikers during the development of the workers' movement from 1989 to 1991, Iadov found that there was a decline in the share of demands on local authorities and a corresponding increase in the share of demands addressed to central authorities; and, while political and economic demands increased and social demands remained stable, the share of technical and organizational demands declined.[67] Having been suppressed under totalitarianism for decades, Russian society could hardly be altered into a civil society overnight by political liberalization. Since there was no developed system of free association between people or traditions and habits of political self-organization within communities, cities and regions, the majority of the independent labor unions and their nationwide organizations were overwhelmingly dominated by their leaders. On the other hand, as cultural and psychological separation between dirty hands (blue-collar work) and clean hands (white-collar work) prevailed among the masses that comprised the majority of the workers' movement, the rank-and-file workers began to keep an eye jealously on those who were previously their blue-color fellows but then led and represented the workers' collectives.[68] Given that the worsening economic situation increasingly worried ordinary workers, "a considerable portion of ordinary working people are opposed to a quick transition to the market and democracy… [though] the rank-and-file hired

[66] Ibid, 39.

[67] Vladimir Iadov, "The Formation of Working-Class Consciousness under Conditions of Social Crisis and the Developing Market Economy in Russia," 9-10.

[68] Leonid A. Gorden, and E.V. Klopov, "The Workers' Movement in a Possible Postsocialist Perspective," 42-44.

worker is troubled not so much by democracy as by a market economy."[69] One thing the Russian scholars of the labor movement ignored is that when workers' concerns moved to their own enterprise, a unified regional or national labor movement did not really help, because the interests of workers in difference enterprises varied. It is thus understandable why Russian workers' attention gradually turned from the macro-political level to the micro-socioeconomic level right before the collapse of the Soviet Empire and the start of privatization. At the same time, "everyone now has to keep track of the situation, to be concerned about the stability of the enterprise's economic position, about whether management intends to economize by cutting payroll costs, etc."[70] Such attitudes reinforced workers' preference for insider privatization.

No doubt the rapid development of the workers' movement put great pressure on political leaders and managers of SOEs. The managers sensed the real power of the workers' strike committees and began to fear that workers might demand an annulment of their power. They realized that they would be unable to work successfully if they lost workers' confidence.[71] As decentralization and privatization had been put on the government agenda, most managers were bewildered. While awaiting denationalization and privatization, and major changes in the branch structure of the economy, they were afraid to ignore the work collectives openly and endeavored to cover their actions as supposedly being in the interest of and in line with the opinion of the workers' collective. They were not even averse to supporting demands that the ownership of state enterprises be transferred to the work collectives. They knew well how to manipulate the work collective and

[69] Ibid, 51.

[70] Boris Rakitskii, "New Buyers and New Sellers in Russia's Labor Market," 47.

[71] V. Kubas Galina, "Workers' Committees in Kuzbass," Sociological Research, 63.

how to be the *de facto* sovereign at an enterprise by using the collective as a democratic screen. They expected that, in this way, they could obtain a certain portion of the shares when enterprises were privatized.[72]

Moving in the opposite direction to Soviet political liberalization, the supreme Chinese leaders decided to crack down on the 1989 democratic movement in Beijing and other cities. Some workers individually or collectively joined the demonstrations, but most workers did not participate in the movement. The political suppression and nationwide arrests after June 4 1989 silenced the whole society, and completely changed the political atmosphere in China. The policies of the stepped-down reform leader Zhao Ziyang were under attack. In a National Work Conference on Finance and the Economy in late 1989, a member of the Standing Committee of the CCP's Politburo, Yao Yilin, said: "We must jump out from the circle Zhao Ziyang designed."[73] On October 1, 1989, the party's new leader, Jiang Zemin, proclaimed in an official speech: "Only socialism can save China… The reform and opening policy is supposed to carry forward the advantages of socialism."[74]

After the June 4th massacre, the regime enhanced its control within SOEs[75] and a top-down political campaign against "Bourgeois Liberalization" reinforced ideological control at the workplace. Zhao Ziyang's policy of "separating the party from business administration" was

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[72] Boris Rakitskii, "New Buyers and New Sellers in Russia's Labor Market," 49-50.

[73] Ling Zhijun, *Chenfu: Zhongguo Jingji Gaige Beiwanglu, 1989-1997* (Sink or Emerge: A Record of China's Economic Reform, 1989-1997), Shanghai, China, Eastern Publishing Center, 1998, 43.

[74] Ibid, 47.

[75] Malcolm Warner, and Zhu Ying, "The Origins of Chinese 'Industrial Relations'," in Malcolm Warner, ed., *Changing Workplace Relations in the Chinese Economy*, New York, NY, St. Martin's Press, 2000, 27.

attacked and seen by top leaders as a measure that would weaken the party's control, as well as being a spigot of the democracy movement. The party secretaries at the workplace were again given the power to tighten control, and unconditional obedience to the communist party was reasserted. Some workers who actively participated in the democracy movement were arrested and persecuted, and a few fled China. Under high political pressure, Chinese workers had to hide their real opinions and demonstrate compliance with the regime, while their consumer pursuits were encouraged by the government, in an apparent attempt to divert attention from politics. Meanwhile, work morale and support for reform significantly declined. According to a nationwide survey of the status of worker conducted by the ACFTU in 1991 and 1992, the rate of workplace attendance dropped to 85 percent in 1990,[76] lower than the level in past years. Attendance rates in the 1980s were usually above 90 percent,[77] but the average number of absentee days in 1990 was thirteen.[78] The ACFTU survey found that workers obviously lacked motivation and creativity, and had become passive at the workplace.[79] On the other hand, discontent with management became obvious: 65 percent of worker respondents believed their managers were involved in either corruption or

[76] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), Beijing, China, the Chinese Press for Social Sciences, 1993, 92. The attendance rate is defined as the percentage of employees who did not involve in absenteeism in a whole year.

[77] "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, the Human Relations, and the Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 144.

[78] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), 117.

[79] Ibid, 92.

maladministration, and only six percent were satisfied with manager conduct.[80] The survey did not touch on any issues related to reform, but listed many questions about worker behaviors, following the pattern of the workers' attitude surveys in the Soviet Union during the Brezhnev era. In the survey of the ACFTU, when asked "do you think you should be obedient to the corrupt activity around you," only thirteen percent of the respondents selected "Yes, I should"; but to the question "are you actually obedient to the corrupt activity around you," 63 percent of the respondents selected "Yes." In another pair of questions, when asked "should you strive for the rights of democratic management," 68 percent of the respondents answered "Yes," whereas when asked "have you actually strived for the rights of democratic management," only 40 percent responded with "Yes." Responding to another question regarding "democratic rights," only 32 percent of the respondents thought "I should accept the democratic rights given by my bosses," but 60 percent answered that "I actually accept the democratic rights given by my bosses."[81] Such answers imply that there existed a growing gap between workers' values and their forced behavior in a repressive political environment.

At a time when the reform policies of the 1980s were under attack and people's income expectations were falling, the Chinese people became cautious in family expenditures. In 1989 the total retail sales of consumer goods of the country dropped seven percent from the previous year.[82] This was a phenomenon that had never been observed in the past decade. The shrinking

[80] Ibid, 97.

[81] Ibid, 480-481.

[82] The State Statistics Bureau of China, *Zhongguo Tongji Nianjian 1993* (Statistical Yearbook of China 1993), Beijing, China, China Statistics Publishing House, 1993, 239, 611.

consumption, together with the regression of Chinese politics after 1989 and other factors, contributed to an economic stagnation in China. After rapidly increasing inventories, about 20 to 30 percent of factories had to stop their operations due to overstocking.[83] In 1990 from January to July the inventories of 11,000 SOEs increased by 46 percent, profits decreased by 56 percent, and one third incurred losses.[84] In order to overcome the economic difficulties after the June 4th massacre, Deng Xiaoping, the supreme leader of China, advertised economic liberalization under authoritarianism in early 1992. In May 1993 the prices of grain and grain products were liberalized in order to reduce fiscal subsidies. Food prices thus increased about 23 percent within days. As a result, the price index of living expenses in 35 large cities increased by 20 percent in the month, while the prices of industrial materials went up by 40 percent.[85] The rate of price increases kept going up, and reached its peak in September of 1994 at a level of 25 percent.[86] However, China's price liberalization did not induce the same sociopolitical impact as price liberalization in Russia from January 1992. The shock of the June 4th massacre remained in people's minds: the rapid increase in prices did not result in protests, and no criticism or complaint was reported in the media, which was strictly controlled by the regime. The former reform leader Zhao Ziyang had tried the same price reform but failed because of the radical social responses and the attacks of the conservative *nomenklatura*. In contrast to the panic from the inflation in 1988 under Zhao's leadership and the forced societal silence during the price liberalization of 1993 and 1994 in China,

[83] Ling Zhijun, *Chenfu: Zhongguo Jingji Gaige Beiwanglu, 1989-1997* (Sink or Emerge: A Record of China's Economic Reform, 1989-1997), 77-78.
[84] Ibid, 91-92.
[85] Ibid, 310-311.
[86] Ibid, 462.

it can be seen that the Chinese government, armed with its iron fist from 1989, enjoyed the advantages of socialism and did not have to worry about the negative social consequences of price liberalization.

Right after the price liberalization in November of 1993, CCP headquarters declared that it was going to promote a socialist market economy, a key task of which was to restructure SOEs into a modern enterprise system, i.e., to incorporate SOEs.[87] This program opened the door for the spontaneous privatization of managers at the cost of workers. The Chinese regime probably saw price liberalization as a test. As high price increases in 1993 and 1994 failed to provoke a social backlash, the regime soon moved further, laying off millions of workers in SOEs. This was an important step in paving the way for the privatization of SOEs in China.

5. The Failure of China's Earlier Enterprise Reform

Why did the Chinese regime initiate the privatization of SOEs and choose large scale lay-offs prior to the privatization? As mentioned earlier in this chapter, the Chinese reform leader Zhao Ziyang tried to push forward enterprise reform from two directions: politically, reducing the role of communist party in the workplace and introducing workplace democracy into SOEs, similar to what Gorbachev attempted; and economically, introducing wage incentives to stimulate the motivation of workers, also almost in the same manner as the Soviet leaders did. While the political aspect of

[87] Jin Pei, *He Qu He Cong: Dangdai Zhongguo de Guoyou Qiye Wenti* (What Course to Follow: The Problems of the State-owned Enterprises in China Today), Beijing, China, China Today Press, 1997, 118.

enterprise reform eventually failed, the economic incentives had been implemented for more than a decade by the mid-1990s. However, the work morale of SOE workers had not substantially improved, and the performance of SOEs turned out to be getting increasingly worse. Beside the shock of the Beijing massacre in 1989, what factors made economic incentives ineffective? Given that the Chinese regime does not want any political change, could incentive-oriented enterprise reform prevent the SOEs from downward sliding? Did Chinese enterprise reform reach a dead-end, if yes, then why? It is necessary to understand the path of the nationwide Chinese privatization in order to answer these questions.

In April 1993, the author conducted an in-depth interview with a senior manager of a large-size SOE located in Chongqing city, in southwestern China.[88] According to the manager, in 1993 many people lacked confidence in the coming post-Deng China and worried about possible instability; on the other hand, a common socio-psychological phenomenon was to grab as much money as possible and as early as possible. In order to reinforce the political control over workers, the role of the communist party at the workplace was once again asserted and strengthened, making enterprise reform merely paperwork and lip service. Labor productivity in large SOEs, including that of his enterprise, kept falling, as workers lacked incentives to be productive. The only way for managers to prevent further declines in productivity was to increase bonuses, while the basic wage was controlled by the central administration. As a result, the labor costs of the enterprise grew rapidly. Moreover, in order to satisfy the need of employees for apartments, the enterprise expended

[88] The interviewee was Mr. Jiang Yue, the assistant to CEO of the Chongqing Special Steel Factory. In 1993, the enterprise had about 20,000 employees, plus 6,000 in affiliated enterprises (the children and relatives of the employees) and 6,000 pensioners.

a lot of resources on housing, while the employees who were given an apartment only paid a subsidized price (4,000 to 5,000 Yuan for a two bedroom apartment, this amount being equal to twelve-month wages and bonus for a middle-aged technician with college education, or a skilled worker). When the profit of the enterprise shrank, it had to survive on bank loans. Consequently, the SOE borrowed more and more loans from state banks, and its debt-to-asset ratio reached 70 percent, a dangerous level. If one were to read media reports about the situation of SOEs in the early 1990s, a similar picture would emerge across the country.

In order to discover workers' real morale, the author further analyzed Chinese workers' attitudes in the late 1980s and early 1990s from several perspectives. The analysis may also show if the situation in the enterprise mentioned above was unique or typical. The data used were taken from three workers' attitudes surveys conducted by Chinese scholars in 1987, 1990 and 1991: the survey of the Institute of Sociology of the Chinese Academy of Social Sciences and the Institute of Philosophy and Sociology of the Hebei Provincial Academy of Social Sciences, in 1987 (referred to in this section as Survey A); the survey of the Institute of Economics of the Chinese Academy of Social Sciences, in 1990 (referred to as Survey B), and the survey of the Chinese Institute of Labor Movement, in 1991 (referred to as Survey C). The sampling method and sample size of the three surveys have been introduced in chapter three. The surveys asked similar questions, and the author will compare their common results.

Two Chinese scholars, Bu and Xu, had tried in late 1993 to analyze worker attitudes in China with a relatively small sample of non-managerial male employees of an SOE in Shanghai, for a comparative study among Chinese, American and Japanese workers. The two authors in the study

focused on three aspects: expectation for job security and company-provided benefits, commitment to the organization, and receptiveness towards the bureaucratic prerogatives of management. Regarding the first issue, they asked five questions about whether a company ought not to lay-off employees even when business declined, not to dismiss incompetent employees, not to terminate the employment of those on long-term sick leave, and whether they ought to be responsible for employees' housing, and provide financial subsidies to those with large families. On the second issue, they asked five questions: whether the "company is of central importance to employees' lives," whether employees ought to "participate in after-hours socialization," whether they should "strive to accomplish assigned tasks," whether they should "stay with the company even when a better opportunity arises elsewhere," and whether "the primary reason for working hard in a company is to fulfill the expectation of the important others." On the third issue, related to management-labor relationship, they asked ten questions, framed as statements that required a yes or no response, "management should not be challenged," "unionization is unnecessary," management ought to be empowered to "evaluate employees' performance," to "determine the procedure for merit rating," to "make promotion decisions" and to "enforce work rules," and finally "management ought to be treated with paternalistic reverence even in non-work related situations and matters." The two authors concluded that the Chinese employees expressed less desire to challenge management decisions than American employees did; fewer Chinese than Americans accepted the legitimacy of management's prerogatives to evaluate employee performance; and the commitment of the Chinese employees to their work organizations was much weaker than that of

Japanese employees, and in some cases, was even weaker than that of American employees.[89] These issues were key concerns in the three surveys mentioned above, but researchers conducting the three large surveys designed better questions as they understood the situation in China's SOEs more thoroughly.

In the Western literature, organizational commitment has been shown to be closely related to productivity related behavior such as absenteeism and turnover, and is often measured by workers' attitudes towards the value of the organization they work for, their loyalty to and pride in their organization, and their motivation to work.[90] The three large surveys as the data sources for the following analysis include many questions regarding worker attitudes about their job satisfaction, work motivation, the degree of their efforts at work, working enthusiasm, factors that affect work motivation, and loyalty to the workplace, as well as workers' participation and other aspects of management-worker relations. The three surveys also asked workers a series of questions about their attitudes towards enterprise reform. Moreover, the surveys revealed how the respondents were recruited into their enterprises and the frequency with which they changed jobs, which reflected the employment features of SOEs in China. The only aspect that was not included in the three surveys but often appears in the Western literature for measuring workers' organizational commitment is workers' attitudes about the value of the organizations they work for. This is probably because the

[89] Bu Nailin, and Xu Ji-liang, "Work-related Attitudes among Chinese Employees *vis-à-vis* 'American' and 'Japanese' Management Models," in Malcolm Warner, ed., *Changing Workplace Relations in the Chinese Economy*, New York, NY, St. Martin's Press, 2000, 196-198. This study interviewed 169 Chinese employees between the late 1993 and early 1994, 491 American employees in 1960, and 756 Japanese employees in 1976.

[90] Duncan Gallie, Dobrinka Kostova, and Pavel Kuchar, "Employment Experience and Organizational Commitment: An East-West European Comparison," *Work, Employment and Society*, Vol.13, No.4, 621.

value of SOEs was set by the state and was more or less identical across the enterprises.

In China a large proportion of SOE employees were appointed to their workplaces, and did not have choices in selecting where they worked. Survey B indicated that 67 percent of the respondents were appointed to their current working organizations by the government, seven percent of them entered the organizations to replace their parents as a result of the state policy favoring the children of SOE employees, and another 22 percent were arranged by the labor department of local governments for job change.[91] The three percentages found from the results of Survey C were 74, 18 and 3, and they suggested that 84 percent of the respondents had never changed jobs.[92] This employment relationship, characterized by job appointment by government, and a very low job change rate suggested that workers were very closely tied to their workplaces and were not able to easily select jobs, even if economic reforms had opened the door for job changes in the non-SOE labor market for more than a decade in China. Moreover, Survey C showed that 38 percent of the respondents had a spouse or other relatives working at the same workplace,[93] whereas the percentage in Survey B was about 50 percent,[94] which implied a kind of family dependence on the workplace. According to Survey C, 38 percent of the respondents lived in the apartments provided

[91] Du Haiyan, ed. *Guanli Xiaolu de Jichu: Zhigong Xintai yu Xingwei* (The Foundation of Management Efficiency: The Psychology and Behavior of Workers and Staff), Shanghai, China, Shanghai People's Press, 1994, 21.

[92] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), 471-472.

[93] Ibid, 472.

[94] Du Haiyan, ed. *Guanli Xiaolu de Jichu: Zhigong Xintai yu Xingwei* (The Foundation of Management Efficiency: The Psychology and Behavior of Workers and Staff), 212.

by their enterprises, and the average space per family member was 12 square meters.[95]

Did the permanence of employment, family dependence, and housing translate into a high organizational commitment in China? Survey A done in 1987 showed that SOE employees in China were eventually satisfied with the pension system and 61 percent of the respondents were satisfied with their jobs, but 57 percent were not satisfied with housing supply and 46 percent were unsatisfied with their wages.[96] As found from Survey B, in 1990 respondents who were not satisfied with their workplaces sat at 74 percent, the dissatisfaction being related to wages, bonuses and housing. [97] According to Survey C, when employee investment in their work organizations was arranged (about seventeen percent of the respondents engaged in this), only 38 percent of the investment activities were voluntary, while the other portion of that was under the prompting, if not coercion, of managers.[98] In order to find the degree of employees' satisfaction with their organization, Survey C asked "when you enter your enterprise everyday what is your feeling?" and "how do you feel when you're working?" To the first question, 32 percent of respondents answered with "pleasure," while 59 percent with "apathetic" and nine percent with "boring"; to the second question 70 percent answered "time goes fast," but 30 percent with "time goes slow."[99] Although

[95] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), 472.

[96] "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, the Human Relations, and the Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 51-55.

[97] Du Haiyan, ed. *Guanli Xiaolu de Jichu: Zhigong Xintai yu Xingwei* (The Foundation of Management Efficiency: The Psychology and Behavior of Workers and Staff), 40, 231.

[98] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), 472.

[99] Ibid.

the questions in the three surveys are not exactly the same, the figures suggest that the degree of worker satisfaction was not high in 1987 and had fallen from 1987 to 1991.

As for motivation, in 1987 Survey A found that only twelve percent of the respondents thought they had used 100 percent of their physical capability at their jobs, and 30 percent used only half of that; even so, still 26 percent of all respondents thought their productivity quota was too high; at the workplaces, only 42 percent reported that they worked with enthusiasm and fourteen percent without.[100] Survey B showed that in 1990 only sixteen percent of the respondents thought they had worked as hard as possible, while 45 percent thought they could have doubled their productivity.[101] In Survey C in 1991, 61 percent of the respondents thought their working motivation quite low. While 58 percent thought that they were supposed to work harder, only 38 percent said they actually did so.[102] The three surveys depict a picture of low worker motivation from 1987 to 1991.

In terms of workers' loyalty to their organizations, Survey A found that, in 1987, 28 percent of the respondents were eager to leave the current working organization for other jobs, 41 percent would rather retire earlier, and 47 percent were not afraid of being laid-off. At that time, as marketization brought about new opportunities for making money, moonlighting or leaving an SOE for individual business attracted many workers. The survey revealed that 41 percent of the

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[100] "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, the Human Relations, and the Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 141, 144, and 160.

[101] Du Haiyan, ed. *Guanli Xiaolu de Jichu: Zhigong Xintai yu Xingwei* (The Foundation of Management Efficiency: The Psychology and Behavior of Workers and Staff), 48.

[102] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), 92, 481.

respondents wanted to get a second job and in some cities 25 percent of the workers had already done so.[103] It was the same phenomenon found in 1980's Hungary. But Survey C done in 1991 shows that moonlighting was not easily done, and leaving the current work organization, with its structured organized dependence, was not easy either. According to Survey C, only about seven percent of SOE employees had other sources of income, and only about ten percent of workers had successfully changed jobs since 1984 from their previous organizations; however, in 1991 still 24 percent of the respondents wanted to leave their current enterprises, among them 60 percent citing the reason as low income and 21 percent saying that their personal capability could not be sufficiently utilized at the current workplace. Interestingly, among those who wanted to leave, only eleven percent wanted to go to another state-owned industrial enterprise, while 23 percent wanted jobs at joint-venture companies, 32 percent wanted to find jobs at educational or cultural organizations, and thirteen percent at government offices.[104] This unusual intention in terms of job change reflected the influence of Mao's policies during the Cultural Revolution when a lot of workers were appointed to educational and cultural organizations and government offices to be cadres. Although only a small portion of the employees really left SOEs or were able to carry on a second job, the loyalty of SOE employees to their working organizations was quite low in 1987 and remained so in 1991. The reason fewer workers wanted to leave their enterprises in 1991 than in 1987 was probably not the result of rising loyalty, but the increasing difficulties of job change.

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[103] "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, the Human Relations, and the Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 7, 163-164.

[104] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), 93, 473-474.

Obviously, Chinese SOE employees' organizational commitment had been quite low, even though incentive-oriented enterprise reform raised their wages, bonuses and benefits. What were the expectation and perceptions of employees about enterprise reform? From Survey A it can be found that they were quite dissatisfied with the egalitarianism in wage and bonus determination at the workplace, which was called in China the *Daguofan* ("big-pot" distribution system).[105] The researchers of the Survey B pointed out that, under the wage policy controlled by the state, not only the wage but also the bonus were more or less distributed equally, as by doing so managers would attempt to prevent the potential conflicts at the workplace among different working groups. Every working group, from manual labor, technicians, to staff, believed they deserved higher bonuses because measurement of individual real work contribution turned out to be difficult. Frequently, the bonus became a fixed part of monthly income.[106] Some researchers found that, as a regression analysis of the wage increase and output of enterprise showed only a quite weak positive relationship, "the rapid increase of wage income in the reform years has not really produced the necessary efficiency." They further concluded that while enterprise reform had included the intention and outcome of increasing material incentives, and had resulted in the expansion of wages and benefits, psychologically workers were supposed to be strongly satisfied; but the sample data showed that the majority of workers and staff were dissatisfied to different degrees with the changes brought about

[105] In 1987, 87 percent of the respondents supported "breaking up the big-pot system," and 76 percent supported "laying-off redundant labor." "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, the Human Relations, and the Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 203.

[106] Du Haiyan, ed. *Guanli Xiaolu de Jichu: Zhigong Xintai yu Xingwei* (The Foundation of Management Efficiency: The Psychology and Behavior of Workers and Staff), 24-35.

by the reform.[107] Survey B in 1990 showed that only seven percent of the respondents thought their income and benefits increased, while fifteen percent saw it as unchanged, with 77 percent perceiving a decrease; at the same time, only nineteen percent of respondents reported that their working motivation increased, whereas 31 percent said it was unchanged, and 49 percent decreased. The researchers of Survey B suggested that the unexpected responses, which were contradictory to the reality of wage increases across those years, could only be partly explained by economic stagnation in 1990, and may partly be interpreted by the rising high income expectations of the workers.[108] The researchers of Survey C, who are scholars of labor relations, believed that the reason why the enterprise reform failed was its overemphasis on managers' authority and the ignorance of workers' participation.

Chinese workers have shown quite high expectations of the behavior and capability of management, but their desire for participation went through a change, from little in the 1980s to significantly more in the early of 1990s. In Survey A of 1987, 73 percent of the respondents believed that "whether the performance of an enterprise is good or not depends upon its leaders," 73 percent expected that their managers could listen to the opinions of workers, and 79 percent did not want to support the managers whose leadership lacked a democratic style; however, only 29 percent were interested in "their power in enterprises," only 46 percent were interested in "playing the role as masters of the workplace," 43 percent cared about "participating in management decision making," and 51 percent about "democratic management and supervision." Only 21 percent were

[107] Ibid, 38-39.
[108] Ibid, 39.

not satisfied with their role as the masters of their workplaces, and 34 percent dissatisfied with the leadership of their managers.[109] But the situation had seemingly changed. As reported the Survey B of 1990, 40 percent of the respondents agreed that "the revenue of the enterprise is made by all employees, thus is supposed to be distributed by them," 83 percent thought "directors of the enterprise are supposed to be elected by employees," and 69 percent agreed that "directors and rank-and-file workers are all masters of the country with divisions of labor, so they should discuss things together to arrive at decisions." At the same time, 73 percent of respondents opposed the idea that "the directors as the representatives of the state are authorized to manage the enterprise, and workers are supposed to obey the instructions of the directors unconditionally." Regarding possible bankruptcy, seventeen percent agreed that "if the enterprise falls into bankruptcy, the managers are responsible for that and should resign," and 76 percent thought "workers are the masters of the country, if the enterprise bankrupts, the state is responsible for arranging jobs for them."[110] This change very likely reflected the awakening of workers' consciousness of participation to protect their own interests in an economic environment in which more and more SOEs were beginning to experience difficulties.

As worker consciousness and desire of greater participation in the decision making of their enterprises increased, their actual status in management-worker relationship was weakened. In order to offer managers more autonomy and incentives, a policy of contracting the enterprise

[109] "The Investigation Group of Working Motivation of Staff and Workers in Enterprises," *Changqing, Renqing, Xinqing: Zhongguo Zhigong Xinli Dadiaocha* (The Situation in Enterprises, the Human Relations, and the Psychology: A Large Survey of the Psychology of Chinese Staff and Workers), 225-226, 228, 264.

[110] Du Haiyan, ed. *Guanli Xiaolu de Jichu: Zhigong Xintai yu Xingwei* (The Foundation of Management Efficiency: The Psychology and Behavior of Workers and Staff), 94.

management with directors was implemented from the latter half of the 1980s, while the managers were still appointed by the government. Such an institutional arrangement enlarged the gap between the enhanced authority of managers and the increasing willingness of workers to participate. Data from Survey C in 1991 showed that the majority of workers did not like the way wages, bonuses and benefits were distributed. When asked "do you think your income at the workplace should be transparent," 89 percent of the respondents supported the idea; at the same time, only 30 percent said they knew the standards of bonus distribution, while 74 percent reported that their bonuses were distributed only by managers rather than discussed by the working group, and 80 percent reported that housing distribution was controlled by managers. 73 percent of them thought their income was too low, but that of managers was too high. 82 percent agreed that "those who work harder are supposed to receive more," but actually only 45 percent thought this was the case at their workplaces, with 55 percent reporting "those who work less do not really earn less." Therefore, 66 percent of the respondents were not satisfied with the situation at the workplace, 46 percent were not satisfied with the leadership of their managers, and 42 percent believed that "the promotion of managers first of all is decided by their relations with bosses," rather than by their capabilities. When 76 percent said "problems at the workplace should be reformed," 79 percent felt they could do nothing to improve the situation. Finally, 48 percent of the respondents thought the management-worker relationship in 1991 was worse than that in 1984, and 45 percent perceived it worse than that in 1988.[111] The researchers of Survey C suggested that the authoritarian

[111] Feng Tongqing, and Xu Xiaojun, eds. *Zhongguo Zhigong Zhuangkuang: Neibu Jiegou ji Xianghu Guanxi* (The Status of Chinese Staff and Workers: Internal Structure and Relations), 98, 475-483.

management at Chinese workplaces simply produced more conflict, and that material incentives hardly worked. Actually, while bonuses increased to one third of workers' income and still kept growing, workers' motivation had not increased significantly; on the contrary, the more bonuses were distributed, the harder it would be for managers to raise motivation.[112]

The discussion above implies that China's enterprise reform starting in the mid-1980s had hit a bottleneck, if not a dead end. Two dilemmas are to be found. First, under the communist authoritarian regime, worker's political mobilization was prohibited, thus workers participation in decision-making at the workplace could hardly be institutionalized. Second, when workers' willingness to participate in the distribution of wages, bonuses and benefits increased, the authority of managers encountered a challenge, as workers understood themselves not simply as wage earners, but the master of their work organizations. The two dilemmas are deeply rooted in the communist system. With the dilemmas unsolved, the material incentives employed in the enterprise reform could rarely contribute to employee motivation. This was exactly the headache Gorbachev experienced.

Although enterprise reform in China did not really improve the efficiency of SOEs, the material incentives employed at workplaces did help maintain political stability. If we move our focus from the workplace to the state-society relationship, we can then understand how the political stability was sustained by an unsuccessful enterprise reform. Actually, material incentives can be seen as an instrument by which the state buys compliance and support from the people, and the state-society relationship can therefore be understood as a kind of social contract. The concept of the

[112] Ibid, 98.

social contract was used in Soviet Studies in the 1970s to explain the stability of the Soviet political system and was later developed further. Its basic idea is derived from a distinctive feature of the state-society relationship in which both the regime and populace contribute something the other needs for its survival, when rulers provide benefits and security and the people agree to acknowledge the legitimacy of the government, and to support, at least passively, the established political order.[113] The same concept can be used to describe the state-society relationship in China since the government initiated economic reform till the mid-1990s. The ability of the communist regime to finance the social contract is a precondition for the maintenance of the contract. During the period from the mid-1980s to the mid-1990s, the key resource the Chinese regime used was the loans from the state banking system to SOEs. The nature of the social contract in China became openly expressed after the June 4th massacre when the regime realized that its political stability could rely not only upon sticks, but needed to use more carrots. In the early 1990s, the official media in China would sometimes use the item "loans for political stability" (*an ding tuan jie dai kuan*). It means that the government offices ordered state banks to make loans to SOEs which lacked money, to maintain the social contract, and SOEs used the loans to pay wages, bonuses and benefits, but never bothered paying back the banks. This example explains how the material incentives of the enterprise reform served the social contract.

[113] Janine Ludiam, "Reform and the Redefinition of the Social Contract under Gorbachev," *World Politics*, No.43, 1991, 284-312; Linda J. Cook, *The Soviet Social Contract and Why It Failed: Welfare Policy and Workers' Politics from Brezhnev to Yeltsin*, Cambridge, MA, Harvard University Press, 1993.

Since maintenance of the social contract does not help improve the efficiency of SOEs but simply increases their wage and benefit expenditures, the financial state of SOEs gradually deteriorated. Indeed, the operating costs of state industries soared while profit declined from 15 percent in 1985 to two percent in 1993, and had remained low,[114] with half of the enterprises being money losers from 1995.[115] As these enterprises made little or no money but had to provide more wages and benefits to buy political compliance, they became increasingly dependent on bank loans. State banks were thus under constant pressure from SOEs to provide a steady stream of credit.[116] In 1994, the SOEs got 79 percent of their financial resources from state banks, but the percentage of their output as a portion of GNP fell to 43 percent.[117] The enterprises once had very few liabilities; in 1979, for instance, they only owed the banks a sum equal to 26 percent of their book value (depreciated fixed capital plus the value of all inventories). This ratio doubled from 1980 to 1989, and had risen to 83 percent by 1994.[118]

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[114] Cheng Xiaonong, "*Weichi wending yu shenhua gaige: Zhongguo mianlin de jueze* (Transition versus Stability: China's Dilemma)," Princeton, NJ, *Dangdai Zhongguo yanjiu* (Modern China Studies), No.1&2 (March 1995), 95.

[115] Niu Wenwen, "*Jianshao guoyou qiye de kuisun: jinhou de jianju renwu* (Reduce Losses of the State Sector: A Tough Task in the Next Years)," Beijing, China, *Jingji Ribao* (Economic Daily), Dec. 11, 1997.

[116] Barry Naughton, *Growing out of the Plan: Chinese Economic Reform, 1978-1993*, New York, NY, Cambridge University Press, 1995, 205.

[117] Cheng, Xiaonong, "*Fanrong cong he er lai?--Zhongguo Jingji Xianzhuang he Qushi de Fenxi* (The Puzzle of China's Economic Prosperity: Problems and Perspectives)," Princeton, NJ, *Dangdai zhongguo yanjiu* (Modern China Studies), No.3, 1996, 31-36.

[118] Cheng Xiaonong, "*Weichi wending yu shenhua gaige: Zhongguo mianlin de jueze* (Transition versus Stability: China's Dilemma)," 97; Gao Shangquan, "*Guoyou qiye de zhidu chuangxin he fazhan ziben shichang* (Institutional Innovation of State Enterprises and Development of Capital Market)," Beijing, China, *Jingji cankao bao* (Economic Information Daily), Sept. 30, 1997.

Key financial capacity in China rests on the state banks. Obviously, the more the state buys societal support, the weaker state capacity becomes.[119] By 1994, about 60 percent of bank loans had turned bad.[120] When dead loans from state banks exceeded the safe limit of the banking system in 1995, and a looming financial crisis threatened economic and political stability, the government finally had to take action to protect the banking system from collapse. To reduce the loans for wages and welfare expenditures of the nearly bankrupted SOEs, it changed its employment policy and allowed the SOEs to lay-off redundant workers. China's official statistics indicate that from 1995 to 1997 about 12 million SOE employees were laid off.[121] As the social contract was broken up, the Chinese government jumped over the unsolvable dilemmas of its earlier enterprise reform and moved to the privatization of SOEs.

6. Russia vs. China: The Path Dependence of the Preparation for Privatization

The privatization of hundreds of thousands of SOEs is not a game simply played by legislators and technocrats. The interaction between the government, managers and workers shapes the path privatization takes. Since the transition from state socialism to democracy and a market economy is not supposed to take the approach of a violent social revolution, managers, as part of

[119] Cheng Xiaonong, "Breaking the Social Contract," in Andrew Nathan, Hong Zhaohui and Steven R. Smith, eds., *Dilemmas of Reform in Jiang Zemin's China*, Boulder, CO, Lynne Rienner Publishers, Inc., 1999, 107-126.

[120] Cheng Xiaonong, "*Fanrong cong he er lai?—Zhongguo Jingji Xianzhuang he Qushi de Fenxi* (The Puzzle of China's Economic Prosperity: Problems and Perspectives)," 51.

[121] *Zhongguo Gaige Bao* (China Reform News), Beijing, China, January 21, 1998.

the *nomenklatura*, are not eliminated and certainly play a very active role in privatization. Their social status and social capital inevitably offer the elite group more opportunities and advantages than workers obtain. The sociopolitical changes prior to privatization decisively influence workers' social status and determine whether they will be able to impose their own choices. The *nomenklatura* in ministries and local administrations may also seek to obtain benefit through individual intervention in the privatization process. All the three groups may behave according to their values, beliefs, and practical calculations.

In the Soviet Union and China, people's attitudes toward possible changes in the socioeconomic sphere in the early reforms were quite similar. A majority of people did want changes in the sociopolitical system, but a lot of them were afraid of negative consequences of the reforms to their daily lives. When their living standards and job security were under threat, the blueprint of technocrats for privatization may not have appeared to be a sound plan. Managers and workers may have had the same interests in some respects, but different ones in others. Both the Russian and Chinese managers encountered an anti-management sentiment and distrust of workers. No matter how much managers were supported by the government, they had to re-position themselves during privatization. Workers in both countries were largely influenced by the communist ideological banner of the "masters of production." This belief could easily lead to embracing workplace democracy, which implies that they should have a vote, or at least have their voice taken into consideration. Moreover, workers worried about unemployment, and realized that job switching between industrial enterprises would not be easy and might simply result in downward mobility. Therefore, they may show increasing concern for the survival of their enterprise during privatization.

A fundamental difference between the sociopolitical environment for privatization in Russia and China is whether the workers were politically mobilized. While political liberalization in the Soviet Union empowered Russian workers, their Chinese counterparts lived under a repressive communist regime. The political rights of Russian workers obtained through collective struggle changed the balance of power between them and their managers, whereas the sociopolitical status of Chinese workers was weakened after 1989, and their managers, backed up by the authoritarian regime, gained much more freedom to act in a way that benefited themselves. This partly explains why many Russian managers were less ruthless to their employees than their Chinese counterparts in privatization. On the other hand, while the Chinese managers were still appointed by the government, the collapse of communist rule in the Soviet Union liberated the Russian managers from the control of the government; thus the latter was able to act independently, but the former had to pursue their own interests carefully along the policy direction. This difference suggests that the hand of government may have less influence at the enterprise level in Russia than in China.

The following chapters will explore how privatization in the two countries played out, and why the dependence of workers on their enterprises was reinforced in Russian's insider privatization, and how Chinese workers were deprived of dependence on their enterprises as privatization favoring management was carried out.

Chapter 5

The Process of Russian Privatization: Attitudes and Actions of Workers and Managers

Russia's privatization, a social experiment that involved hundreds of millions of people, might be the largest privatization in the world history. Victor Supyan pointed out that the privatization entailed complex social and economic consequences. Among them are: the emergence of a new social structure based mainly on the distribution of former state-owned assets; the formation of a new income structure, with much greater stratification than had existed under the Soviet regime, and with incomes derived from private capital that had never previously existed; the development of a new relationship between employees and management; and changes in work motivation and managerial practices.[1] Among Russian and Western scholars who analyzed the privatization, Supyan appears to be one of the few Russian researchers who have mentioned the changes in management-worker relationships after the privatization and considers the issue an important aspect to be explored. Indeed, without analyzing the management-worker relationship during and after privatization, we can neither well understand nor properly evaluate the process and its consequences, not only because managers and workers are the two key participant groups of the privatization in Russia, but also for the reason that their interaction and cooperation decided the direction of the process. This chapter discusses Russia's privatization by

[1] Victor Supyan, "Privatization in Russia: Preliminary Results and Socioeconomic Implications," Moscow, Russia, *Demokratizatsiya* (Democratization), winter, 2001, 1.

analyzing the attitudes and interaction of managers and workers during the process.

In most discussions by neoclassical economists, marketization includes liberalization of market signals (prices, interest rates, exchange rate, tax rates, etc.), macroeconomic stabilization, privatization and corporate governance. Usually such discussions focus on legal procedures or government regulations and deviations in practice from designed policy goals. The discourse may ignore a possibility that the legally approved procedures and regulations are frequently reformulated by different social groups who are able to influence the implementation of the policies. How and why social groups act is certainly an important topic for our analysis. In this chapter, the author will first briefly review the formation of the voucher privatization program, then focus on analysis of the attitudes and behavior of workers and managers whose enterprises were privatized, thus trying to answer why they selected an insider privatization, and how the insider privatization was further turned into a managerial privatization.

1. The Formation and Content of the Voucher Privatization Program in Russia

At the beginning of 1991 the Russian Federation had approximately 23,766 medium size and large industrial enterprises.[2] In the last years of the Soviet Union, large scale privatization had been discussed by some scholars. In 1990 Academician Shatalin, who became Gorbachev's informal economic adviser in late 1988, together with a young economist Yavlinsky, drafted a

[2] Joseph R. Blasi, Maya Kroumova, and Douglas Kruse, *Kremlin Capitalism: The Privatization of the Russian Economy*, Ithaca, NY, Cornell University Press, 1997, 25.

500-Day Program for a radical reform.[3] Shatalin and Yavlinsky were inspired by Poland's shock therapy and included in their program the privatization of SOEs by offering them for sale.[4] Gorbachev later realized that the program could not be adopted, though it was attractive because of its freshness.[5] In the first months of 1991, media in the country began in-depth discussion about privatization.[6] Soon, the Russian Supreme Soviet adopted the Act on the Privatization of State and Municipal Enterprises and the Act on Personal Privatization Accounts on July 3, 1991. The main elements of the laws related to the preparation of a state privatization program, the establishment of institutions responsible for managing the program and holding and transferring state assets, and the specification of methods of privatization and restrictions on the purchase of shares.[7] However, the laws simply provided a broad outline of how privatization was to occur, but did not include a detailed framework for implementation. Thus it was not ready for immediate operation. Some managers and workers had already begun a kind of experiment of privatization, however, by leasing their enterprises from the state. By Feb. 1992, 9,541 SOEs with eight percent of total employment had been leased by their managers and workers.[8]

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[3] Mikhail Gorbachev, *Memoirs Mikhail Gorbachev*, New York, Doubleday, 1995, 379.

[4] Joseph Blasi, et al. *Kremlin Capitalism: The Privatization of the Russian Economy*, 20.

[5] Mikhail Gorbachev, *Memoirs Mikhail Gorbachev*, 382-383.

[6] Pekka Sutela, "Insider Privatization in Russia: Speculations on Systemic Change," *Europe-Asia Studies*, 1994, Vol.46, Issue 3, 418.

[7] Timothy N. Ash, and Paul G. Hare, "Privatization in the Russian Federation: Changing Enterprise Behavior in the Transition Period," *Cambridge Journal of Economics*, No.18, 1994, 620-621.

[8] Joseph R. Blasi, et al. *Kremlin Capitalism: The Privatization of the Russian Economy*, 25.

In fact, since late 1991 the Russian people were weary of indecision over economic reform, and were exhausted with the talks about reform that did not produce real reform.[9] After Yeltsin and the Presidents of Ukraine and Belorusssia decided to end the Soviet Union, one of the earliest policies put on the agenda by Yeltsin was privatization. On December 29, 1991, Yeltsin issued a decree, the Basic Provisions of the State Program for Privatization of State and Municipal Enterprises in the Russian Federation. According to the July 1991 Act and the Presidential decree, about 90 percent of the small SOEs in retail, public catering and consumer services would be privatized through auction in 1992.[10] While managers and employees of the small SOEs or other investors could buy their enterprise with personal savings, the medium size and large industrial SOEs could hardly use this method, simply because the savings of the Russian population were inadequate to purchase such a huge volume of state assets, while price liberalization followed by hyperinflation eroded the purchasing power of personal savings. Moreover, public opinion surveys showed that many citizens were reluctant to use their savings to buy the shares of industrial enterprises being privatized.[11]

Among possible privatization approaches, the one often advocated by neoclassical economists is based on the proposition that SOEs should be sold to anyone who wants to buy them at the market price. This was commonly used in Western countries and Japan, and was adopted in Hungary, Estonia and Germany. However, it was not realistic in Russia. As Supyan

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[9] Lynn D. Nelson, and Irina Y. Kuzes, *Radical Reform in Yeltsin's Russia: Political, Economic, and Social Dimensions*, Armonk, NY, M.E. Sharpe, 1995, 42.

[10] Ibid, 44.

[11] Ibid, 45.

writes, neither companies nor individuals, nor even criminal organizations had enough free capital to purchase state-owned firms at market prices; nor did such investors existed abroad. Moreover, this approach failed to address issues of social justice. Theoretically, the liberal approach is supposed to promote maximum economic efficiency through responsible ownership of enterprises. For Russia, however, the approach would have been economically counterproductive because of the length of time required to make it work.[12] In Russia, leftist political forces, including the newly reorganized communist party, left-wing intellectuals, and labor unionists pursued another approach, i.e. to transfer SOEs to the work collectives or to sell the enterprises to the collectives on an installment plan, using discounted government loans, then let the privatized enterprises be run by workers' self-management. The second approach obviously discriminates against the interests of the citizens who do not work in SOEs. Assuming that all Russian people had participated in the creation of national wealth in the communist era, a third approach could be a free distribution of SOEs to the whole Russian population.[13] Interestingly, while the drafting of the Russian privatization program started more or less from the idea of the first approach and was then altered in the direction of the third approach, the actual process of privatization began through a combination of the second and third approaches, but ended with a structure that none of the three approaches had ever provided for. The formation of the privatization program and its implementation were indeed a contested terrain affecting various social forces and the bulk of the Russian population.

[12] Victor Supyan, "Privatization in Russia: Preliminary Results and Socioeconomic Implications," 2.
[13] Ibid.

On January 29, 1992, Yeltsin issued a decree to accelerate privatization of state and municipal enterprises. The Russian government established *Goskomimushchestvo* (*GKI*, the State Property Committee) and its local offices and *Rossiiskii Fond Federalnogo Imushchestva* (Russian Federal Property Fund) and its local agencies. The former was in charge of decision-making during the privatization, by appraising and approving the privatization plan of each SOE; the latter implemented the decisions by organizing tenders and auctions of shares of SOEs.[14] According to the July 1991 privatization act, managers and workers could only obtain 25 percent of shares of their own enterprise free of charge. This option was later included in the final version of the privatization program as Option 1 (*Variant 1*). The limit opened the door for outsiders to obtain control of the enterprises. However, during the spring of 1992, under the leadership of Arkady Volsky, the head of the Russian Union of Industrialists and Entrepreneurs, the opponents to the original privatization program mobilized enormous pressure for alternative options favorable to them. They worked together with the Federation of Independent Labor Unions. Their protests resulted in the passage by the Supreme Soviet of an expanded privatization law on June 11, 1992. It provided an alternative option for insiders, later often called Option 2 (*Variant 2*), to satisfy both the representatives of the communist party and the faction of managers in the Supreme Soviet.[15] It was in the fights among various social and political forces that the final draft of the voucher privatization program in Russia

[14] Timothy N. Ash, and Paul G. Hare, "Privatization in the Russian Federation: Changing Enterprise Behavior in the Transition Period," *Cambridge Journal of Economics*, No.18, 1994, 622-623.

[15] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, London, UK, Routledge, 2003, 80-81.

was completed. In an interview about the privatization process, Anatoly Chubais, the head of the Russian privatization program, admitted: "This is not an economics program; it is a political program. It is five percent economics and 95 percent politics."[16]

The Russian administration had to balance different social and political forces, and maintained a fragile cooperation with the Supreme Soviet in order to have its privatization program implemented. Several important forces that greatly influenced the drafting and approval of the privatization program included the Supreme Soviet, branch ministries, managers, workers, and the public. The Supreme Soviet was lobbied heavily by managers, labor unions and the state apparatus; the branch ministries and departments tried to get their enterprises out of privatization, and managers and workers wanted to prevent outside investors from taking over. Moreover, a large portion of Russian citizens working outside the SOE system, who had contributed to the accumulation of the state assets, also staked their claim to the benefits of redistribution through privatization. Therefore, the deputy chairman of *GKI* said in the summer of 1992: "We have changed our position over time, partly because of political compromise, and partly because we have learned more about the situation."[17] Certainly the situation was much more complicated than what was imagined by the Western economic advisors to the Russian administration.

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[16] Lynn D. Nelson, et al. *Radical Reform in Yeltsin's Russia: Political, Economic, and Social Dimensions*, 158.

[17] Lynn D. Nelson, and Irina Y. Kuzes, "Coordinating the Russian Privatization Program," *RFE/RL Research Paper*, Vol.3, No.20, May 20, 1994, 16-23.

In order to pull the privatization program out of endless debate at parliament, on July 1, 1992, Yeltsin issued the No. 721 Presidential Decree, On Organizational Measures to Transform State Enterprises and Voluntary Associations of State Enterprises into Joint-Stock Companies, which required that all enterprises subject to privatization be converted to open join-stock companies by November 1, 1992. After the decree for mandating corporatization of SOEs, on August 14, 1992, Yeltsin signed another decree authorizing the voucher privatization program. According to the program, in the privatization process, 149 million vouchers, each with a nominal value of 10,000 rubles, were issued to Russian citizens in November 1992. Even so, some local Soviets and administrations still attempted to stop the voucher option. The resistance to the privatization was not simply based on the concerns for the welfare of the local community, but also sometimes out of a wish to retain their longstanding control over local enterprises. "They want to keep the most efficient enterprises under their supervision."[18] At the same time, public opinion surveys revealed that "more than half of Russian respondents preferred an option where they could own their enterprise collectively and appoint their managers."[19] Comparing this attitude to that of Polish workers, one may find a significant difference in values and political culture between Russian and Polish or between the cradle of revolution and the place where communist rule was imposed. At the Third National Convention of Poland Solidarity in Feb. 1991, delegates were surveyed. When asked whether they thought employees should elect directors in

[18] Ibid, 20-21.

[19] Vladimir Magun, "Job Values and Labor Ethics in Socialist and Post-socialist Russia," Moscow, Russia, the Institute of Sociology and the Institute of the World Economy and International Relations of the Russian Academy of Sciences, 1994, p.36.

state-owned firms, 50 percent of the white-collar delegates and 44 percent of the blue-collar delegates answered never or rarely.[20]

While the Russian Presidential decrees were perceived as a compromise to the demands of managers and workers of SOEs, they were, at the same time, considered by many a reaction to the moves of the spontaneous privatization promoted by the *nomenklatura* of the branch ministries. Nelson and Kuzes noted that once the *nomenklatura* realized the inevitability of the privatization, they turned to acquire control over the enterprises to be privatized.[21] From 1991 to 1992, having adopted the discourse of market reform and privatization, a lot of the branch ministries were eager to convert themselves into new commercial organizations in the period immediately before the formal dissolution of the Soviet Union. Sometimes they simply converted the same industrial sector they administered into a new corporation. The new corporations could take two forms: either a supra-enterprise body, as a company holding controlling stake in each of its member enterprises, or a joint-stock corporation in which the member enterprises held all the shares in the supra-enterprise body. "Most of the top officials of the old ministries chose to move into the 'commercial' organizations."[22] The policy makers of the privatization thus had to break up the power of the state apparatus as soon as possible by building a foundation for democracy and independent enterprise through privatization. As the Presidential decrees offered the insiders of

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[20] Marc Weinstein, "Competing Notions of Stakeholders Rights in Poland," paper presented to Eighth International Conference of Europeanists, Chicago, March 1992; cited from David Ost, "Labor in Post-Communist Transformations," Berkeley, CA, Center for German and European Studies, University of California, *Working Paper 5.17*, July 1993.

[21] Lynn D. Nelson et al. *Radical Reform in Yeltsin's Russia: Political, Economic, and Social Dimensions*, 145.

[22] Stephen Fortescue, "Organization in Russian Industry: Beyond Decentralization," *RFE/RL Research Paper*, Vol.2, No.50, Dec., 1993, 35-39.

SOEs voting power to determine whether they wanted to be put under the umbrella of the *nomenklatura*'s supra-enterprise body (only if at least 50 percent of the work force of each enterprise agreed), the double-edge sword of the voucher privatization program reduced the possibility of the holding companies established by the *nomenklatura* taking over the previous constituency enterprises under control on the one hand, but, on the other, opened the door for the insider privatization.

Russia formally began its voucher privatization of mid-size and large industrial SOEs in the latter half of 1992. On October 14, 1992 another Presidential decree On Promoting the System of Privatization Vouchers in the Russian Federation (No.1229) was issued.[23] According to the final version of the voucher privatization program, while the industrial SOEs were corporatized as joint-stock companies (JSCs), they were supposed to be sold through issuing their shares to buyers. At the same time, every adult Russian citizen acquired, after payment of an administration fee, a voucher with a nominal face value of 10,000 rubles. These vouchers could be used to bid for shares of JSCs through voucher auctions organized by the offices of the Russian Federal Property Fund. Voucher owners could sell the vouchers on the open market or through registered security exchanges, bid for shares directly via the auctions, or divest the shares to investment funds which then used the shares to bid for JSC shares in the auctions.[24]

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[23] Alexander Radygin, "The Russian Model of Mass Privatization: Governmental Policy and First Results," in Michael McFaul, and Tova Perlmutter, eds, *Privatization, Conversion, and Enterprise Reform in Russia*, Boulder, CO, Westview Press, 1995, 6.

[24] According to Alexander Radygin, "The market price of vouchers rose steadily until mid-December, 1992, although it was still short of the face value; it then fell sharply to one-third of the face value by early February 1993. From mid-February, the rate increased again, and was relatively stable by May. Large-scale

Also, workers and managers of SOEs might use their vouchers to pay for the referential sale of shares via methods selected from three options.[25] About 30 percent of SOEs, including the energy and military-industrial enterprises, were not subject to the privatization.[26] The three options provided in the final version of the voucher privatization program for selection by SOE employees are listed below.

Option 1 (*Variant 1*): Workers of JSCs can receive a free allocation of non-voting shares to 25 percent of the capital value of their firms, and up to a maximum of twenty times the maximum salary of each worker. The distribution of the shares among workers is decided by enterprise's work collective. Beyond the free allocation of the 25 percent non-voting shares, workers have the right to purchase shares of their enterprise at 30 percent of the nominal share value, up to a limit of ten percent of the capital value of the firm; managers are able to purchase five percent of the shares of the JSC. The remaining shares can be sold through a voucher auction to potential investors, including foreign buyers. Workers may receive a sum equal to ten percent of the

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clearing operations of 10,000-30,000 vouchers at a time helped to stabilize the market as opposed to short-term speculations with cash payments. By September-October, 1993, the price of the voucher was between 10,000 and 12,000 rubles, varying according to the political situation and fluctuation both on exchanges and in private sales. It should be noted that due to rapid inflation throughout 1992 and 1993, 10,000 rubles at the end of 1993 was worth less in real terms than 4,000 rubles in the fall of 1992." Ibid, 7.

[25] Timothy N. Ash, and Paul G. Hare, "Privatization in the Russian Federation: Changing Enterprise Behavior in the Transition Period," 623-625.

[26] However, a lot of managers of military-industrial giants were eager to privatize their enterprises. As *Samala* Research Group observed, "Far from trying to avoid privatization, chiefs of many enterprises which were initially excluded because of their military significance even tried to reclassify their enterprises to take advantage of the opportunities opened up by privatization." *Samala* Research Group, "Two Military-Industrial Giants," in Simon Clarke ed., *The Russian Enterprise in Transition: Case Studies*, UK, Edward Elgar, 1996, 249.

proceeds from the sale of the firm, which could then be used to purchase shares of the enterprise.[27]

Option 2 (*Variant 2)*: On the approval of two-thirds of the workers of the enterprise, workers can purchase 51 percent of the shares of the enterprise through a closed subscription, by paying a price for the shares 70 percent above the book value. Not less than 50 percent of the payment has to be made in vouchers, whereas the rest of the payment can be made in cash, which can be accumulated through the enterprise's privatization fund. The remainder of the shares was to be sold at voucher auction or by tender.[28]

Option 3 (*Variant 3)*: This option is limited to enterprises with more than 200 workers and with assets valued at between one and 50 million rubles (in 1991 purchasing power). On the approval of two-thirds of the workers, a group of employees (including managers) that promises to restructure the enterprise by signing a contract can purchase twenty percent of the shares; in addition, employees of the enterprise are entitled to purchase twenty percent of the shares at a 30 percent discount up to a maximum value of twenty times the minimum wage of each employee. Payment for all shares bought by workers can be made in vouchers.[29]

Under Option 1, workers and managers may obtain up to 40 percent of the shares of their enterprise, of which 25 percent are free, thus establishing minority employee ownership would be established. This option allowed managers to acquire five percent of shares on very beneficial

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[27] Timothy N. Ash, and Paul G. Hare, "Privatization in the Russian Federation: Changing Enterprise Behavior in the Transition Period," 624.

[28] Pekka Sutela, "Insider Privatization in Russia: Speculations on Systemic Change," 421; Victor Supyan, "Privatization in Russia: Preliminary Results and Socioeconomic Implications," 5.

[29] Timothy N. Ash, and Paul G. Hare, "Privatization in the Russian Federation: Changing Enterprise Behavior in the Transition Period," 624; Joseph R. Blasi, et al. *Kremlin Capitalism: The Privatization of the Russian Economy*, 41.

terms, but the traditional workers' opposition to management privileges made it less acceptable to workers. Under Option 2, workers and managers may obtain control over their enterprise by buying 51 percent of the shares with cash and vouchers at a price 70 percent higher than the asset's book value. This is a relatively expensive way of buying shares for employees, but it guarantees majority employees control at pre-auction tender.[30] Option 3 is actually an approach favorable for management buyout, applied only to medium-size enterprises.[31] The Russian privatization administration then believed that, among the three options, Option 1 would become the most popularly selected approach by workers and managers;[32] however, the actual result turned out to be quite different, as about 80 percent of the privatized enterprises selected Option 2.[33] But, "in large, capital-intensive enterprises, insiders were unable to accumulate enough funds to buy 51 percent of shares under Option 2; as a result, these firms mostly followed Option 1 privatization."[34]

When making decisions, the Russian privatization administration assessed that Russian SOE workers would make practical calculations in selecting their preferred option for privatization. This consideration is certainly reasonable. However, it fails to read the minds of most workers and managers correctly. As the privatization regime believed that the free shares distributed to the workers regulated by Option 1 were more attractive in contrast to Option 2,

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[30] Trevor Buck, Igor Fliatotchev, and Mike Wright, "Employee Buyouts and the Transformation of Russian Industry," *Comparative Economic Studies*, Vol.36, No.2, summer 1994, 8.

[31] Joseph R. Blasi, et al. *Kremlin Capitalism: The Privatization of the Russian Economy*, 41.

[32] Pekka Sutela, "Insider Privatization in Russia: Speculations on Systemic Change," 421.

[33] Victor Supyan, "Privatization in Russia: Preliminary Results and Socioeconomic Implications," 5.

[34] Paul Hare, and Alexander Muravyev, "Privatization in Russia," Moscow, Russia, Russian-European Center for Economic Policy, *Research Paper Series*, Aug. 2002, 7.

in that workers had to pay for the shares at quite a high price, it seemingly speculated that the motivation of the workers in the selection would be money-driven and based on a short-run cost-profit analysis. Actually, the majority of the SOE employees selected Option 2 instead, not only driven by concern over job security, a kind of long-term calculation of gains and losses after privatization, but also guided by their values and beliefs. The gap between the perceptions of the policy makers and those of the workers suggests a need to analyze workers' attitudes toward privatization.

2. The Panic and Hesitation of Workers in Privatization

The privatization program shifted workers' attention from the nationwide struggle against the communist leadership to the workplace. For Russian workers whose enterprises were privatized, it was the first time in their lives that they were given an opportunity to determine which option they would like to select for their future well-being. Then questions arose: what did they think about privatization and why? Although the VCIOM provides a lot of data about workers' attitudes towards privatization, researchers of privatization seldom analyze the data systematically, and the motives of Russian workers have not been well explored. This section will fill the gap. As the majority of workers chose Option 2 for insider privatization, five questions need to be discussed: First, do they worry about their job security? Second, do workers support privatization? Third, do they expect to become the owner of their own enterprise? Fourth, do they buy the shares of their own enterprise or that of other enterprises? And the fifth, do they perceive

themselves owner-controllers of their privatized enterprise if they hold controlling shares in it?

2.1. The Job Security Concerns of Russian Workers

First of all, what was the key concern of Russian workers right before privatization started? From 1993 to 1994, during the privatization period, the VCIOM survey designers listed a series of questions regarding job security, together with questions about workers' attitudes towards privatization, and the survey data show that about 80 percent of respondents worried about losing their job in 1993, the key year of the voucher privatization (see Table 5-1).

Table 5-1 Employees' Worry about Job Security

Respondents	Mar-Apr. 1993 (%)	Dec.1993 (%)
Total respondents	80	83
By age group		
Under 29 years old	77	…
30-49 years old	83	…
50 years old & above	78	…
By groups with different education		
Higher education	82	…
Seven years' school	82	…
Incomplete Seven years' school	77	…
By occupation group		
Skilled worker	77	79
Unskilled worker	77	81
Technician	84	86
Clerical worker	86	87
Manager	79	92
Respondents in industry, construction and transportation	81	86

Note: The question is: "Do you think that people have recently begun to be more or less in danger of losing

their jobs?"
Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), Moscow, Russia, Aspect Press, No.2, 1993, 53, 58, 66, No.3 1994, 54, 59. Sample size: the 1993 Mar.-Apr. survey, 1,999; the 1993 December survey, 1,799.

Obviously, job insecurity was one of the top concerns of the majority of the Russian working population. Indeed, "In the final years of the Gorbachev era, practically everyone in the Soviet Union was experiencing insecurity, especially concerning their economic future. This insecurity was shared not only by people who wished for a return to the old ways, but also by those who looked forward to the establishment of a market economy."[35] When the majority of working people had the worry of losing their job during almost the entire year of privatization, it was no longer a concern simply based on the individual status of certain social groups; instead, it was a widely existing social phenomenon. The author uses "panic" to describe the psychology of the Russian population regarding these worries. As almost no one in the society then had any memory or experience of a market economy after 70 years of communist rule, suddenly people were led into a period when radical transition was accompanied by a worsening economic situation. It is understandable that, encountering great uncertainty and a completely unfamiliar new socioeconomic system, the Russian people would most care about job security, because that would be their only way to survive.

[35] Gemnady M. Denisovsky, Polina M. Kozyreva, and Mikhail S. Matskovsky, "Twelve Percent of Hope: Economic Consciousness and a Market Economy," in Arthur H. Miller, William M. Reisinger, and Vicki L. Hesli, eds, *Public Opinion and Regime Change: the New Politics of Post-Soviet Studies*, Boulder, CO, Westview Press, 1993, 224.

Table 5-2 Threat of Layoff at Workplace

Respondents	Mar-Apr. 1993 (%)	Aug. 1993 (%)	Dec.1993 (%)
Total respondents who responded “YES	46	46	48
By occupation group			
Skilled worker	45	…	50
Unskilled worker	42	…	40
Technician	48	…	47
Clerical worker	45	…	45
Manager	42	…	49
Respondents in industry, construction and transportation	57	…	61
Total respondents who responded “No”	40	44	32

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial’nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 63, 71, No.3 1994, 54, 59. Sample size: The 1993 Mar.-Apr. survey, 1,827; the 1993 Aug. survey, 1,805; the 1993 Dec. survey, 1,799.

Table 5-3 Employees’ Worry about Job Security at the Workplace

Respondents	Mar-Apr. 1993 (%)	Aug.1993 (%)	Dec.1993 (%)
Total respondents	37	42	38
By age group			
Under 29 years old	34	…	34
30-49 years old	36	…	37
50 years old & above	42	…	45
By groups with different education			
Higher education	35	…	35
Seven years’ school	39	…	40
Incomplete Seven years’ school	34	…	36
By occupation group			
Skilled worker	36	…	41
Unskilled worker	42	…	36
Technician	37	…	36
Clerical worker	38	…	36
Manager	32	…	36
Respondents in industry, construction and transportation	41	…	46

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial’nae Peremenay: Monitoring*

Obshchestvennego Mneniia, Informatsionnay Bulletin (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 54, 64, 72, No.2, 1994, 78, 84, 89. The percentages include those who reported "very likely" and "there exists such a possibility." Sample size: The 1993 Mar.-Apr. survey, 1,827; the 1993 Aug. survey, 1,805; the 1993 Dec. survey, 1,799.

Another reason why the worries of loss were perceived as panic is because they were not completely based on employees' observations of the situation at the workplace. As evidence, the answers to the question "in your company, is there a threat of a significant reduction in the work force" suggest that the Russian working population were less worried about the real threat of large-scale layoffs at the workplace, as the percentage of respondents who indicated this was only about 45 percent (see Table 5-2). If the threat of large-scale layoffs was lower, did the employees worry about smaller-scale dismissals? The answers to another question "do you think you personally could lose job in the near future, in connection with a reduction of staff, or a liquidation of workers at your workplace" confirm that only about 37 to 42 percent of the respondents were so concerned (see Table 5-3).

Moreover, the data in Table 5-1, Table 5-2 and Table 5-3 show that age, education and occupation differences are not significant. In other words, employees had almost the same degree of worries about losing job, and the worries in industrial enterprises were either the same as the average for all economic sectors or a little bit higher. If the lower percentages in Table 5-2 and Table 5-3 were interpreted as a sign of the real situation at the workplace, the difference between them and that in Table 5-1 might be considered a result of the impact of social panic in that year, for several possible reasons. It may have been a reflection of the

worsening economic situation and the feeling of uncertainty linked with privatization, or a result of SOE managers threatening to fire workers. If the workers had believed that the threat of losing a job came from within the workplace, they might have united against their managers in order to protect their jobs. However, such organized activities do not seem to have happened widely and frequently.

As explained in chapter four, before the privatization many Russian workers had already accumulated experiences in labor organizing. If workers believed that the threat of losing their jobs was likely to be due to their managers, would they defend their job security by organized struggles at the workplace? In the VCIOM survey conducted in Mar.-Apr. 1993, a question was asked: "How did the threat of retrenchment, and being in danger of losing their jobs, influence the behavior of the workers in your company?" The answers to the question are: first of all, while 23 to 34 percent of the respondents believed that "the danger of cutting jobs would arouse estrangement among workers," only about one to four percent of the respondents selected "organizing collective activities against the dismissal," and three to twelve percent of them selected "reviving the unity of the working collective," although 19 to 29 percent considered the possibility of "fighting for workers' interest" as a response to layoffs. At the same time, 21 to 34 percent of the respondents selected "looking for another job without waiting for dismissal," (skilled workers and technicians were more interested in that) and 13 to 27 percent, particularly technicians and clerical workers, preferred to "approach the boss to secure his support" (see Table 5-4). It seems that they tended to behave more individually than collectively. Workers' low inclination to organize struggles against managers suggests that the

panic of losing their jobs was more closely linked to their worries about the consequences of privatization than the actions of their managers.

Table 5-4 Possible Behavior Responding to a Layoff

Possible Behavior	Skilled Labor (%)	Unskilled Labor (%)	Technician (%)	Clerical Worker (%)
A rise in estrangement among workers	26	23	34	32
Conflicts and fights initiated for Workers' interests	19	21	24	29
People begin to look for another job, and retire without waiting for dismissal	31	21	34	26
Many try to approach their boss to secure his support	16	13	27	20
People become more tolerant of each other	7	11	8	7
The unity of the working collective is revived	4	12	3	5
Organize collective activities against the dismissal	2	5	1	1
Others	2	0	3	1
Hard to answer	32	21	25	28

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 63. Sample size = 1,827.

2.2 The Attitudes of Workers to Privatization

In order to get rid off the Soviet system, Russia had to start its privatization without a satisfactory social or psychological preparation for the radical transformation that was to come. While the panic of losing work preoccupied the majority of Russian workers, their top concern

was survival rather than building an ideal private enterprise system as expected by many Western economists.

Table 5-5 Attitudes towards Privatization Program

Evaluation to Privatization Program	Mar-Apr. 1993 (%)	Aug. 1993 (%)	Dec.1993 (%)
The approach offers people material support	10	11	10
A step so people could become owner	15	14	19
Just a show, actually nothing is going to change	53	56	49
Hard to answer	21	19	21
Did not answer	1	0	1
Total	100	100	100

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 57, No.3, 1994, 53. Sample size: The 1993 Mar.-Apr. survey, 1,999; the 1993 Aug. survey, 1,805; the 1993 Dec. survey, 1,799.

What did Russian employees really think about the voucher privatization that was pushed by the government? The VCIOM surveys asked a question "there are various points of view regarding the making of privatization checks (vouchers) available to the public; with which of these do you most strongly agree, " and Table 5-5 shows the responses. About 49 to 56 percent of the respondents thought the privatization program was "simply a show and will not change anything." Only about fifteen percent believed "the privatization program is a step to make people owners."

Moreover, analyzing the attitudes of managers and employees towards privatizing their own enterprise, the author noticed that about one third of Russian respondents found it hard to

answer, about 20 percent thought privatization of their own enterprises was unnecessary, those who opposed privatization decreased from ten to three percent as the mass voucher privatization program had already moved ahead in 1993, and only about one third to 40 percent of the respondents thought the privatization of their own enterprise necessary (see Table 5-6).

Table 5-6 Attitudes toward Privatizing Own Enterprise

Answers	Mar-Apr. 1993 (%)	Aug. 1993 (%)	Dec. 1993 (%)
"Necessary"	34	41	38
By occupation group:			
Manager	26	…	61
Technician	43	…	48
Clerical worker	30	…	36
Skilled labor	35	…	36
Unskilled labor	13	…	27
"**Not Necessary**"	20	20	20
By occupation group:			
Manager	42	…	14
Technician	17	…	21
Clerical worker	24	…	23
Skilled labor	18	…	20
Unskilled labor	0	…	14
"**I'm Opposed to Privatization**"	9	5	3
By Occupation Group:			
Manager	21	…	2
Technician	11	…	2
Clerical worker	6	…	3
Skilled labor	9	…	3
Unskilled labor	6	…	6
Hard to answer	37	33	38
Not answered	0	1	1
Total	100	100	100

Note: The question is: "Do you think your enterprise needs to be privatized?"

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 61, No.2, 1994, 77. Sample size: The 1993 Mar.-Apr. survey, 1,827; the 1993 Aug. survey, 1,805; the 1993 Dec. survey, 1,799.

The attitudes indicate that only a small portion of the interviewees were opposed to privatization, but the portion of those who supported it was not large either. Very likely, many Russians did not fully understand what a private company was supposed to be and what kind of roll they were supposed to play in it. Looking at each occupational group, the author found that the percentage of those who supported privatization was significantly higher among technician and skilled workers than unskilled workers, while among the latter only 13 to 27 percent thought it was necessary. The more educated and skilled groups showed more confidence in privatization.[36] The difference was also reported by Gordon and Klopov, based upon the VCIOM July 1992 data which was not published.[37] Generally speaking, about 60 percent of the Russian working population did not embrace the privatization program enthusiastically.

2.3 Workers' Preferred Owners of the Privatized Enterprises

In the voucher privatization process, in order to seek the attitudes of respondents based on their values and beliefs, the VCIOM repeatedly asked "whom would you like to see in the role of the enterprise's owner," with six choices, "working collective," "current management,"

[36]The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay:Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2 (Mar-Apr), 1994, 77.

[37] Leonid A. Gorden, and Eduard V. Klopov, "The Workers' Movement in the Post Socialist Russia," *Sociological Research*, Vol.33, No.2 (March-April), 1994, 77.

"current director," "new owner from Russian entrepreneurs," "foreign entrepreneurs," and "the board of shareholders." The answers to the question are shown in Table 5-7.

Table 5-7 Preferred Owners of the Privatized Enterprises

Preferred New Controller	Mar-Apr. 1993 (%)	Sept.1994 (%)
Working collective	40	47
By Occupation Group:		
Manager	43	39
Skilled labor	45	49
Current management	2	2
By occupation group:		
Manager	8	8
Current director	11	10
By occupation group:		
Manager	11	22
New owner from Russian entrepreneurs	7	5
Foreign entrepreneurs	5	5
Board of shareholders	15	12
Other	1	1
Hard to answer	18	18
Not answered	1	0
Total	100	100

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, p. 63, No.6, 1994, p.80. Sample size: The 1993 Mar.-Apr. survey, 1,827; the 1993 Sept. survey, 1,700. The percentages include only answers of the respondents whose enterprises had already been privatized or would be privatized.

From Table 5-7 it could be found that about 40 to 47 percent of the respondents preferred the working collective as the new owners of the privatized enterprises; and skilled workers were more inclined to the option than other occupational groups. Only about fourteen percent

of the respondents considered the board of shareholders desirable as the new owners of the privatizing enterprises. When only five to seven percent of the respondents welcomed the new Russian entrepreneurs as new owners, and another five percent chose foreign investors, about twelve percent would rather have their current managers as new owners. It should be pointed out that, in September of 1994 when the insider privatization was done and workers already held controlling shares, still only about thirteen percent of the respondents wanted the board of shareholders to be the owners. This attitude suggests that their support for the working collective to be the owner is linked to a belief that the working collective is the master of the enterprise.

Another phenomenon noticeable is that the respondents did not want their managers to be the new owners. Very likely, many of them did not really think their managers were capable of improving the performance of their own enterprises. When respondents were asked “do you consider your firm’s (organizational) leadership capable of really improving its economic position,” only about 31 to 32 percent of them were confident in the ability of their managers. Technicians who knew more about technological potential of their enterprises were seemingly even less confident than other employees (see Table 5-8).

Table 5-8 Employees' Confidence in the Ability of Their Managers

Respondents	Aug.1993 (%)
Total respondents	31
By age group	
Under 29 years old	35
30-49 years old	30
50 years old & above	28
By groups with different education	
Higher education	33
Seven years' school	30
Incomplete Seven years' school	32
By occupation group	
Skilled worker	33
Unskilled worker	23
Technician	27
Clerical worker	30
Manager	47
Respondents in industry, construction and transportation	34

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.6, 1993, 54, 73. Sample size = 1,981.

3. Insiders vs. Outsiders: Why the Voucher Privatization Became Insider Privatization?

When many SOE employees were not quite sure how the voucher privatization program would affect their lives, they acted on their own judgment. As no nationwide survey was done in Russia on the voucher transactions, we may use the VIOCM opinion data to convey a brief picture of voucher transactions during privatization.

After the voucher privatization was officially started, there were four possibilities for SOE employees to buy the stocks of the privatizing enterprises (see Table 5-9): buy stocks of their own and other enterprises (type I); buy stocks of their own enterprise only (type II); buy stocks of other companies only (type III); and do not buy any stock (type IV).

Table 5-9 Four Possible Types of Stock Buying

		Buy Stocks of Own Enterprise	
Buy Stocks of Other Enterprises		Yes	No
	Yes	Type I	Type III
	No	Type II	Type IV

In the VCIOM surveys there are two related questions: 1. Did you buy the stocks of your own enterprise? 2. Did you buy the stocks of other companies (including investment funds)? The two questions did not clearly differentiate between the four types. However, by analyzing the responses to the two questions, the author got a glimpse of the behavior of the participants in privatization.

The data include the percentages of those who “do not want to buy the stocks of their own enterprise” and of those who “do not want to buy the stocks of other companies.” As the percentage of “do not want to buy the stocks of their own enterprise” includes Type III and Type IV, and the percentage of “do not want to buy the stocks of other companies” includes Type II and Type IV, their difference ((Type II + Type IV) – (Type III + Type IV) = (Type II - Type III)) reflects the difference between the percentage of Type II and that of Type III. In

other words, the percentage of those who selected “do not want to buy the stocks of their own enterprise” and that of those who selected “do not want to buy the stocks of other companies” both include the fraction of Type IV of those who did not want to buy any stock nor invest their vouchers in any privatization investment fund; very likely, they privately exchanged their vouchers for cash (with friends, brokers, or their managers), if not for vodka. This fraction of the SOE employees could be identified as inactive participants in voucher privatization, but we can not find out the exact figure of this portion. One would assume that the percentage of Type II (those who bought stocks of their own enterprise but did not want to buy the stocks of other companies) is higher than that of Type III (those who bought stocks of other companies but did not want to buy the stock of their own enterprise), because employees usually are missing the performance and financial information of other companies. If the percentage of Type II is significantly higher than that of Type III, the difference, together with other data, could be considered evidence of an inclination toward insider privatization.

From the VCIOM data it is found that about 55 to 60 percent of the employees of the privatizing enterprises chose to buy the stocks of their own enterprises, among them the skilled workers and managers were more interested in doing so; and the percentage of the employees in the industrial, construction and transportation sector was 62 to 72 percent, much higher than that of the enterprises in other sectors (see Table 5-10). At the same time, 45 percent of the employees did not want to buy the stocks of other enterprises or investment funds, and the percentage of the employees in the industrial, construction and transportation sector in April 1994 was 54 percent, much higher than the average of all sectors (see Table 5-11).

Table 5-10 Participation Rate of Privatizing Own Enterprise

Answers	Mar/Apr. 1993 (%)	Aug.1993 (%)	Dec.1993 (%)	Apr.1994 (%)
"I Already Bought"	27	32	37	34
By occupation group:				
Manager	21	…	53	33
Skilled labor	29	…	39	36
Technician	27	…	34	32
Unskilled labor	23	…	31	31
Clerical worker	25	…	28	32
Respondents in industry, construction and transportation	33	…	49	43
"I May Buy"	30	22	22	21
By occupation group:				
Manager	49	…	22	30
Skilled labor	26	…	23	21
Technician	35	…	19	21
Unskilled labor	16	…	25	10
Clerical worker	38	…	24	22
Respondents in industry, construction and transportation	31	…	23	19
"Do not Want to Buy"	43	46	41	45
By occupation group:				
Manager	30	…	25	37
Skilled labor	45	…	38	43
Technician	38	…	47	47
Unskilled labor	61	…	44	59
Clerical workers	37	…	48	46
Respondents in industry, construction and transportation	36	…	28	38
Total	100	100	100	100

Note: The question in questionnaire is "Did you to buy stocks of your own enterprise?"

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 56, 66, No.2, 1994, 78, 83, No.4, 1994, 62, 68. Sample size: The 1993 Mar.-Apr. survey, 1,818; the 1993 Dec. survey, 1,799; the 1994 Apr. survey, 1,698. The data only included the answers of the employees whose enterprises had already been or would be privatized.

Table 5-11 Participation Rate of Privatizing Other Enterprise

Answers	Mar/Apr. 1993 (%)	Aug.1993 (%)	Dec.1993 (%)	Apr.1994 (%)
"I Already Bought"	7	17	23	27
By occupation group:				
Manager	14	…	35	32
Skilled labor	5	…	22	28
Respondents in industry, construction and transportation:			28	34
"I May Buy"	30	25	24	11
By occupation group:				
Manager	37	…	27	9
Skilled labor	26	…	23	11
Respondents in industry, construction and transportation:			31	11
"Do not Want to Buy"	41	38	36	46
By occupation group:				
Manager	22	…	23	39
Skilled labor	48	…	40	47
Respondents in industry, construction and transportation			41	55
"Hard to answer"	22	20	17	16
Total	100	100	100	100

Note: The question is "Did you buy stocks of other companies?"
Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 57, No.2, 1994, 78, 84, No.4, 1994, 62, 68. Sample size: The 1993 Mar.-Apr. survey, 1,818; the 1993 December survey, 1,799; the 1994 April survey, 1,698.

Declining to have an outside new owner like Russian new entrepreneurs or foreign investors (see the data in Table 5-7) who might lay off current employees, the employees of the privatizing enterprises used their vouchers and money to gain ownership of their enterprises. Given that they were not confident about the necessity and effects of privatization, this could

be interpreted as defensive behavior meant to protect the status quo at the workplace from possible threats of lay-offs, and well explains why about 80 percent of the privatized enterprises selected Option 2 in the voucher privatization program.

Comparing the percentages of the respondents of industrial, construction and transportation enterprises who answered that they "did not want to buy the stock of their own enterprise" (Type III + Type IV) and that they "did not want to buy the stocks of other companies" (Type II + Type IV), the author lists the result in Table 5-12. Indeed, the portion of the respondents who reported that they "bought the stock of their own enterprise but did not want to buy the stocks of other companies" (Type II) is much higher than those who reported that they "bought the stocks of other companies but did not want to buy the stock of my own enterprise" (Type III). In other words, about thirteen to sixteen percent of the respondents of privatized enterprises bought the stock of their own enterprise but did not want to buy any stock of other companies. They only cared about how to obtain the ownership of their own enterprise, but had no motivation to make an investment in other companies.

Table 5-12 Percentage of Non-participation in Privatization

Type	Dec. 1993 (%)	Apr. 1994 (%)
Type II + Type IV	41	54
Type III + Type IV	28	38
Type II – Type III	13	16

Note: The data in the table are the percentages of the respondents in industry, construction and transportation who replied "do not want to buy," selected from Table 5-10 and 5-11.

According to surveys in Czechoslovakia, technicians and skilled workers were more motivated in privatization; but unskilled workers were interested in privatization only if it was linked to job security, while many of them did not show much initiative or readiness to take part, and if got shares they often tried to sell them.[38] The situation in Russia was more or less similar. Among the five occupational groups (managers, technicians, skilled workers, unskilled workers and clerical workers), unskilled workers were most reluctant to participate in privatization. In this group, the percentage of those who answered "do not want to buy the stocks of their own enterprises" was 61 percent in March-April 1993 and 59 percent in April 1994 (see Table 5-10). Therefore, the vouchers distributed to them and their family members were more likely to be transferred into the hands of managers for cash. Behaving differently from the unskilled workers, about one fourth of the skilled workers in Russia not only bought the stocks of their own enterprises, but also bought those of other enterprises or investment funds (see Table 5-11).

From March to April of 1993, right after privatization was launched, among the interviewed Russian working people about one third bought stocks for up to 10,000 rubles (see Table 5-13). At the same time, one third of the working population did not want to buy more (see Table 5-14), among whom unskilled workers were more inclined to do so. Very likely, this portion of the respondents only used their own voucher with a face value of 10,000 rubles to buy stocks, without using the vouchers of their family members or spending any disposable income.

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[38] Daniel Vangham-Whitehead, "Workers Financial Participation in an East-West Comparative Perspective," a paper presented in Moscow International Symposium "The Man in the Socio-Economic System", 1992, Moscow, the Institute of Economics of the Russian Academy of Sciences, Aug. 13, 1992, 31.

Table 5-13 Stocks Already Bought

Amount	Mar-Apr. 1993	Occupation Groups		
		Manager (%)	Skilled Worker (%)	Unskilled Worker (%)
Up to 10,000 Rubles	32	17	42	65
10,000-30,000 Rubles	31	46	22	7
30,000-50,000 Rubles	19	17	28	7
50,000-100,000 Rubles	10	12	3	7
More than 100,000 rubles	1	0	0	0
Hard to answer	3	4	3	0
Did not answer	4	4	2	14
Total	100	100	100	100

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 57. Sample size = 1,999.

Table 5-14 Stocks to be Bought

Amount	Mar-Apr. 1993	Occupation Groups		
		Managers (%)	Skilled Worker (%)	Unskilled Worker (%)
Do not want to Buy more	36	24	39	57
Up to 10,000 Rubles	14	12	12	10
10,000-30,000 Rubles	13	15	14	6
30,000-50,000 Rubles	6	9	4	3
50,000-100,000 Rubles	3	7	2	1
More than 100,000 rubles	2	5	2	0
Hard to answer	24	27	25	22
Did not answer	2	1	2	1
Total	100	100	100	100

Note: The question is "Except what you have already held, in what amount would you buy stocks?"
Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 57. Sample size = 1,999.

On the other hand, another third of the respondents bought stocks for up to 30,000 rubles, with 46 percent of managers taking that option. Buck, et al. estimated that if each SOE employee contributed three free vouchers from their family entitlement, this would be sufficient, on average, to secure a majority employee holding in most privatized enterprises.[39] The respondents who bought stocks for up to 30,000 rubles more likely used the vouchers of their own and that of their family members (assuming three vouchers per family). And the rest of the 30 percent of the respondents who bought stocks valued more than 30,000 rubles would more likely be investors as they had to use cash to buy more stocks, and not necessarily those of their own enterprises. The percentage of respondents who bought the stocks of other companies gradually increased from seven percent in 1993 to 27 percent in 1994 (see Table 5-11). It could be said that about 30 percent of the working population not only took the defensive actions to buy stocks of their own enterprises (if their enterprises were being privatized), but also tried to invest in the stocks of other enterprises or investment funds.

4. Win or Lose? Self-Perceptions of Rank-and-File Employees in Privatizing Enterprises

After 55 to 60 percent of workers bought the stocks of their own enterprises, did ownership by the working collective become a reality? The VCIOM asked the question in its

[39] Trevor Buck, Igor Fliatotchev, and Mike Wright, "Employee Buyouts and the Transformation of Russian Industry," *Comparative Economic Studies*, Vol.36, No.2, summer 1994, 8-9.

surveys: “Who, in your opinion, owns or would really own the enterprise where you work after privatization?” Answers to the questions were quite surprising (see Table 5-15).

Table 5-15 New Owner of Privatized Enterprise

Type of New Owner-Controller	Mar-Apr. 1993 (%)	Sept. 1994 (%)
Working collective	15	12
By occupation group:		
Manager	22	23
Skilled labor	14	13
Current management	32	35
By occupation group:		
Manager	27	21
Skilled labor	34	38
Current director	19	31
By occupation group:		
Manager	11	33
Skilled labor	20	30
New owner from Russian entrepreneurs	3	4
Foreign entrepreneurs	0	0
Board of shareholders	6	5
By occupation group:		
Manager	11	14
Skilled labor	4	4
Other	0	0
Hard to answer	20	12
Did not answer	5	1
Total	100	100

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial’nae Peremenay: Monitoring Obshchestvennego Mneniia*, *Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 62, No.6, 1994, 70. Sample size: 1993 Mar.-Apr. survey, 1,827; 1994 Sept. survey, 1,700. The percentages include answers of the respondents whose enterprises had already been privatized or would be privatized.

In September 1994, only twelve percent of the respondents thought the new owner-controller of their privatized enterprise was the working collective, whereas about 66 percent of them perceived the “current management or directors” to be the owner. At the same time, only five percent of the respondents believed that the board of shareholders was the representative of the owners. This result and the data in Table 5-7 reveal a sharp difference between the owner-controller structure and that of the preferred structure, while 47 percent of the respondents would like to have the working collective to be the owner and only twelve percent considered the “current management and director” an acceptable owner.

Were employees disappointing or dissatisfied with the result of privatization? The VCIOM asked in its surveys three questions: 1. Do you think you personally win or lose from your company being privatized? 2. If you win from your company being privatized, what in particular would be your benefits? 3. If you lose from your company being privatized, what in particular would be your losses? Answers to the questions help us understand workers’ self-perceptions about the results of privatization.

From Table 5-16 one may find two trends in terms of the opinions of respondents. First, the percentage of self-perceived winners gradually decreased from 21 percent in March-April 1993 to fourteen percent in September 1994. Among different groups at the workplace, the percentage of managers who thought themselves winners remained quite stable, but the percentage of skilled workers declined dramatically. Second, the percentage of self-perceived losers increased from ten percent in March-April 1993 to sixteen percent in September 1994 correspondingly, and the percentage of those who felt that they “neither won nor lost”

increased from 26 percent to 50 percent significantly. The whole picture in September 1994 is that two thirds of the respondents either thought they did not win or lose or could not make a clear judgment. Clear winners and losers were a much smaller fraction.

Table 5-16 Perceptions about Privatization

Answers	Mar-Apr. 1993 (%)	Aug. 1993 (%)	Dec. 1993 (%)	Apr. 1994 (%)	Sept. 1994 (%)
"More Likely Won"	21	20	20	9	14
By occupation group:					
Manager	33	…	37	…	31
Skilled labor	21	…	18	…	9
"More Likely Lost"	10	12	17	20	16
By occupation group:					
Manager	7	…	19	…	12
Skilled Labor	13	…	18	…	17
"Neither Won nor Lost"	26	42	36	45	50
By occupation group:					
Managers	23	…	30	…	46
Skilled labor	21	…	37	…	53
"Hard to answer"	38	26	25	24	19
Did not answer	5	…	2	2	1
Total	100	100	100	100	100

Note: The question is: "Do you think you personally win or lose from your company being privatized?"
Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 62, No.2, 1994, 77, No.4, 1994, 64, and No.6, 1994, 79. Sample size: The 1993 Mar.-Apr. survey, 1,818; the 1993 Aug. survey, 1,805; the 1993 Dec. survey, 1,799; the 1994 Apr. survey, 1,831; the 1994 Sept. survey, 1,700. The percentages include answers of the respondents whose enterprises had already been privatized or would be privatized.

Table 5-17 Perceptions of Winners in Privatization

Answers	Mar-Apr. 1993 (%)	Aug. 1993 (%)	Dec. 1993 (%)	Apr. 1994 (%)	Sept. 1994 (%)
"My position at the enterprise become more stable"	31	32	38	32	24
Manager	75	…	38	…	26
Skilled labor	24	…	38	…	25
Unskilled labor	33	…	54	…	0
Technician	32	…	42	…	30
Clerical worker	31	…	18	…	25
"I began earning more"	77	69	59	47	57
Manager	25	…	63	…	61
Skilled labor	85	…	59	…	37
Unskilled labor	89	…	46	…	100
Technician	68	…	58	…	32
Clerical worker	85	…	73	…	86
"Working conditions changed for better"	15	21	10	15	22
Manager	17	…	19	…	28
Skilled labor	22	…	14	…	53
"Possibilities of better working appeared"	22	15	19	5	22
Manager	17	…	0	…	25
Skilled labor	22	…	25	…	31
Technician	11	…	16	…	36
"Psychological climate in the collective became better"	10	3	11	14	6
Manager	17	…	19	…	7
Skilled Worker	11	…	9	…	8
"Hard to answer"	1	5	2	6	4

Note: The question is: "If you win from your company being privatized, what in particular would be your benefits?"

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 62, No.2, 1994, 77, No.4, 1994, 64, and No.6, 1994, 79. Sample size: The 1993 Mar.-Apr. survey, 1,818; the 1993 Aug. survey, 1,805; the 1993 Dec. survey, 1,799; the 1994 Apr. survey, 1,831; the 1994 Sept. survey, 1,700. The percentages include answers of the respondents whose enterprises had already been privatized or would be privatized.

Table 5-18 Perceptions of Losers in Privatization

Answers	Mar-Apr. 1993 (%)	Aug. 1993 (%)	Dec. 1993 (%)	Apr. 1994 (%)	Sept.1994 (%)
"Danger of losing job increased"	41	48	72	45	54
By occupation group:					
Manager	75	…	25	…	78
Skilled labor	24	…	74	…	53
Unskilled labor	33	…	100	…	77
Technician	32	…	63	…	30
Clerical worker	31	…	57	…	60
"My wages were cut"	33	34	39	59	46
By occupation group:					
Manager	25	…	13	…	35
Skilled labor	85	…	38	…	61
Unskilled labor	89	…	31	…	14
Technician	68	…	50	…	52
Clerical worker	85	…	57	…	2
"Now I have to work much more intensively"	8	16	2	5	5
By occupation group:					
Manager	17	…	0	…	0
Skilled labor	22	…	3	…	2
Unskilled labor	0	…	0	…	0
"Psychological climate in the collective changed for the worse"	16	21	24	32	29
By occupation groups:					
Manager	17	…	50	…	39
Skilled labor	11	…	28	…	25
Unskilled labor	…	…	0	…	4
Clerical worker	…	…	14	…	48
"Hard to answer"	29	8	2	3	4

Note: The question is: "If you lose from your company being privatized, what in particular would be your detriments?"

Source: The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, 62, No.2, 1994, 78, No.4, 1994, 64, and No.6, 1994, 79. Sample size: The 1993 Mar.-Apr. survey, 1,818; the 1993 Aug. survey, 1,805; the 1993 Dec. survey, 1,799; the 1994 Apr. survey, 1,831; the 1994 Sept. survey, 1,700. The percentages include answers of the respondents whose enterprises had already been privatized or would be privatized.

If one further reads the data about self-perception of winners and losers, the picture becomes more confusing. Among the winners, 57 to 77 percent reported their wages increased, 24 to 38 percent said their positions at workplace were more stable, and 15 to 22 percent said their working conditions improved (see Table 5-17). Further analysis about the wage increases indicates that higher earnings were more likely to be offered to unskilled workers, clerical workers and managers, rather than to technicians and skilled workers. Moreover, while a high percentage of technicians and skilled workers reported that their wage increased in March-April, 1993, the percentage drastically dropped over the next eighteen months. Why did managers of privatized enterprises raise wages for the majority of employees in the early months of privatization, but later only for unskilled and clerical workers? It is possible that managers tried to favor all employees at the early stage of privatization to encourage them to support insider privatization; and later, once it was realized, the managers began to obtain shares from employee-owners, particularly from clerical and unskilled workers who were more likely to sell their shares, by raising their wages in exchange.

Among the respondents who perceived themselves as losers, the top concern was “the danger of losing my job increased”, as 41 to 71 percent of them reported; the second concern was wage cuts, and the third being that the “psychological climate in the working collective changed for the worse” (see Table 5-18).

The above discussion focuses on workers’ perceptions and reactions to privatization. Summarizing my findings, I would like to point out here: first, worker really worried about job security, and a lot of them did believe that the working collective was supposed to be the new

owner-controller of the privatized enterprise – they thus supported the privatization scheme in confusion and with hesitation; second, a large portion of them obtained the stocks of their own enterprises with vouchers and implemented an insider privatization as allies of their managers against outside investors. Another key player of the privatization was SOE managers. The next section further explores the attitudes and actions of managers.

5. Managers' Attitudes and Strategies in the Voucher Privatization

SOE Managers were part of the *nomenklatura* and an influential social group in Post-Soviet Russia. During the transition years, they had strong incentives to retain their social status and power, and saw the maintenance of prestige and financial status as part of individual survival. Since their positions would no longer rely on governmental appointment, they had to rebuild their power by a new arrangement through the privatization of their enterprises. Otherwise, their social capital alone would not be sufficient to consolidate power. Many scholars have shown how SOE managers were involved in spontaneous privatization before 1992, how they lobbied the Supreme Soviet for a favorable version of the privatization program, and how they made themselves the winners in privatization. In 1991, Johnson and Kroll found that some managers created new holding companies or small enterprises as conscious strategies for restructuring transactions with other enterprises as many SOEs in Kiev were cut off from their traditional material and product networks in other former Soviet republics; Johnson and

Kroll wrote that their "acquisition of property does involve an element of theft."[40] Leonid Khotin, a sociologist who studied red directors since 1981, pointed out that "since privatization began in 1992, many state enterprise directors have openly become the main shareholders of privatized enterprises and their numbers are growing."[41] The opinions of the rank-and-file employees of privatized enterprises about the results of privatization have confirmed Khontin's observation (see Table 5-15). Blasi, Kroumova and Kruse also mentioned: "Though the top managers publicly proclaimed their support for employee ownership, in interviews held out of the public view in 1992 and 1993, they repeatedly voiced the opinion that they should control the enterprises and own a large amount of the stock. For many managers, employee ownership was a cover for pursuit of their own interests."[42] It is no doubt that the managers had greatly influenced the privatization process in Russia. Cook and Gimpelson pointed out: "The managers had positional resources; they controlled flows of information, had strong formal and informal influence on workers, and were usually backed by local authorities as well. It was management who usually initiated the privatization process and 'taught' the workers how to vote and how to make use of their shares."[43]

What were the attitudes of Russian SOE managers towards privatization and what strategy did they adopt to retain power? Were Russian managers able to do whatever they liked by

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[40] Simon Johnson, and Heidi, Kroll, "Managerial Strategies for Spontaneous Privatization," *Soviet Economy*, Vol.7, No.4, 1991, 281-316.

[41] Leonid Khotin, "Old and New Entrepreneurs in Today's Russia," *Problems of Post-Communism*, Jan./Feb. 1996, 50.

[42] Joseph Blasi, et al. *Kremlin Capitalism: The Privatization of the Russian Economy*, 36.

[43] Linda J. Cook, and Vladimir E. Gimpelson, "Exit and Voice in Russian Managers' Privatization Strategies," *Communist Economics & Economic Transformation*, Vol.7, No.4, 1995, 473.

manipulating privatization for their own interests? This section will discuss these issues.

5.1 Managers' Fears

If Russian SOE managers were indeed in quite a strong position and could dominate the privatization process for their own interests, they presumably would have been quite confident about the stability of their positions or jobs. But that was not the case. Actually, the majority of managers worried very much about losing their jobs during privatization. Table 5-1 shows that, in 1993 when the voucher privatization program was implemented, the percentage of managers who worried about job security increased from 79 percent in March-April to 92 percent in December (see Table 5-3). Among all five occupational groups at the workplace, the managers worried most about their jobs, even more than unskilled laborers. The percentages reflect the general feelings of Russian managers in a society where mandatory privatization was being pushed forward. In reality, the real threat of losing their jobs at their own workplaces was not so large-only about one third of the managers reported that fear when answering the question "do you think you personally could lose job in the near future?"

The widespread fear by Russian managers suggests that they encountered great uncertainty during privatization. In the Soviet Union, managers were selected and appointed by the party-state as agents of the state, and their authority was imposed from above on SOEs and legitimized by the party-state. However, the collapse of communist rule turned a lot of things upside-down, including the disappearance of the foundation of authority. As the appointment principal no longer existed, managers suddenly lost their legitimacy and became just employees

of SOEs like other rank-and-file workers without any legal support for their leadership or authority at the workplace. They were thus left in a very strange status: their boss, the party-state, was removed forever, and they stayed at the leadership positions simply because they were there before, or their authority was recognized by the rank-and-file workers based on the homo sovieticus (the habits of adaptation mechanisms in the Soviet era)[44] which itself was diminishing. Logically, they might get rid of this fragile status by declaring themselves the new bosses of their enterprise, as some did earlier through various methods. However, such an attempt was blocked by the voucher privatization program, and was not socially acceptable as long as the anti-*nomenklatura* atmosphere remained popular. Moreover, the privatization scheme provided workers a kind of power by letting workers approve the privatization plan of their own enterprise. "The workers' power derived from *de facto* veto rights over the privatization process. If during this process a labor-management conflict occurred, not only would privatization be halted, but dismissal or resignation of top managers was probable."[45] Unlike workers, if a manager was removed from his current position, he could hardly find a similar job in another privatized enterprise, since everywhere the Soviet type managers filled these. From here one may find the very nature of the huge uncertainty Russian managers then encountered, and thus the source of worry about their jobs. In other words, the managers had more fears than the rank-and-file workers: beside the popular panic due to the worsening economic situation during the transition

[44] Andrzej W. Tymowski, "The Roots of Counter-Reform: Bad Habits or Social Justice?" *Problems of Post-Communism*, May-June 1996, 3-10.

[45] Linda J. Cook, and Vladimir E. Gimpelson, "Exit and Voice in Russian Managers' Privatization Strategies," 473.

period, managers worried about the attenuated basis of their authority and the legal vacuum they were operating in.

Attitudes of Russian managers towards privatization were diverse. In an interview by Nelson and Kuzes, Dmitrii Vasilev, the deputy chairman of *GKI* (the State Property Committee) pointed out that the directors' corps had the most complicated assortment of motives among all of those whose interests were affected by privatization, while one group of directors wanted to become the *de facto* owners of their enterprises, another group feared negative effects from losing state patronage and Central Bank credits; some of them favored ownership among workers' collectives, and others anticipated benefits from outside investment.[46] His brief description does not provide a detailed picture, but the VCIOM surveys do. In answering "do you think your enterprise needs to be privatized" in March-April of 1993, only 26 percent of managers responded with "Yes", whereas 41 percent answered "No" and 21 percent said "I'm opposed to privatization in principle" (see Table 5-6). Obviously, at the early stage of the voucher privatization, about two thirds of managers did not want privatization to take place. The percentage was twice as high as that of any other occupational groups at the workplace. Therefore, it could be said that managers were actually the group at the workplace with the strongest opposition to privatization at its beginning stage. Although almost no one has mentioned it in discussions about the Russian voucher privatization, the fact is very important for understanding the path of the privatization process.

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[46] Lynn Nelson, and Irina Kuzes, "Coordinating the Russian Privatization Program," *RFE/RL Research Report*, Vol.3, No.20, May 20, 1994, 17.

Once privatization turned out to be inevitable, did managers believe that they could claim themselves the positions as new dominant owners of their privatizing enterprises? Nelson and Kuzes interviewed directors in 164 enterprises in 1993. When they asked the directors, "of the following proposals, which one do you think has the most merit?" only seven percent of the directors chose "privatization through voucher auction," 42 percent favored "privatization by turning ownership over to the personnel in an enterprise," and sixteen percent preferred "selling shares of enterprises to anyone who wants to buy them." Their findings suggest that the "directors wanted enterprise personnel either to own their enterprises….. or to be able to sell shares to acquire needed capital. What they opposed was…… a giveaway of shares, at no cost, to new outside owners."[47] Cook and Gimpelson further explained that, confronted with the threat of losing control over their enterprises to new owners who might replace them, the managers tried to preserve their positions, but "straightforward claims of managers' rights would have been politically inadvisable and isolating, given the pervasive charges of '*nomenklatura* privatization' and attendant concerns about violations of social justice."[48] The VCIOM nationwide surveys of employees of the privatized or privatizing enterprises asked the question: "Who would you like to see in control of your company after its privatization?" In March-April 1993, only nineteen percent of managers responded that they would like to see the current management or directors be the new owner, and 24 percent answered that they would

[47] Lynn D. Nelson, and Irina Y. Kuzes, *Radical Reform in Yeltsin's Russia: Political, Economic, and Social Dimensions*, 150-151.

[48] Linda J. Cook, and Vladimir E. Gimpelson, "Exit and Voice in Russian Managers' Privatization Strategies," 468.

like to see the board of shareholders be the new controller, but 43 percent replied that they would like to see the working collective be the new owner (see Table 5-7). The data suggest that, although the managers did want to obtain control over their enterprise, the majority of them dared not openly admit it; instead, they had to agree that either the working collective or the board of shareholders was supposed to be the new controller. Given that most managers did not want their enterprise to be privatized, this attitude implies that, whether they liked it nor not, they knew that they could lose their position as the real controllers of the enterprise, if they lost the support of the workers.

5.2 Allying with Workers: the Survival Strategy of the Managers

How did the Russian SOE managers defend their own interest in a rapidly changing organizational environment? Struggling for individual survival, the managers adopted a strategy to work together with the rank-and-file workers under the banner of the interests of the working collective as allies against a possible outsiders' takeover; the process looked like the "directors have made all major decisions about the method of privatization chosen; workers then ratified there decisions."[49] Two things that have often been taken for granted in the literature about Russian privatization should be verified here. First, without democratization the managers would not have experienced the legal vacuum and authority crisis and have to seek workers' support for their own survival. Second, the voucher privatization program, particularly Option 2, had not only offered the

[49] Michael McFaul, "Agency Problems in the Privatization of Large Enterprises in Russia," in Michael McFaul, and Tova Perlmutter, eds., *Privatization, Conversion, and Enterprise Reform in Russia*, Boulder, CO, Westview Press, 1995, 45.

workers decisive power to select the new ownership structure, but also changed the balance of the relationship between managers and workers, at least during the privatization period, as the privatization scheme prevented managers from gaining a core stake without the approval of employees and the workers could use their vouchers to vote. This change in the relationship made the managers vulnerable if they did not stand together with their workers.

Both Russian SOE managers and workers did not want outside investors to get control over their workplace, and workers' mistrust of outsiders was much stronger than their mistrust of their own managers,[50] therefore an alliance between the managers and outside investors, which was often found in China, turned out to be much less possible in Russia, and insider privatization became the choice of both parties in the Russian workplace. According to the VCIOM data, when voucher privatization finished in September 1994, only 0.4 percent of respondents of privatized enterprises reported that foreign entrepreneurs became the new owner of their enterprises, and four percent reported outside Russian entrepreneurs as the new owners (see Table 5-15).

As Cook and Gimpelson described, in accord with Option 2 of the privatization program, in order to maintain control over their enterprises in the privatization process, managers had to gain the cooperation and consensus of the bulk of their workforce; otherwise, if conflicts developed, workers could, in principle, set up commissions without management; and, if the workforce could not reach a decision within the established time-frame, the GKI could impose Option 1 by default. Therefore, workers did have the potential to disrupt the privatization

[50] Linda J. Cook, and Vladimir E. Gimpelson, "Exit and Voice in Russian Managers' Privatization Strategies," 474.

process and trigger state interventions that would be detrimental to managers' control, and the managers had strong incentives to minimize conflict.[51] The mutual dependence of managers and workers in the strategic alliance for privatization was an informal one, more like a consensus between the two parties. Their common interests led them to work together, in order to guarantee the safety of their enterprise from takeovers by outsiders. In a survey about the privatization process done in 27 enterprises in March 1993, Ash and Hare heard from interviewees an interpretation presented by managers of a factory on behalf of workers and using the words of workers: "We own the state, the state owns the business; therefore we own the business. If we have to privatize then we will buy the business to stop anyone else doing so, even though we are being asked to buy something we already own."[52]

After the voucher privatization was launched, "managers often encouraged their workers to select the worker-buyout option to block new outside owners," but "the adoption of the worker-buyout model was not a result of pressure from organized labor."[53] Instead, it was the result of the collective actions of the majority of SOE insiders based on a consensus. The cooperation between the managers and workers during the voucher privatization process increased the confidence of managers regarding their future. Evidence of the successful cooperation is the changing attitudes of the managers towards the voucher privatization. Interestingly, the percentage of managers who thought their enterprises should be privatized

[51] Ibid, 469-470.

[52] Timothy N. Ash, and Paul G. Hare, "Privatization in the Russian Federation: Changing Enterprise Behavior in the Transition Period," 629.

[53] Penny Morvant, and Peter Rutland, "Russian Workers Face the Market," 9.

increased dramatically from 26 percent in March-April 1993 to 60 percent in December the same year (see Table 5-6). At the beginning of the voucher privatization, managers were somehow a little hesitant to buy the stocks of their own enterprise. According to the VCIOM data, in March-April 1993, the percentage of the managers who reported they had "already bought the stocks of their own enterprise" was only 21 percent, even lower than that of skilled workers, whereas those managers who "may buy the stocks of their own enterprise" reached 49 percent, and those who "do not want to buy" was 31 percent; nine months later, the percentage of managers who had "already bought the stocks of their own enterprise" increased to 53 percent, much faster than any other groups at the workplace, and those who "may buy the stocks of their own enterprise" decreased to 22 percent, while those who "don't want to buy the stocks of other companies" increased from 22 percent to 39 percent (see Table 5-11 and 5-12). The changing attitudes of the managers towards privatization implied that they quickly learned how to make it more favorable to themselves.

The alliance of the managers and workers simply blocked outsiders from taking over. The alliance not only used vouchers to obtain the shares of their own enterprises, but also tried to buy more from voucher auctions. Observing five voucher auctions in Yaroslavl district, two scholars noticed that workers and managers bought on average 80 percent of the stocks put up for sale.[54]

[54] Bozidar Djelic, and Natalia Tsukanova, "Voucher Auctions: A Crucial Step toward Privatization," *RFE/RL Research Report*, July 23, 1993, 10-18.

5.3 Moving toward Managerial Privatization

Managers would be in a weak position if they could not obtain controlling shares from their workers. Therefore, when the Russian government declared that voucher privatization was ended in mid-1994, transactions in shares kept proceeding within enterprises, and more and more shares flew from the workers to their managers. Blasi, et al found from their investigations that the top managers "wanted eventually half the firm to be held by managers, with a large chunk of ownership for the general directors personally and a significant amount for other top managers."[55] A lot of methods were employed to acquire additional shares for the managers. Some managers simply bought workers' shares, with either revolving funds of the enterprises or loans from commercial banks; at the same time, they tried to prevent the workers from selling shares to outsiders. "Those who resisted were threatened with dismissal. Managers held tight to company registers and simply refused to record share transactions of which they disapproved. They bought up still more shares at public voucher auctions (which could be made less public if the managers had the sympathy of local Property Fund officials in changing of running the auctions)."[56] Many managers also appealed to local governments to restrain large investors[57] so they could maintain control over their enterprises. As only about one third of the privatized enterprises were able to pay dividends under a severe economic recession after the disintegration of the Soviet Union, many

[55] Joseph R. Blasi, et al, *Kremlin Capitalism: The Privatization of the Russian Economy*, 64.

[56] Roman Frydman, Kenneth Murphy, and Andrzej Rapaczynski, "Capitalism with a Comrade's Face," *Transition*, Jan. 26, 1996, 8.

[57] Andrei Shleifer, and Dmitry Vasiliev, "Management Ownership and Russian Privatization," in Roman Frydman, Cheryl W. Gray, and Andrzej Rapaczynski, eds., *Corporate Governance in Central Europe and Russia: Vol.2, Insiders and the State*, 74.

workers lacked incentives to keep shares; but the shares were also of only very low liquidity on the emerging stock market, therefore those workers who wanted to sell their shares found that the easiest way was to sell to their managers.[58]

Table 5-19 Change of Ownership Structure of a Factory

Shareholder	1992 (%)	1995 (%)
Managers	4	20
Rank-and-file workers	38	53
Pensioners of the factory	12	19
Funds of the factory	10	8
Outside pension funds	36	0
Total	100	100

Source: The data was provided by Mrs. Cyntsova, the CEO of the *Pervo Mayskaya Zarya* (The First May Dawn) in Saint Petersburg.

In the summer of 1995 the author interviewed Mrs. Galina G. Sintsova, the general director (CEO) of a joint-stock garment company, *Pervo Mayskaya Zarya* (The First May Dawn), in Saint Petersburg, which was founded in 1926, privatized in 1992 and had cooperation in 1995 with French, Swiss and German firms. The medium-size SOE chose Option 2 for privatization. The ownership composition of the company showed that in 1992 when the company was just privatized, 36 percent of its shares were bought by outside pension funds in auctions, and rest of them were in the hands of insiders, including the rank-and-file workers, managers, pensioners of the company

[58] Linda J. Cook, and Vladimir E. Gimpelson, "Exit and Voice in Russian Managers' Privatization Strategies," 474.

and a fund of the company. A feature of the privatization in this company was that the managers mobilized the pensioners retired from the company[59] to buy the stocks and established a special fund to buy the shares as well. Pensioners' support for such an idea may have been due to trust in their former workplace based upon the paternalistic culture of the Soviet era. Although the company is located in the second largest city of Russia rather than in an isolated industrial town, and the pensioners don't have to live completely upon the facilities provided by the company, they still have a lot of connections with its previous workplace years after retirement. In Russia, pensioners could be recruited as insiders, and many of the pensioners see themselves as family members of their previous workplace. The designers of the Russian privatization and its Western commentators have ignored the possibility that such outsiders could be turned into insiders for an insider privatization. Three years later, in 1995, all the shares held by the outside pension funds were bought back by the managers, workers and pensioners. As a result, the joint-stock company became a 100 percent insider-held firm, while managers controlled 20 percent of the shares (see Table 5-19). This is a typical case of how a medium-size SOE was internally privatized within the existing legal framework.

Although in many privatized enterprises, the proportion of shares held by the rank-and-file workers is much larger than that held by their managers, rarely has workers' self-management been adopted. A Russian scholar of labor relations explains that, after the

[59] According to the regulations on privatization in Russia, pensioners who had worked in the privatized enterprise for certain years could also participate in the privatization of their former workplace. Samala Research Group, "Two Military-Industrial Giants," in Simon Clarke, ed. *The Russian Enterprise in Transition: Case Studies*, UK, Edward Elgar, 1996, 280.

managers transferred the SOEs to the work collectives, as large work collectives cannot effectively manage enterprises and organize production, this opens the way for full control over the enterprise by a small group of particularly active people, usually representatives of the management. The further reorganization of the cooperative (or JSC) leads to the concentration of the controlling shares in a few hands.[60] He mentions that "many former state enterprise directors have retained control over the property they used to manage by converting it into their own private property."[61]

5.4 Managers' Self-Perceptions of Privatization

Can we assume that most of the managers are the winners? Indeed, a significantly larger portion of the managers, 33 percent in March-April 1993, 37 percent in December 1993 and 31 percent in September 1994, saw themselves as the winners (see Table 5-16). However, an even larger portion of the managers thought they neither won nor lost. This portion was only 23 percent in March-April 1993 when privatization started, but gradually increased to 46 percent in September 1994 when it ended. And a small portion, sixteen percent of them, thought they were losers in the process.

How did managers evaluate their personal status, as winners or losers, in the privatization? Among those who believed themselves to be winners, in September 1994, 61 percent thought they "began earning more," 28 percent reported that "working conditions

[60] Vladimir Gimpelson, "Russia's New Independent Entrepreneurs," *RFE/RL Research Report*, Vol.2, No.36, Sept. 10, 1993, 47.
[61] Ibid, 46.

changed for better," 26 percent believed "my position at the enterprise become more stable," and 25 percent said "possibilities of better working appeared" (see Table 5-17). Apparently, the first thing managers did after privatization was to raise their own wages. In contrast to the winners, among those who believed themselves to be losers, some worried that the "danger of losing my job increased," some reported that the "psychological climate in the working collective changed for the worse," and others said "my wages were cut" (see Table 5-18). Job security, increasing tension at the workplace, and reduced earnings, were the three main concerns of the losers.

Given that many managers made efforts to obtain more stocks of their privatized enterprises, but only 26 percent of the self-perceived winners believed that their positions at the privatized enterprise became more stable, and the majority of the self-perceived losers reported their positions weakened after the privatization, what was the real ownership composition of the privatized enterprises from the view of management? According to Table 5-15, the percentage of the manager respondents reporting that the current director became the real owner through the privatization increased from eleven percent in March-April 1993 to 33 percent in September 1994, and that of the manager respondents saying that the current management team became the real owner changed from 27 percent to 21 percent. Therefore, it could be seen that from early 1993 to late 1994 managerial ownership increased significantly, from 38 percent to 54 percent. It thus confirmed that managerial privatization did take place. Very likely, the self-perceived winners belong to this group which successfully obtained controlling shares of their own enterprises. At the same time, about one fifth of manager

respondents reported that the working collective was the real owner of the privatized enterprises, and this percentage remained relatively stable from 1993 to 1994. And another ten to fourteen percent of the manager respondents said the real owner was the board of shareholders. Finally, the percentages of the manager respondents who reported that the real owner was new Russian entrepreneurs or foreign entrepreneurs were too small to be taken into consideration.

I would briefly summarize the ownership composition of the privatized enterprises: when voucher privatization came to its end, at least about half of the mangers had obtained dominant ownership at their privatized enterprises, but still a lot of managers were unable to win this way and the nominal owner-controller of their enterprises was the working collective. This picture could be observed from a more direct way by reading the statistics of the ownership structure of the privatized enterprises which is discussed in the next section.

6. The Results of the Privatization in Russia

Under the voucher privatization program, by July 1, 1993, 98 percent of the issued vouchers had been used, 550 investment funds were formed and purchased about 25 percent of the vouchers;[62] but most enterprises were owned by workers and managers through selecting Option 2. As of February 1994, 620 such funds were created, attracting 60 million vouchers; however, within a few months about half of the funds collapsed, ultimately the voucher funds only

[62] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, 88.

controlled about three percent of the shares of the privatized enterprises. The voucher privatization went on for about eighteen months, and was formally ended on July 1, 1994. At the end of 1993, 8,509 mid-sized and large enterprises were privatized,[63] and by July 1994, almost 15,000 enterprises out of 19,000 eligible for the program had been privatized. According to the earlier statistics, about two thirds of the privatized enterprises had chosen Option 2, one third had chosen Option 1, and only one percent selected Option 3.[64] Later, it was reported that about 80 percent of the privatized enterprises selected Option 2.[65]

As most factories of raw materials, electrical-generation, telecommunications and the military industry remained in the hands of the state, before the voucher privatization was completed, Yeltsin issued a decree for the second stage of Russia's privatization on December 24, 1993. On April 7, 1994, the Russian government adopted the post-voucher privatization policies which allowed enterprises to sell their remaining shares for cash or investment guarantees, in hoping that core investors, such as financial-industrial groups, would take control of the larger firms with high value through buying shares for cash and investment tenders.

The second stage of privatization was launched in July 1994. Because the enterprises to be privatized at this stage were usually quite large and the state often held some portion of ownership, insiders could hardly gain control over the enterprises with their vouchers and outside institutional investors stepped in. The Russian government expected that it could collect some revenue through

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[63] Joseph R. Blasi, et al, *Kremlin Capitalism: The Privatization of the Russian Economy*, xviii.

[64] Linda J. Cook, and Vladimir E. Gimpelson, "Exit and Voice in Russian Managers' Privatization Strategies," 472-473.

[65] Victor Supyan, "Privatization in Russia: Preliminary Results and Socioeconomic Implications," 5.

selling the shares of the large SOEs to private institutional investors, so its budget deficit might be reduced.

Most private banks in Russia were then under the control of former *nomenklatura* members, many of whom were former factory managers and former senior members of *nomenklatura* and were close to Kremlin headed by Yeltsin.[66] Several such financial oligarchs lent money to the Russian government, and asked in exchange that the government put up collateral for the loans in the form of the shares of large SOEs.[67] The arrangement was called "loans for shares." But, when the shares were auctioned, "by holding the auction in remote locations, closing the airport on the day of the auction, or specifying terms that only the auctioneer himself could meet,"[68] government officials and the oligarchs manipulated the auctions. As a result, "the auction rarely generated more than a few dollars above the original offering price;" and the winner of the auctions were usually the affiliates of the banks that held the auctions.[69] Sometimes, the oligarchs even worked together with local governments to initiate some trumped-up criminal charges against the enterprises they wanted, frozen the bank accounts of the enterprises, then bought up the debt of the enterprises, demanded the right to install new management and took over control.[70]

Ultimately, according to Goldman, the Russian government collected only about $6 billion as revenues from privatizing the large SOEs, while the voucher privatization generated very little

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[66] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, 103.
[67] Ibid, 3-4.
[68] Ibid, 4-5.
[69] According to Goldman, until March 1997 the biggest beneficiary in most of the auctions is Oneximbank, a private bank founded by Vladimir Potanin who once served as the First Deputy Prime Minister. Ibid.
[70] Ibid, 34-35.

revenue for the government; "two-thirds of the country's companies were given away or seized at prices far below their market value."[71]

Unlike in the first stage privatization when asset stripping were eventually done by insider managers through buying shares from employee or outsider shareholder with the fund or loans of the enterprises, in the second stage of the privatization of large SOEs it was the holding investment companies established by the oligarchs or similar people that acquired shares and gained control of the privatized large enterprises, many of which possessed the most valuable raw materials in Russia.[72] The scale of asset stripping at each enterprise during the second stage privatization was much greater than that in the voucher privatization period, and the approaches of asset stripping involved more collaboration between government officials and the oligarchs.

At the end of 1995, 75 percent of the total mid-sized and large industrial enterprises (17,937[73]) were privatized. As of 1999, the government only maintained 100 percent ownership in 382 companies, over 50 percent in 470, 25 to 50 percent in 1,601, and less than 25 percent in 863.[74] So, in 1999 altogether only in 3,316 companies did the Russian government still hold certain portion of ownership, while all other enterprises were privatized.

There have been a number of studies on the composition of ownership of privatized enterprises. One such survey reported: "When voucher-based privatization ended, half of the enterprises had no outside shareholders at all and two-thirds of them had no outside shareholders

[71] Ibid, 93.
[72] Ibid, 1-2.
[73] Joseph R. Blasi, et al, *Kremlin Capitalism: The Privatization of the Russian Economy*, xvi-xix.
[74] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, 95.

on their boards of directors."[75] Nelson and Kuzes reported the results of their 1993 survey: among 164 privatized enterprises, insiders owned at least 50 percent of the shares, and in 85 of the enterprises insiders owned 100 percent of the shares.[76] The largest and most representative survey was conducted by the World Bank in July 1994 at the close of the voucher privatization. It showed a clear dominance of insider ownership at 56 percent of all shares, while outsiders had 23 percent and the state had 20 percent.[77]

Would the insiders' dominant ownership of Russian enterprises gradually shrink? After the second stage (or money stage) of privatization, a survey conducted by Blasi, Kroumova and Kruse found insiders' ownership declined seven percent from 1994 to 1996, from 65 percent to 58 percent, of which managers owned eighteen percent of their firms and the rank-and-file workers as a group owned 40 percent; but the ownership of outsiders was found smaller (32 percent) in the survey. The three authors pointed out that, while the insider's portion decreased, the number of companies with big concentrated stakes (20 to 40 percent) by managers grew substantially between 1995 and 1996, as many managers admitted that their companies bought back shares from outsiders; thus, in 1996, top managers owned more than 30 percent of five percent of all Russian companies and more than 23 percent of ten percent of all Russian companies.[78] An official study by the Russian Federal Securities Committee reported a similar observation that 65

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[75] *Segodnia* (Today), Moscow, Russia, Feb. 18, 1995, 3.

[76] Lynn D. Nelson, and Irina Y. Kuzes, *Radical Reform in Yeltsin's Russia: Political, Economic, and Social Dimensions*, 237.

[77] John S. Earle, "Privatization in Russia Offers Lessons for Others," Washington, DC, Center for International Private Enterprise, *Economic Reform Today*, No.2, 1999, 42.

[78] Joseph R. Blasi, et al, *Kremlin Capitalism: The Privatization of the Russian Economy*, 54-56.

percent of Russian companies were owned by the insiders in 1996.[79] Comparing several survey results, Sprenger reported that from 1995 to 1999, the percentages of the shares held by banks, investment funds, foreigners, non-financial firms and holdings/investment companies had changed slightly; the percentage of managers' shares remained relatively stable between fourteen and eighteen; the only obvious change of the ownership structure was that the percentage of workers' shares declined from 46 percent in 1995-1996 to 32 to 35 percent in 1999-2000, at the same time, the percentage of outsider individuals increased from six in 1995-1996 to nineteen in 1999.[80] Among the surveys conducted by Russian researchers after 1996,[81] a survey of 530 large- and medium size industrial firms in twenty regions found that the shares of the state declined nine percent from 1994 to 1999, and the shares of workers also decreased by six percent; at the same time, the shares of managers increased three percent, the portion held by outside individuals increased four percent, and that by legal entities increased

[79] *Financial Times*, Sept. 6, 1996, 10.

[80] Carsten Sprenger, "Ownership and Corporate Governance in Russian Industry: A Survey," London, UK, European Bank for Reconstruction and Development, *Working Paper*, No.70, Jan. 2002, 4.

[81] For instance, Sergiy Biletsky, David Brown, John Earle, Julia Khaleeva, Ivan Komorov, Olga Lazareva, Klara Sabirianova, and Carsten Sprenger mentioned a survey of 530 industrial firms in 20 regions in their 2001 mimeo "Inside the Transforming Firm," and the Center for Economic and Financial Research (CEFIR) in Russia and the Institute for the Economy in Transition (IET) conducted surveys of several hundred large- and medium size companies, and drafted an unpublished paper "A Survey of Corporate Governance in Russian Companies in 2005 and 2006." IET was originally the Institute for Economic Policy of the Academy of National Economy and the Academy of Sciences of the USSR established in 1990 by Yegor Gaidar and was renamed as the Institute for the Economy in Transition in 1992. The reports of the surveys were not published. See Olga Lazareva, Andrei Rachinsky, and Sergey Stepanov, "A Survey of Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, New York, NY, Springer, 2008, 317-318.

seven percent.[82] Other surveys in several hundred large- and medium-size firms found that from 2002 to 2006 the average portion of the shares held by management increased three percent, while the portion in the hands of the largest outside blockholders increased eleven percent.[83]

Obviously, the money stage of privatization increased the proportion of large outside shareholders, but the insider dominance remained unshaken. After privatization, subsequent ownership redistribution in Russia led to a decline in workers' ownership, as managers and outsiders bought employee shares,[84] and a slight increase of the shares held by managers. Lazareva et al. pointed out: "Russian assets have ended up in the hands of a small group of people… about 40% of the Russian industry belong to 22 largest business groups, controlled by 'oligarchs.'"[85]

Russia's voucher privatization was designed to meet the interests of all members of society and create millions of individual owners. The priority of survival for both workers and managers in most small and medium SOEs led them to work together in an alliance against

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[82] The data was cited by Olga Lazareva et al. from a mimeo titled "Inside the Transforming Firm," written by Sergiy Biletsky, David Brown, John Earle, Julia Khaleeva, Ivan Komorov, Olga Lazareva, Klara Sabirianova, and Carsten Sprenger. See Olga Lazareva, Andrei Rachinsky, and Sergey Stepanov, "A Survey of Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, 318.

[83] The data was cited by Olga Lazareva et al. from "Ownership Concentration in Russian Industry" (Sergei Guriev, and Andrei Rachinsky, *CEFIR Working Paper*, No.45, 2004) and "Survey of Corporate Governance in Russian Companies in 2005 and 2006" of the CEFIR and IEF (unpublished). The target samples of the surveys were very similar. See Olga Lazareva, Andrei Rachinsky, and Sergey Stepanov, "A Survey of Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, 318.

[84] Taraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, 226-227.

[85] Olga Lazareva, Andrei Rachinsky, and Sergey Stepanov, "A Survey of Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, 317-318.

outside investors, and maintain their enterprise under the control of insiders; subsequently, managers collected more and more shares from their workers, and transformed the insider's privatization into *de facto* managerial privatization. In many enterprises this occurred with workers' tacit approval. Neither satisfactory corporate governance nor worker's self-management was established. It could be said that Russia's voucher privatization created a surprising record, as "such a concentration of employee ownership of the core of an economy is unprecedented in world economic history."[86] The second stage, or money privatization, turned out to be a banquet for a small group of the New Russians to grab public property into their own hands. The outcome went far beyond the expectations of many Western observers, and has not produced the results that had been anticipated when the objectives of privatization were developed.

Actually, considerable criticism of the privatization process has been presented. Some Russian scholars used the term *prikhvatizatsiia (*grabization) to describe the behavior of SOE managers and other members of the elite,[87] while Goldman calls it piratization.[88] Many commentators call it *nomenklatura* privatization, because a number of powerful financial groups have acquired enterprise shares through voucher speculation, and many members of the old CPSU *nomenklatura* have taken advantage of their positions and power in a time of economic disorder to secure valuable assets for themselves and their associates, while a number of enterprise directors

[86] Ibid, 58.

[87] Kiril G Holodkovsky, "*Rossiskaya Privatizatsia: Stolkhnovenye Interesov* (Russia's Privatization: Clash of Interests)," *Mirovaya Ekonomika i Mezhdunarodnoe Otnoshenya* (World Economy and International Relations), No.1, 1995, 72-86.

[88] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, 92.

have found themselves strategically placed to transfer the control of state property into their own hands. Russians with only entrepreneurial spirit but having no *nomenklatura* connections or large sums of money have had less success, however.[89] The evaluation from a moral dimension explains why many Russians were disappointed with the results of privatization. However, some scholars argue that the disappointment in privatization was stimulated by other factors as well. For instance, an expert on privatization for the World Bank who advised the Russian government notes: "Every time we polled the Russian population on privatization, it was clear that their responses were colored by the overall anger at inflation and the broader economic reforms. Privatization served as a lighting rod for other angers. Beyond this, citizens in their own minds even thought that privatization had caused the inflation and the bad things happening to them."[90]

No matter how people in Russia and outside evaluate the privatization, they will have to wait to see if the privatization program has improved the performance of the privatized enterprises. From a sociological view, the performance issue is not only related to managers' skills of marketing and competitiveness, more basically, it is related to the reconstruction of the management-worker relationship at the workplace. The next chapter will discuss the important problem.

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[89] Lynn Nelson, and Irina Kuzes, "Coordinating the Russian Privatization Program," *RFE/RL Research Report*, Vol.3, No.20, May 20, 1994, 25-26.

[90] Joseph R. Blasi, et al, *Kremlin Capitalism: The Privatization of the Russian Economy*, 79.

Chapter 6

The Post-Privatization Managerial Dominance and Management-Worker Relationship in Russia

Following the completion of the Russian privatization, a lot of scholars made their evaluation. Many of them focus on ownership change, the performance of the privatized firms, and the gap between the ideal type of corporate governance and the reality in Russia. They often put property rights, the role of board of directors and new management strategies at the center of discussion, but left the issue of labor-management relationship peripheral. The findings from case studies of this author in Russia, with a focus on management-worker relationship of the privatized enterprises, could provide a lot of fresh and important ideas from a different dimension as to why the privatization in Russia has not reached a satisfactory outcome.

First of all, corporate governance of privatized enterprises was not necessarily determined by ownership structure, but was rather shaped by the social relations between employee-owners, outsider investors, and managers who wanted to dominate the enterprises. By manipulating the interaction between the three parties, managers were able to exclude outsider investors and non-managerial employee owners from the board of directors and maintain an exclusive control over their enterprises with little shares.

Second, value orientation of managers might play an important role in selecting ownership structure and corporate governance. While a lot of managers preferred an authoritarian control over their enterprises, there were managers who supported the idea of workplace democracy and

cooperated with workers to establish the corporate governance that would absorb representatives of non-managerial employee-owners into the board of directors, and offered the employee owners more rights than other managers did.

Third, after privatization, managers with diverse value orientations might develop different patterns of management-worker relationships. In a cooperative management- worker relationship, workers would express their satisfaction with the result of privatization and their managers by showing motivation and initiatives to implement organizational goals; whereas in an authoritarian management-worker relationship, workers would feel that their rights as owners disrespected and, strongly dissatisfied with their social status at the workplace, they were demotivated and had a growing distrust of their managers. Many of these workers said their working conditions became even worse than in the Soviet era.

Fourth, in enterprises where managers adopted the authoritarian management approach, the quality of management was usually poor, the labor union was either weak or dissolved, and managers did not work hard to improve the performance of their enterprises as profit maximization might not be their top concern.

1. Ownership vs. Control: CEOs' Dominance in Privatized Enterprises

Corporate governance refers to the exercise of power and responsibility by company owners regarding the maximum return for their investment. A lot of Western observers assumed that proper and functional corporate governance of privatized enterprise would be a key goal of privatization in

Russia and, with a belief in ownership determination deeply rooted in the environment of rule of law in free market economies, they expected that blockholders of privatized enterprises should have seats in the board of directors and be able to play a positive role in making important decision for the enterprises' profit maximization in the long run. When they found out the composition of the board of directors in Russia's privatized enterprises tended not to really reflect the ownership structure of the firms, they usually blamed either the managerial owners or the majority owners, the non-managerial employees, and perceived the ownership of managers and non-managerial employees as a barrier to the proper functioning of corporate governance. But, as Thirkell, Petkov and Vickerstaff pointed out, much of the economic literature on privatization in Eastern Europe and Russia failed to focus on the complexities of ownership change and ignored the enterprise level, where real changes were thought to be contingent upon ownership restructuring.[1]

From interviews conducted in privatized enterprises, the author found that some large outside shareholders had no seats in the board of directors or had some seats but did not exercise their governance power, the majority ownership of non-managerial employees in some enterprises had no opportunity to oversee their managers, and top managers of a lot of enterprises gained full dominance with a small portion of shares or simply without any shares. Ownership change in the enterprises determined neither their corporate governance nor the real control of the enterprises. The findings also suggested that actual control was a core issue more important than ownership

[1] John E. M. Thirkell, Krastyu Petkov, and Sarah Vickerstaff, *The Transformation of Labour Relations: Restructuring and Privatization in Eastern Europe and Russia*, Oxford and New York, Oxford University Press, 1998, 64.

structure, and we should focus more on who really controlled the privatized enterprises.[2]

Before the voucher privatization was completed, the Russian government had already realized the potential problems of corporate governance, and had tried to correct the existing problems regarding corporate governance in the privatized enterprises. In the beginning of 1994 President Yeltsin issued a decree on minority shareholder rights, which mandated that, on the one hand, each enterprise should use cumulative voting method in its shareholders' meeting so that minority shareholders could elect some members to the board of directors, and minority shareholders could target all votes toward one or several specific nominees so that at least some outsiders would be elected into the board; and, on the other hand, no more than one-third of the members of the board of directors could be employees of an enterprise.[3]

According to the Presidential decree, a mandated new shareholder meeting was supposed to be held no later than March 31, 1994 in all privatized enterprises. However, the "Russian government's major initiatives on corporate governance were formally ignored… with an attitude of arrogance and defiance."[4] Based on their survey in December 1994, Blasi and Shleifer found that firms with outsider (non-state) board representatives increased from 40 percent in April to 76 percent in

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[2] After Russia's privatization was done, Clarke mentioned control without ownership very briefly, in a context completely different with my discussion. He talks about commercial and financial structure gained control over the privatized enterprises, thus "the Russian form of privatization is one in which capital can enjoy the fruits of control without the burden of ownership." (Simon Clarke, "The Enterprise in the Era of Transition," in Simon Clarke, ed. *The Russian Enterprise in Transition: Case Studies*. Cheltenham, UK, Edward Edgar, 1996, 43.) What is discussed here refers to how managers of privatized enterprises gained control over their enterprise with little investment and ownership.

[3] Joseph Blasi, and Andrei Shleifer, "Corporate Governance in Russia: An Initial Look," in Roman Frydman, Cheryl W. Gray, and Andrzej Rapaczynski, eds., *Corporate Governance in Central Europe and Russia: Vol.2, Insiders and the State*, Budapest, Hungary, Central European University Press, 1996, 82.

[4] Ibid, 87.

December that year, while the typical board has one outsider, one state representative, and four insiders (usually CEO and other senior managers who were subordinates of the CEO).[5] Obviously, senior managers occupied the majority seats in the board of directors. To limit the power of the outsider shareholders, Russian managers used various tactics, including persuasion of workers not to sell shares to outsiders,[6] issued new shares to managerial staffs and other employees with a minimal amount of charge, bought back shares from outsiders with company's funds then sold the shares to managers and employees at a very low price,[7] and encouraged employee-owners to delegate their voting rights to managers at the shareholder meeting. During the privatization years, "[I]t is impossible to know how widespread these practices were. Technically, they were not against the law, because Russian corporate law was still evolving."[8]

A new corporate law drafted by a team at the International Institute for Law-Based Economy in Moscow came into effect from January 1996. It attempted to exert a determining influence over corporate governance and stipulated that every corporation bring its corporate charter into compliance with the law. According to that law, all companies with more than fifty employees should be openly traded, but the law provides some protection for insiders and current shareholders against surprise takeover attempts. These provisions were designed to balance the interests of workers and managers and current shareholders against those who aggressively seek corporate

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[5] Ibid, 88.

[6] Samara Research Group, "Two Military-Industrial Giants," in Simon Clarke ed., *The Russian Enterprise in Transition: Case Studies*, UK, Edward Elgar, 1996, 293.

[7] Joseph Blasi, Maya Kroumova, and Douglas Kruse, *Kremlin Capitalism: Privatizing the Russian Economy*, Ithaca, NY, Cornell University Press, 1997, 93-94.

[8] Ibid, 94.

control. Under the new corporate law, any shareholder who owns at least two percent of a firm's stock or more has the right to introduce two proposals to the agenda of the annual shareholders' meeting and to nominate candidates to the board of directors and the audit committee. If ten percent of shareholders are dissatisfied, they can call a special shareholders' meeting by their own authority.[9] Some effects of the law could be observed, as about three-fourths of the large- and medium-sized companies across Russia had outsiders on their boards of directors in 1996, as compared with two-thirds in 1995.[10] However, the corporate governance of the privatized enterprises had not seen much improvement. "While the emergence of outside ownership is associated with some changes in corporate behavior, the attitudes of the general directors have remained very rigid in most companies, no matter who owns them."[11]

Blasi, Kroumova, and Kruse conducted a research in 1996 to evaluate corporate governance of Russian corporations through observing the number of outsiders on the board of directors, cumulative voting, the use of independent shareholder registration, the degree to which owners of concentrated blocks of stock (over five percent) had board seats in proportion to ownership, and maneuvering to keep new share issues and stock buybacks within the firm. They reported that thirteen percent of companies engaged in bad practices so systematically that their corporate governance was graded as horrible, 46 percent were received bad corporate governance grades, 39 percent engaged in one or two questionable practices, and only two percent of the surveyed

[9] Ibid, 98-99.
[10] Ibid, 100.
[11] Ibid, 100,102.

companies attained excellent scores.[12] Their conclusion was echoed by other researchers. Through a detailed study of twenty privatized enterprises in 1996 for example, Gurkov and Maital found that "for nearly half of the firms, managers were perceived to be the real owners and controllers, of the privatized firms."[13] Based on their survey in 2000, Estrin and Bevan too found that the average board composition of the sampled enterprises neither reflected the ownership structure nor corresponded to standards from other countries; and that management and sometimes regional authorities were over-represented while other stock- and stakeholders were under-represented.[14]

In Russian privatized enterprises one can often find two governing bodies—the board of directors and the council of directors, and may be confused about the difference between the two. The board of directors—consisted of senior managers, representatives of labor union, employee-owners, youth organization, and sometimes a few outsider owners as well, [15] —functioned more like a managerial council, whose members serve as counselors to CEO (commonly called as general director in Russia), than an institution to oversee the CEO's operation and make strategic decisions. Very often, the board of directors simply endorses decisions of the CEO and does not play the role normal corporate governance would need. Incidentally, the council of directors looks more like the board of directors in the West as it usually consist a CEO, deputies

[12] Ibid, 101.

[13] Igor Gurkov, and Shlomo Maital, "Perceived Control and Performance in Russian Privatized Enterprises: Western Implications," *European Management Journal*, Vol.14, No.2, April 1996, 160.

[14] Saul Estrin, and Bevan Alan, "Determinants of Russian Enterprise Performance," *Comparative Economic Studies*, Vol.45, No.2, 2003, 10.

[15] Veronika Kabalina, "Privatization and Restructuring of Enterprises: Under 'Insider' or 'Outsider' Control?" in Simon Clarke, ed. *Conflict and Change in the Russian Industrial Enterprise*, UK, Edward Elgar, 1996, 256-259.

of the CEO, and sometimes representatives of outside property owners from banks, property funds or local administration. A mixture of an executive body and representatives of some outside large owners, its main role is to assist rather than supervise the CEO. In enterprises where the CEO dominates everything, the council of directors rarely meets. A Russian scholar so depicts, "the Council of Directors is a rather passive or even superfluous organ in many enterprises. Generally, its role was not apparent."[16] Actually, a lot of official organizations named as council in the Soviet era were simply figureheads. Russian managers are familiar with such council institutions,[17] and they played a crafty game] by appointing managerial team members into the broad of directors, thus effectively turning it to a managerial council and by creating a council of directors with the people who were supposed to be the members of the board of directors, then rendering the council of directors functionally inactive. This practices often get tacit approval from outsider-owners including representatives from banks, property funds and local administration, who are more concerned with maintaining personal contact with the CEOs for mutual personal benefits than performing the role of oversight.[18]

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[16] Katharina Pistor, "Privatization and Corporate Governance in Russia: An Empirical Study," in Michael McFaul and Tova Perlmutter, eds., *Privatization, Conversion, and Enterprise Reform in Russia*, Boulder, CO, Westview Press, 1995, 73-74.

[17] The original meaning of the word "Soviet" in Russian is council. In the Soviet Union, when an organization was named *soviet*, people would perceive it simply a council with only nominal power. For instance, the 1977 Constitution of the Soviet Union, remained essentially unchanged from the 1936 Constitution, defined the Superior Soviet as the national parliament; but the legislative branch was actually dominated by the executive branch of the USSR government and had no real power. See Stephen White, Alex Pravda, and Zvi Gitelman, eds. *Developments in Soviet & Post-Soviet Politics*, Durham, NC, Duke University Press, 1992, 90-91.

[18] For example, the author interviewed a CEO of a private bank in summer 1995 in St. Petersburg and found the relationship between managers of industrial enterprises and private bank owners was interdependent. The bank CEO was the former communist party secretary of a district of the city, and a lot of SOE general directors

If the outside large blockholders did not really gain control in the board of directors, could the privatized enterprises with a large rank-and-file workers' ownership in Russia somehow recognize and respect the interests of workers? When managers and workers became owners, theoretically they have a greater incentive to improve performance because they share in the benefits of that improvement.[19] Puffer and McCarthy thought that the role of worker collective in enterprise decisions during the communist and *perestroika* periods could lead to worker representation on the board of directors, as in Germany and some other countries.[20] The Russian government perhaps anticipated the same, as the Russian Federation State Committee for State Property (GKI) required all firms to provide the rank-and-file employees with one board representative in the early stage of privatization. Nevertheless, the rank-and-file board members were removed from most of the boards by managers later. Although workers could theoretically have voted the rank-and-file members into the board in 91 percent of the enterprises, workers' control has not materialized after Russia's privatization.[21] Jones found that the overall influence of the non-managerial employees on decision-making was low and independent from the form of

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were appointed by her. After the collapse of the Soviet Union and the Soviet communist party, she immediately discussed with the SOE managers, and registered a private bank. The SOE managers transferred funds of their enterprises to the private bank in exchange for shares of the bank; the bank so collected its capital then lent the funds back to the SOEs. As the shareholders of the bank which provided loans to the SOEs, the managers were able to consolidate their power at the workplace and gained control over the enterprises.

[19] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, New York, NY, Springer, 2008, 225.

[20] Sheila M. Puffer, and Daniel J. McCarthy, "The Emergence of Corporate Governance in Russia," *Journal of World Business*, Vol.38, No.4, 2003, 296.

[21] Joseph Blasi, and Andrei Shleifer, "Corporate Governance in Russia: An Initial Look," 81.

ownership; even if workers had majority shares of a firm, they did not necessarily control it.[22]

The form of managerially controlled employee-owned firms can also be found in some enterprises in the West, where institutional mechanisms for the majority of employee owners to exercise their potential control, such as electing employee representatives onto the board or forming institutions enabling the workers to vote as a block at shareholder meeting, are absent or weak.[23] In Russia, the institutional weakness is not the only problem; actually, a lot of managers have purposively reduced the rights of employee shareholders. For instance, Blasi and Shleifer found that Russian managers often manipulated shareholder meetings with various excuses to prevent employee owners from confidential voting; moreover, "[M]anagers in various parts of the country provided the interviewers with a number of very clear descriptions of the bush meeting/proxy voting method of collecting employee votes… Those employee representatives who come to the meeting are mainly managers themselves;"[24] but, when interviewed, "[M]anagers often attempt to present other top management members who serve on the board as rank-and-file board representatives."[25] Consequently, "[R]ank-and-file employee shareholders are the largest

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[22] Derek Johns, "The Economic Effects of Privatization: Evidence from a Russian Panel," *Comparative Economic Studies*, Vol.40, No.2, 1998, 75-102; quoted from Garsten Sprenger, "Ownership and Corporate Governance in Russian Industry: A Survey," *European Bank for Reconstruction and Development, Working Paper*, No.70, Jan. 2002, 8.

[23] John S. Earle, and Saul Estrin, "Employee Ownership in Transition", in Roman Frydman, Cheryl W. Gray, and Andrzej Rapaczynski, eds. *Corporate Governance in Central Europe and Russia, Volume 2: Insiders and the State*, 4.

[24] Joseph Blasi, and Andrei Shleifer, "Corporate Governance in Russia: An Initial Look," in Roman Frydman, Cheryl W. Gray, and Andrzej Rapaczynski, eds., *Corporate Governance in Central Europe and Russia: Vol.2, Insiders and the State*, 101-102.

[25] Ibid, 89.

insider blockholders in the companies, yet they have no corporate power."[26]

In order to retain workers' control over enterprises, the Russian Parliament adopted the Law on Particularities of Legal Status of Employees' Joint Stock Company (People's Enterprises) on June 24, 1998, under the pressure of communists and other leftists groups. According to the law, employees of the people's enterprise should possess at least 75 percent of shares, and each shareholder can not possess more than five percent of the shares; employees leaving the enterprises are required to sell their shares to the enterprise; and voting on important issues such as electing CEO and the board of directors, or approving auditor's reports, is done according to the principle of one shareholder one vote. Supporters of this corporate form argued that the people's enterprises fit into the Russian tradition of community-style work, and can create a wide middle class of workers. But, the practice have turned out to be a failure, because in most regions of Russia no enterprise has adopted the corporate form, except in Kabardino-Balkaria region of the North Caucasus Mountains, where local government recommended the people's enterprise to 90 collective farms.[27]

How did managers and employee-owners of privatized enterprises describe and evaluate the relationship between managers, employee owners and outside owners? Existing literature provided no detailed information and answers to the question. The data from my in-depth interviews might help explore some important aspects of the relationship. Twenty months after the 1996 corporate law came into effect, the author conducted interviews in eleven privatized

[26] Joseph R. Blasi, Maya Kroumova, and Douglas Kruse, *Kremlin Capitalism: Privatizing the Russian Economy*, 105.

[27] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, New York, NY, Springer, 2008, 235-236.

industrial enterprises in Moscow area in the autumn of 1997. In each enterprise a manager and three workers were interviewed. The enterprises and interviewees were randomly chosen by my Russian collaborators of the Vox Pupuli public opinion survey organization from its enterprise list, as introduced in Chapter three. The basic information of the eleven enterprises is listed in Table A-1 and 44 interviewees in Table A-2 of the appendix of this chapter. Enterprises, both large and small,[28] of eight different sectors from manufacturers of transportation equipment, of measuring instruments, food producers, lingerie to wallpaper makers were included in the interviews. The change of employee numbers in the enterprises somewhat reflected the economic situation of the firms before and after privatization (see Table A-1). Before privatization three enterprises (C, D and G) expanded their employment, but seven conducted downsizing. After privatization, G maintained a good economic status and continued to increase its employee numbers, but all other enterprises had more or less reduced their employees. While both profitable and loss-making firms were included in the interview, those enterprises with better economic status did not necessarily enjoy good corporate governance or management-worker relationship; whereas in enterprises with poor economic status, managers and workers worked together and developed a cooperative management-worker relationship. The issue will be further explored in section three and four of this chapter.

The information about the ownership structure of the eleven privatized enterprises interviewed is listed in Table 6-1. Among these enterprises, one was fully owned by top managers (enterprise B), two were almost fully owned by non-managerial employees (enterprise

[28] Among them the smallest enterprise had 260 employees and the largest one had 4,000.

D and H), and in five enterprises 50 percent or more shares were held by insiders (enterprise C, E, F, I and K), while in three enterprises 50 percent or more shares were in the hands of outsiders (enterprise A, G and J). It is noticeable that perhaps reluctant to disclose the accurate number of the shares in their hands, managers of enterprise A, C and F did not reveal the ratio of the shares owned by employees. Observing the ownership structures of eleven enterprises, one might find that ownership dominance of both insiders and outsiders existed. The results did not differ significantly with existing literature reports.

Table 6-1 Ownership Structure of Eleven Privatized Enterprises

Enterprise	Enterprise Size (employee number)	Owner				
		Government (%)	Manager (%)	Workers (%)	Other People (%)	Other Organization (%)
A	400	10	15		10	65
B	623	…	**100**	…	…	…
C	1,000	20	50		30	
D	4,000	…	0	**98**	2	…
E	700	…	30	55	15	…
F	500	…	60		40	…
G	2,500	…	5	20	20	55 (bank)
H	280	…	2	**98**	…	…
I	260	20	49	10	8	…
J	330	…	10	30	20	40
K	400	…	15	43	…	42

Note: The question is: “Percentages of the shares of your enterprise held by top managers, other employees, governments, outsider individuals, other institutions (banks, funds, enterprises, etc.) in 1997?”
Source: The information is collected from my questionnaire No.1, No.5, No.9, No.13, No.17, No.21, No.25, No.29, No.33, No.37 and No.41, answered by managers.

Answers of eleven manager interviewees regarding the composition of the board of directors were listed in Table 6-2, and compared with the ownership structure and the composition of the board of directors in Table 6-3. Data collected from the interviews show that the status of the board of directors varied in the enterprises, and the ownership structure of the enterprises had only a minimal impact on the composition of the boards of directors. No matter how many shares the managers held (sometimes only a very small portion, as in enterprise D and H), they often occupied the majority seats in the board of directors (enterprise D, F, G, H, I and J), and manager board members include CEO, first deputy director for production, commercial director, technical or engineering director, and director for construction, even branch managers and leading technical specialists (for example, in enterprise D and F).

Table 6-2 Composition of the Board of Directors of Eleven Enterprises

Firm	Government representative	Managers	Representative of workers	Representative of outsiders
A	Board of directors exists but is operated poorly			
B	There exists only an observant council with 4 managers			
C	…	Some	…	Some
D	…	All board members are managers	…	…
E	…	2	…	2
F	…	All board members are managers	…	…
G	…	4	3	…
H	…	5	3	…
I	1	3	…	…
J	…	5	…	1
K	Manager didn't answer who were the board members and what role the board played			

Note: The question is: "Who are the members of your Board?"

Source: Information in the table is collected from my questionnaire No.1, No.5, No.9, No.13, No.17, No.21, No.25, No.29, No.33, No.37 and No.41.

In the eleven enterprises most boards were mainly composed of managerial team members appointed by CEO, they could hardly serve to oversee the CEOs and might be perceived as the managerial council for the CEOs. In four enterprises, investment funds, banks, other organizations (such as the state property committee of Moscow District) held more than 40 percent of shares (enterprise A, G, J and K), but the outside blockholders either sent only one director to the board (enterprise J) or none at all (enterprise G). In other two firms the board was poorly run (enterprise A and K) and the outsider large shareholders seemingly did not care about that. In nine enterprises employee shareholders hold more than ten percent of shares, but only in two of the enterprises did representatives of employee shareholders have seats in the board.

Table 6-3 Status of the Board of Directors in Eleven Enterprises

The Status of the Board of Directors	Ownership Composition		
	Fully Insider Ownership	Insider Ownership Over 50%	50% Outsider Ownership or More
There is no Board of Directors, or the Board is operated poorly	enterprise B	enterprise K	Enterprise A
Only Managers in the Board	enterprise D	Enterprise F	
The Majority in the Board are Managers, And Outsider Members are Minority	N.A.	enterprise I	enterprise J
A Half of Board Members are Managers, And Another Half are Outsiders	N.A.	enterprise E	Enterprise C
The Majority in the Board are Managers, and Representatives of Employee Shareholders are Minority	enterprise H	…	enterprise G

Note: The table is complied based on the information in Table 6-1 and Table 6-2.

As mentioned earlier, in enterprises where managers dominated the board of directors, a council of directors—which role was different from that of the board of directors, was set up to arrange seats for representatives of the outsider blockholders. For instance, the deputy CEO of enterprise G reported that in the enterprise both the board of directors and the council of directors existed, and each had seven members. While the former was composed of two managers, one representative from the labor union, two section managers and two representatives of non-managerial employees, the latter included a general director, the chairman of labor union, and five representatives from their outside blockholder investor-bank (holding 55 percent of the shares). In enterprise B where managers held 100 percent of the shares, the board of directors was abandoned, and replaced by "an observant council with four people, the CEO, a technical director, a chief designer and another senior manager."[29]

Through observation of the privatization took place in the interviewed enterprises, it could be found that a lot of managers controlled the board of directors with some portion of shares, and have gained dominance in their enterprises, regardless of who were the majority shareholders of those enterprises. There has been a lot of discussion about the weak legal environment, the immature outside investors and stock market in the existing literature about Russia's privatization. Having analyzed the interview data, the author would like to suggest that with their strong desire to control the board of directors, coupled with large outside investors' lukewarm appetite for control, CEOs had significantly weakened the role of the board of directors and corporate governance.

[29] Questionnaire No.5, p.2.

In 2000 Russia was ranked the last among 25 emerging countries on responsible corporate governance criteria.[30] In a speech delivered at the American Chamber of Commerce in Russia in 2001, former finance minister Boris Fedorov said: "It's clear that despite nearly 10 years of economic changes, we have not yet developed a culture where people understand properly the relationship between managers, shareholders, minority shareholders and the state."[31]

In order to help improve corporate governance in Russia, in 2002 the Russian government introduced the Code of Corporate Conduct (it was made effective in 2004) and adopted new laws and amendments to the existing laws.[32] Shleifer and Vasiliev hoped that the role of large shareholders in corporate governance would strengthen over time.[33] In fact, redistribution of ownership in the years after privatization was characterized by two main parallel trends: further concentration of control in the hands of managers, and an increase in the shares of outside blockholders.[34] "What lies behind these changes, and what real effects will the changes have?" Lazareva, Rachinsky, and Stepanov wrote about Russian large companies: "After years of repeated, grave malfeasances against minority shareholders and fierce battles for assets,

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[30] Craig Karmin, "Corporate-governance issues hamper emerging markets," *Wall Street Journal*, November 8, 2000, C1.

[31] Boris Fyodorov, "Speech at the American Chamber of Commerce in Russia conference," April 26, 2001; quoted from Sheila M. Puffer and Daniel J. McCarthy, "The Emergence of Corporate governance in Russia", *Journal of World Business*, Vol.38, No. 4, 2003, 286.

[32] According to Kirill Ratnikov, the Code was drafted by lawyers from a New York based law firm Coudert Brothers LLP, and a group of Russian law scholars (www.corp-gov.org/bd/db.php3?db_id=437&base_id=3).

[33] Andrei Shleifer, and Dmitry Vasiliev, "Management Ownership and Russian Privatization," in Roman Frydman, Cheryl W. Gray, and Andrzej Rapaczynski, eds., *Corporate Governance in Central Europe and Russia: Vol.2, Insiders and the State*, 75.

[34] Olga Lazareva, Andrei Rachinsky, and Sergey Stepanov, "A Survey of Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, New York, NY, Springer, 2008, 317.

controlling owners of Russian firms have begun to understand that the only way to sustain the development of their companies is by attracting external funds;" but, some of the large owners simply wanted to exit their businesses by selling their assets at a good price.[35]

Table 6-4 Board Composition

Representatives of Shareholders and Stakeholders in the Board of Directors	Board Composition		
	1998 Survey (%)	2002 Survey (%)	2006 Survey (%)
Workers	22	21	14
Managers	39	35	52
Outside large individual shareholders	16	18	…
Outside minority shareholders	…	…	14
Government (all levels)	5	7	…
Commercial organizations	12	13	…
Other directors (including independent directors)	4	5	20
Non-commercial organizations	2	1	…
Total	100	100	100

Source: Olga Lazareva, Andrei Rachinsky, and Sergey Stepanov, "A Survey of Corporate Governance in Russia," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, New York, NY, Springer, 2008, 329. Sample size: 1998 survey, 278; 2002 survey 294; 2006 survey, 75 (listed firms).

Analyzing board compositions of sampled firms in 1998, 2002 and 2006, Lazareva et al pointed out that in Russia boards are often dominated by managers and large shareholders' representatives; employee shareholders are generally on the incumbent management side; local governments often have some seats in the boards even if they do not own shares; independent board members have increased since 1998, but they may have close ties with the management or

[35] Ibid, 315.

the controlling shareholders (see Table 6-4).[36] As of 2009, about one third of companies still did not have independent board members.[37]

Lazareva et al noticed that, on average, boards of directors spent too much time on tactical issues, which is consistent with the insider domination in Russian firms (such concerns normally should be performed by management).[38] Kozarzewski found that, as the code of corporate conduct in Russia was not compulsory and generally applied only to listed companies, for 93 percent of surveyed companies in Russia, introducing efficient practices of corporate governance was a question of a good will and understanding of the role of good corporate governance mechanisms in the company's success; and in the companies, all the decisions, including strategic ones, were taken, or at least prepared by the executive branch, while the board of directors rather played the role of a supervisory board with its predominantly control and permissive functions.[39]

In 2008, Lazareva et al concluded that the largest Russian companies were gradually improving their corporate governance as they moved into international financial markets and wanted to raise their market valuation and establish good reputation; however, overall, corporate governance in a typical Russian company remained at a rather low level; and firms' ownership structure were still very concentrated and companies attracted little external funds.[40]

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[36] Ibid, 328-330.

[37] Russian Economic School, "Corporate Governance Practices in Russia: 2004-2009 Comparative Study, New Trends in 2009," Moscow, Russia, 2010, 27 (http://www.nes.ru/dataupload/files/events/news/CG_2004-2009_Eng.pdf).

[38] Olga Lazareva, et al, "A Survey of Corporate Governance in Russia," 330.

[39] Piotr Kozarzewski, "Corporate Governance Formation in Poland, Kyrgyzstan, Russia, and Ukraine," in Robert W. McGee ed. *Corporate Governance in Transition Economies*, 276-277, 281.

[40] Olga Lazareva, et al, "A Survey of Corporate Governance in Russia," 341.

2. Managers' Characteristics and Value Orientation

The above-mentioned discussion about the status of the board of directors in Russia's privatized enterprises suggested that manager, particularly the CEO, was a key player in restructuring the enterprises. After-privatization, even if a CEO has kept his position unchanged, he could no longer count on the support of the state to maintain his power. Given that outsider investors often exert little influence on management, what kind of authority over previous worker-comrades has the managers reconfigured? With the data gathered from interviews, the author will analyze in this section the background of manager interviewees and their different value orientation—a necessary step toward further discussion about the new management-worker relationship in sections to follow.

Russian managers were educated and trained in a Communist society, and their values and behavior were shaped by the Soviet culture with little influence of other civilizations. In 1987, Khotin conducted in-depth interviews with émigré respondents and asked them to describe the directors with whom they had worked in the Soviet Union. According to the respondents' evaluations, the vast majority of directors possessed good knowledge of production, ability to get along with subordinates, were workaholic (working at least 80 hours a week) and strict but fair to employees.[41] Martin indicates that in the socialist period management required at least formal commitment to socialism and a combination of technical and political skills; the factory director

[41] Leonid Khotin, "Old and New Entrepreneurs in Today's Russia," *Problems of Post- Communism*," Jan.-Feb., 1996, 51.

was the arbiter of his enterprise, and decisions at the enterprise level were highly centralized, founded on the ideology of the "one man manager."[42]

After privatization was implemented, a lot of old managers were replaced. Blasi, Kroumova and Kruse report that 33 percent of large- and medium-sized enterprises had replaced their CEOs since 1992; in about 80 percent of the firms CEOs were replaced by other managers from within the company.[43] Perepelkin so described the characteristics of the managers: they were predominantly men between the ages of 30 and 40s who were born outside Moscow, finished secondary school at hometown and then entered higher educational establishments in Moscow; their behavioral stereotype of the "provincial fellow"—collective, active, and ambitious, acquired in youth, was still in place and helped them not only to endure, but also to outstrip the less tenacious Muscovites in the routines of daily life; they often demonstrated patriarchal traditions, and had a tendency of nepotism. These managers would hire their friends, relatives or the people they recommended instead of shortlisting specialists through competition.[44]

It was found from the interview data that a lot of characteristics of the manager interviewees were quite similar to what Perepelkin described: of the eleven manager interviewees, nine were male and only two are female (F1 and K1); eight out eleven were "provincial fellows" born in places distant from Moscow[45] and received college education either

[42] Roderick Martin, *Transforming Management in Central and Eastern Europe*, Oxford University Press, 1999, 97-98.

[43] Joseph R. Blasi, et al, *Kremlin Capitalism: Privatizing the Russian Economy*, 135.

[44] O. V. Perepelkin, "The Russian Entrepreneurs: Sketches for a Social Portrait", *Sociological Research*, Jan.-Feb., 1996, 74-75.

[45] Their birthplaces are: A1, Moscow; B1, Donetzk; C1, Aletset'ebek; D1, Harkov; E1, Arhangol'sk; F1,

before they entered enterprises or during the years they worked for the enterprises; among them three were promoted to their current positions before privatization and eight were promoted after privatization (see Table 6-5), but no one was selected from outside. Except manager A1, all ten other managers entered their enterprises after received college education. During the Soviet era no departments of business administration existed in universities, nor were courses of modern economics or management provided; therefore, majors of the managers in colleges were usually in the fields of technology. They had to accumulate knowledge about management only from work experiences. That was probably why Russian managers were often promoted within workplaces, because their knowledge in management was largely linked with their work experience in the enterprise they had been working for.

Table 6-5 Carriers of Managers

Age	Promoted to current position in or after 1992	Current position appointed before 1992
36-45 years old in 1997	C1, F1, G1, J1	…
46-55 years old in 1997	H1	A1
> 56 years old in 1997	B1, I1, K1	D1, E1
Total	8	3

Source: My questionnaire No.1, No.5, No.9, No.13, No.17, No.21, No.25, No.29, No.33, No.37 and No.41.

A common feature of their career was that, as of 1997, the average years they worked in their enterprises was fifteen. In other words, a lot of them worked in the enterprises since 1982, before

Drozgon; G1, Stavropolskyi Area; H1, Moscow; I1, Moscow District; J1, Kursk District; K1, Azerbaijan.

perestroika (reform) was initiated. With such a long history as insiders of the enterprises, at an average age of 47, they were either appointed to the current position by the government before privatization or got promoted afterward. Most of them had a strong commitment to their organizations,[46] and were quite familiar with both the daily operation of their enterprises and the rank-and-file workers. Among them, C1, F1, G1 and J1 began their socialization in the Brezhnev era, while A1, B1, D1, E1, H1, I1 and K1 were socialized during the Khrushchev era. Their personal background information implied that all managers accumulated their work experiences in the Soviet era; even though some of them were promoted to head newly established marketing and finance offices in the factories, they usually had no training in the new fields and could only learn through trials and errors.

It might be too idealistic to assume that after privatization Russian managers could change their management skills and style immediately; on the other hand, the background information also suggested that the managers' value orientation could be largely influenced by the traditional Soviet managerial culture.

In the last two decades of the twentieth century, the Soviet Union/Russia had tried two key policies for enterprise reform, i.e., the workplace democracy policy implemented by Gorbachev (mentioned in chapter four), and the privatization policy. The idea of workplace democracy in

[46] In my questionnaire manager interviewees were asked such a question: "Do you agree that the longer you work for your enterprise, the more you feel you belong, in 1987, 1992, and now?" A1, B1, D1, E1, F1, G1, J1 and K1 responded with "fully agree" or "almost agree" for year 1987, 1992 and 1997; C1 and H1 said they "almost not agreed" for year 1987 but "fully" or "almost" agreed for year 1997.

the Soviet Union was very different with that of the concept used in the US.[47] The official version of workplace democracy in the Soviet Union was rooted in the dogma of master of production, and was not based on workers' ownership or self-control and self-management. Under the policy, workers' rights were not clearly defined, and they were simply allowed to elect top managers. When the policy was implemented, in many enterprises the procedure of managers' election was manipulated by managers, and the workplace democracy policy did not necessarily raise workers' working motivation or improve efficiency of enterprises. Here the reason that Russian managers opposed the workplace democracy policy and whether or not they liked the privatization policy will be discussed. It is worth noting that how Russian managers viewed the two policies could reflect their perceptions of managerial authority at the workplace and their attitudes towards enterprise restructuring.

My interview questionnaire included two open-ended questions: 1. "How do you evaluate Gorbachev's policy of workplace democracy? Do you think that this reform effectively improved the performance of your enterprise? Why?" and 2. "Do you think that the employee ownership through privatization has given workers more rights, power and advantages? Why?" From the answers of eleven manager interviews it was found that eight managers evaluated the workplace democracy policy negatively (see Table 6-6) with different explanations.

[47] Frank Lindenfeld, and Joyce Rothschild-Whitt, eds. *Workplace Democracy and Social Change*, Boston, MA, Porter Sargent Publishers, 1982, 6-7.

Table 6-6 Managers' Attitudes towards Workplace Democracy and Workers' Ownership

Number of Interviewees and Percentage	Positive Attitude towards Workplace Democracy	Negative Attitude towards Workplace Democracy	Total
Positive Attitude towards Employee Ownership	H1	0	1
Negative Attitude towards Employee Ownership	G1, I1	A1, B1, C1, D1, E1, F1, J1, K1	10
Total	3	8	11

Source: My questionnaire No.1, No.5, No.9, No.13, No.17, No.21, No.25, No.29, No.33, No.37 and No.41.

An explanation often mentioned was that workers would not elect the right person to the CEO position. For example, B1 said that the workplace democracy policy advocated nonprofessional leadership, and failed to make work more effective; thus it was a wrong way. He thought the council of directors may elect the general director, as there people are at the same level; whereas if a worker got elected he could do nothing.[48] E1 replied that "the policy was negative to productive activities of enterprise; often workers elected not the better but the comfortable managers."[49] F1 expressed the same concern, "Psychology of individual turns out to be that he would not elect the intelligent and familiar person, rather, he might elect the provocative trust one."[50] And A1 said that the workplace democracy "does not offer managers the complete unbiased evaluation."[51] Such opinions reflected the worries that some managers might not be elected by workers under the workplace democracy policy. Another reason interpreted by C1 was that the state ownership still existed and managers should be appointed by

[48] Cited from questionnaire No.5, p.13.
[49] Quoted from questionnaire No.17, p.13.
[50] Quoted from questionnaire No.21, p.13.
[51] Quoted from questionnaire No.1, p.13.

the state owner of enterprises.[52] Interestingly, there were three managers (G1, H1 and I1) who somewhat supported the workplace democracy policy. G1 said: "This is a fine policy. The effectiveness of work in the enterprise became increased, as manages' authoritarian style was moved away and normal conditions for workers were created."[53] His opinion implied that workers might not dislike the authoritarian style of managers. H1 pointed out that the workplace democracy policy was away from market relations, and Gorbachev's policy solved no problems; but some kind of manager election by workers' collective helped improve work effectiveness at enterprise, as more intelligent specialists became managers.[54] And I1 so described: "In the first stage the policy of Gorbachev really helped. Workers had interest and possibility to participate in management of enterprise. It helped the work of enterprise with new effective ways, and appeared the brigades for self-control and the aspiration of saving materials."[55] The opinions of the three managers are different with that of others.

From the answer of the manager interviewees to the second open-ended question regarding privatization, divergent opinions were again found. Among the manager interviewees, H1 was the only one who thought that after privatization employee owners should be given rights, power and advantages, and these ideas had actually been implemented in enterprise H (see Table 6-5). He said: "The privatization of our enterprise really gave workers more power. I agree with this idea that the presence of workers' shares represents their rights in the way of voting for important

[52] Cited from questionnaire No.9, p.13.
[53] Quoted from questionnaire No.25, p.13.
[54] Quoted from questionnaire No.29, p.13.
[55] Quoted from questionnaire No.33, p.13.

decisions. Earlier the workers' collective didn't have a decisive voice; decisions were taken conveniently by managers."[56] All ten other manager interviewees, however, admitted that in their enterprises employee-owners were not given rights and power after privatization, while in nine enterprises (except enterprise B) employees held considerable amount of shares. B1, C1, J1 and K1 thought that employee-owners should not be given power and rights. B1 said: "Giving them some stocks, and that's enough, if they will receive dividends upon the stocks;"[57] K1 said that not any worker "feels himself as shareholder;"[58] and J1 thought that "workers won't make efforts in management."[59] On the other hand, when explaining why employee owners were not given rights and power in their enterprises, A1, D1 and G1 said that each worker held only small amount of shares, therefore the employee owners should not play any role in the board of directors. For instance, A1 said: "There is no an identical working collective. Even if workers bought 51 percent of shares, no one holds more than two percent that could offer him rights to raise a motion."[60] D1, of an enterprise which 98 percent of shares were in the hands of employees, said that employee owners in his enterprise did not get owner's rights as they individually possess only small amount of shares;[61] and G1, of an enterprise which employees held 20 percent of shares while managers had none, said, "more rights and power were not offered to workers, though there are employee

[56] Quoted from questionnaire No.29, p.13.

[57] Quoted from questionnaire No.5, p.13. This is simply an expression of the manager's opinion regarding employee ownership. The actual situation in enterprise B is that workers' shares had been completely bought by managers, and the firm is 100 percent owned by managers.

[58] Quoted from questionnaire No.41, p.13.

[59] Quoted from questionnaire No.37, p.13.

[60] Quoted from questionnaire No.1, p.13.

[61] Quoted from questionnaire No.13, p.13.

shareholders, because the controlling pact of shares are not in the hands of workers."[62] The answer of F1 was somehow insightful: "Stocks don't give rights; rather, the relationship in society gives the rights."[63] As the author understood it, the relationship in society mentioned by F1 implies the social relations at the workplace. In other words, a lot of Russian managers don't really regard employees' ownership; instead, they perceive themselves a kind of permanent leader and workers simply wage earner, no matter whether they hold shares or not. The manager interviewees were also asked if employee-owners could play an important role in decision making.[64] Only H1 and G1 expressed that the employee shareholders of their enterprise played an important role in decision making, but other respondents said they did not think so.[65]

The answers of the manager interviewees suggested that value orientation of the respondents varied, while most of the managers took their managerial positions for granted and worked in a somewhat authoritarian manner, a few of them supported the socialism idea of workplace democracy and cared about employee owner's rights. Comparing their value orientation with the composition of the board of directors of their enterprises, the author noticed that only managers of enterprise H and G supported the workplace democracy policy and allowed representatives of employee shareholders to have seats in the board of directors; however, in other enterprises where managers negatively evaluated the workplace democracy policy, representative of employee

[62] Quoted from questionnaire No.25, p.13.

[63] Questionnaire No.21, p.13.

[64] The question is: "Do you think that employee shareholders of your enterprise play an important role in decision making?"

[65] H1 and G1 said that they were fully certain that the employee shareholders in their enterprises played an important role; but other respondents replied with either "almost not" or "absolutely not."

shareholders were excluded from the board of directors, even though ten to ninety-eight percent of shares of those enterprises were in employees' possession (see Table 6-1).

3. The Cooperative Management-Worker Relationship: A Case Study of the Moscow Wallpaper Factory

Democratization and privatization were two key aspects of Russia's transition. During the process SOE managers were detached from government's managerial apparatus; their political skills in dealing with the Communist regime and central planning system were no longer needed. As Martin pointed out, "managerial careers became tied to the performance of the enterprise, not to the reputation within the *nomenklatura* system; career progression involved commitment to the enterprise, not to the Party."[66] In the privatization process, SOE managers fought for survival of their enterprises and indeed gained support from their employees under the banner "we are all one big family." After their control over enterprises was consolidated, did managers become closer to or more distant from the workers? The managerial authority of the Soviet enterprises could be depicted as having a dual feature: the patriarchal leadership of general director and a "comrade" face in front of workers. A traditional practice of Soviet management had been "going to the people" by face-to-face comrade-like talk with individual workers at the workshop to mobilize them for better work,[67] and its Chinese version was to "believe in the masses and rely on them".

[66] Roderick Martin, *Transforming Management in Central and Eastern Europe*, 97.

[67] Samara Research Group, "Two Military-Industrial Giants," in Simon Clarke ed. *The Russian Enterprise in*

Now that both managers and workers are owners of their enterprise, had they become real comrades? How was the post-privatization management-worker relationship reconfigured in the enterprises? Inspired by the value orientation of manager H1, the author did a case study of enterprise H and found that the relationship between managers and workers appeared to be really cooperative.

Located in the northeast of Moscow city, enterprise H, a wallpaper producer with a history that could be traced back to the 19th century, was established in the 1860s, and was owned by Dmitrievoy at the beginning of the 20th century. In 1916 it had 64 employees. After the October Revolution the factory was nationalized in 1923 and renamed as the Fifth Wallpaper Factory. After 1988 the enterprise experienced dramatic changes. In 1997 the author interviewed with a manager and three workers in that enterprise: H1 (the chief engineer), H2 (operator), H3 (machinist) and H4 (controller) from different workshops.[68] While H1 was a male, H2, H3 and H4 were all female aged 42, 55 and 35 when they were interviewed. H1 was 53 years old in 1997 with a college education. He was transferred to the enterprise in 1988, and promoted to the post of chief engineer in 1993. Both H2 and H4 graduated from technical school while H3 had only finished middle school education. All three workers had worked there for more than 15 years, and had witnessed all the changes that took place in the enterprise since the early 1980s. My long questionnaire included 106 questions regarding their working motivation, perception of actual wage

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Transition: Case Studies. UK: Edward Elgar, 1996, 252. In her *Dream of a Red Factory: The Legacy of High Stalinism in China* (New York: Oxford University Press, 1994), Deborah Kaple discussed mainly the formal methods of politically mobilizing workers.

[68] The information used in the section is cited from Questionnaire No.29 (H1), No.30 (H2), No.31 (H3) and No.32 (H4).

determination, and management-worker relations from various dimensions.

All worker interviewees said that their working motivation in 1987 was mainly determined by wage amount and the desire for maintaining personal social status at the workplace, and somehow by the desire to obtain high productive results and that for self-actualization and personal achievements at their workplace. They thought that in 1987 one's wage at the workplace was determined only by his job performance, and one's good performance in implementing organization's goal could help him get a better job or promotion. They said that at that time they were somewhat satisfied with their job and felt their own job interesting, had usually worked very well and reached the targets of their jobs, though H3 admitted that she could have worked better and accomplished much more. H2 and H4 reported that sometimes their workload was so heavy that they could hardly finish it in ordinary workdays. They also mentioned that their commitment to the work organization was quite high, as they either fully or almost fully agreed that the longer they worked for the enterprise, the more they felt themselves belong to it. But the worker interviewees complained that their wage in 1987 was either much or little lower than that of workers in other enterprises.

In terms of the management-worker relationship in 1987 in enterprise H, the worker interviewees shared a lot regarding the management approach of the general director (CEO). They reported that in 1987 the managers did not share information with the rank-and-file workers, and there were almost no interaction and communication between the two parties for achieving organization's objectives; workers rarely participated in discussion and decision of production problems; they even did not feel free to discuss important things about their jobs with immediate

superiors; only when decisions about employees' welfare were being made could they participate in discussion with the management. H3 and H4 felt that workers were not encouraged to implement organization's goal. The three worker interviewees expressed that frequently little actions could be taken until a supervisor approved a decision, and a worker who wanted to make his own decisions would be quickly discouraged; therefore, workers had no initiative to make suggestions or proposals for achieving organization' goal to top managers. They said that, at that time, besides the regular working relations, personalized friendliness between superiors and subordinates did not exist. When being asked if the majority of workers were satisfied with the work of their workshop leaders and that of the CEO, the interviewees replied that they were somewhat satisfied with the workshop leaders, but were not so with their CEO. H1 felt quite serious resistance from the bottom level to the goals set by management. In answering the question "do you think that most rank-and-file employees in your enterprise feel responsible for achieving organization's goals in 1987," all worker interviewees replied with "absolutely not at all." It seemed that the willingness of the worker interviewees to actively participate in management was quite strong, but the CEO rejected the idea.

In 1988 the workers of Enterprise H successfully removed the CEO. As mentioned in chapter 4, Gorbachev's policy of workplace democracy took effect in January 1988, and the policy gave workers the right to elect their managers. The workers of enterprise H took this opportunity to elect a new managerial team and replace the old one. When being interviewed, H2 said: "In terms of the goal of Gorbachev's policy I regard it as negative. But in terms of electing managers I regard it all right, as we had a successful election of managers. Only thanks for the

efforts we have survived." H3 so expressed: "I greeted this policy because the elected managers are more responsible." H4 replied: "Electing deserving managers makes things better."

Enterprise H was actually a pioneer in enterprise reform. The worker interviewees considered the privatization of their enterprise started in 1990 before the Soviet Union collapsed, much earlier than the nationwide voucher privatization. In November 1989 the Soviet government issued a decree to allow workers to lease their SOE. In 1990 the managers and employees of enterprise H decided to lease their enterprise. The worker interviewees reported that after the enterprise was leased by workers collectively, some changes took place. For instance, managers increased workers' wage and made its amount much higher than that of other enterprises, they shared more information with workers than in the past, and often listened to workers' ideas and opinions. However, workers remained as passive they were as before, they could not participate in discussion about important decisions of the enterprise as managers thought workers' approval was neither important nor necessary.

During the voucher privatization process the enterprise was privatized by insiders. Since then the rank-and-file workers held 98 percent of the shares and managers~~,~~—two percent. After privatization, all shares have been kept by insiders; none were sold to outsiders, and managers had not bought shares from the employee-owners. H1 felt that if managers had got more shares, they would have not obtained more authority in the enterprise. The enterprise was registered in June 1994 as a joint stock company named *Moscowvskaya Oboynaya Fabrika* (the Moscow Wallpaper Factory). After the privatization the board of directors of the enterprise included only insiders: a CEO, four chief engineers, and three representatives of employee owners. All interviewees in

enterprise H positively evaluated the results of the privatization. Although the manager interviewee thought that the shareholders' congress of the enterprise played only some role in making the most important decisions, the three worker interviewees all fully agreed that, being shareholders of their enterprise, they felt themselves one of the real controllers of the enterprise. H4 told that "workers possessing stocks show their participation in decision of some problems." While enjoyed their rights, the worker interviewees also expressed their satisfaction with benefits from the privatization. They thought that holding shares of their enterprise was very important to keep their jobs in the organization, and their personal situation in the enterprise was greatly or somewhat improved. H2 said that "we are paid very good dividends"; and H3 said, "privatization is a good process with good dividends as we have." The author would like to point out that, while the employee owners received certain amount of dividends for their investment, the monetary incentive of wage-increase practice adopted by the managers from 1988 to 1992 was somehow reduced after the voucher privatization, as workers' wage amount remained the same as that in other privatized enterprises, partly because of the difficulties in Russia's transitional recession.

According to the interviewees, if the situation of the enterprise in 1997 was compared with that in 1992 prior to the voucher privatization, a lot of positive changes occurred, and workers' attitudes towards managers and the management-worker relations at the workplace dramatically changed. First of all, both managers and workers changed their attitudes towards the enterprise. For instance, H1, the manager interviewee said that managers should make more efforts to work and their efforts rather than that of workers were more needed; and H2 said that, in order to improve efficiency of their enterprise, both the efforts of workers and managers were needed,

while managers should be intelligent and keep competent governance. According to H1, after the privatization most managers became very much responsible for achieving organization's goals, much better than did in the period from 1988 to 1992, and the worker interviewees fully agreed with that. H2 and H3 felt that workers had also become more engaged in achieving organizational goals, whereas in 1992 they did not feel responsible for that at all.

Second, in enterprise H, leadership climate changed and workers showed quite high expectations of their managers. While both the managers interviewee and the workers interviewed agreed that, before the privatization, even if workers perceived managers' behavior as inappropriate, the authority of the managers was not weakened at all， whereas in 1997 the interviewees all thought that, if the behavior of a manager was perceived to be inappropriate, the authority of the manager would certainly be weakened. At the same time, H2 and H4 thought that, after the privatization, in the enterprise if a manager wanted to exercise authority over his subordinates effectively he should behave properly in accordance with moral standard, and H1 agreed with the point, whereas in 1992 the worker interviewees did not feel managers to be as restrained. Moreover, all interviewees thought in 1997 that managers should take care of their workers. H1 explained that "better psychological climate in the working collective assists better work," and the worker interviewees thought that only when managers supported their workers by providing a normal life would workers work hard and better.

Third, interaction and communication between managers and workers significantly improved. Interestingly, H1 admitted that the managers of enterprise H in 1997 actually were "very unwilling" to share information with workers. He believed that only technical intellect,

rather than the initiative of workers, would be able to raise labor productivity and profit. At the same time, he recognized that after privatization it became important to know workers' ideas and opinions and to get approval of workers on important matters before going ahead; and the worker interviewees all thought so. Indeed, the worker interviewees reported that after the privatization managers often shared information in terms of achieving organization's objectives with workers, and workers were no longer in a passive mode and had shown their initiatives to implement organizational goal, and such enthusiasm was encouraged by managers. They often made suggestions or proposals for achieving organization's goal to top managers, and most of their suggestions or proposals were accepted by managers. The worker interviewees admitted that they frequently participated in discussion and decision of productivity problems at branch or workshop. Nevertheless, in terms of workers' participation in management, evaluations between the manager interviewee and worker interviewees were different, while the former thought workers already more or less participated in management, the latter did not think so.

Fourth, managers further implemented the merit-based management than before. In 1997 both the manager and worker interviewees reported that rewards and punishment were used more often than in 1992, while any employee with ability and willingness to work hard had better chance of being successful than in 1992, and only those who worked poorly were laid off. H1 told that in 1997 employees were checked more often on for rule violations than in 1992. While the worker interviewees mentioned that they always worked very hard, their satisfaction with their jobs became a little bit less than in 1992, as their regular wage amount was no longer higher than the average level in other enterprises as it once was in 1992. Therefore, both H1 (manager) and the

worker interviewees (H2 and H3) recognized that in 1997 if the enterprise wanted to further stimulate workers' motivation, it needed to pay "higher wage" or "increase material guarantee."

Fifth, after the privatization the managers in enterprise H made efforts to improve management-worker relationship; however, the perceptions of managers and workers regarding the management-worker relationship were seemingly different. H1 admitted that, while in 1992 his management task could be satisfactorily carried out without good personal relations with workers, in 1997, without such relations, his task might be done "badly somehow"; consequently, all the worker interviewees reported that, besides the regular working relations, the personalized friendliness between managers and workers had somewhat developed after the privatization. In 1997, while the trust and confidence of the worker interviewees in their shop floor leaders remained the same as in 1992, their trust and confidence in CEO greatly increased. On the other hand, the improved personalized friendliness between managers and workers and the trust of workers in CEO by no means implied there would be fewer labor conflicts at the workplace than before. Actually, while the employee-owners felt free to address their requests such as wage increase, conflicts between management and workers might still appear. The worker interviewees reported that such conflicts very rarely occurred in 1992, but happened sometimes in 1997; and the manager interviewee considered the conflicts took place quite often in 1997. H1 explained that the main reasons of the conflicts included "level of wage, expansion of productive duties and workers' all purposes;" H2 said that the conflicts occurred when "injustice arose from distributing dwellings;" H3 also expressed that "conflicts arise from level of wage and receipt of dwelling;" but H4 reported that there were "only little conflicts, and everything is held at the workplace of

workers." It seemed that the conflicts had only minimal impact on workers' satisfaction with the work of the CEO and their workshop leaders, while the worker interviewees reported that the majority of workers were fully satisfied with their workshop leaders and were fully or almost fully satisfied with the performance of the CEO. By contrast, in 1992 the three worker interviewees were not satisfied with the work of their CEO at all. While asked the overall relations between managers and workers at the workplace, all the worker interviewees agreed that the relations were better in 1997 than in 1992; but the manager interviewee perceived it worse in 1997 than in 1992. Very likely, it was really harder for a manager to handle the management-worker relations in 1997 than in 1992.

The management-worker relationship in the Soviet Union had a double face: a long-term tension between the two parties regarding working relations and a family-like interaction between them under a paternalistic culture. The paternalism was usually perceived by Russia scholars in two aspects: maintaining the existing working collective[69] and keeping non-wage social benefits (housing, health care, facilities for sport and rest, child care, food parcels and so on).[70] What did workers and managers of enterprise H think about the paternalism practices? According to the interviewees, from 1987 to 1992 both the manager and worker interviewees believed it was important that employees got help in solving their personal problems so that the goals of their enterprise could be achieved; but their opinions differed in 1997. While the worker interviewees still thought the same, H1, the manager interviewee, saw it differently. As mentioned above, the

[69] Peter Rutland, "Firms Trapped between the Past and the Future," *Transition*, Mar. 22, 1996, 30.

[70] Linda Cook, and Vladimir E. Gimpenson, "Exit and Voice in Russian Managers' Privatization Strategies," *Communist Economies & Economic Transformation*, Vol.7, No.4, 1995, 475.

enterprise acquired some apartments for employees after privatization; in other words, some practices of the paternalism remained at the workplace. The workers could raise such demands and press the management to meet them, and the labor union of the enterprise has been quite active in representing workers' interests.

During the transition recession, the enterprise experienced a very difficult economic situation. In 1987 it employed 500 people; the number was reduced to 450 in 1992. After privatization its employees were further reduced to 280 in 1997. In one workshop workers were reduced from 80 in 1992 to 40 in 1997, in another it was from 40 to 20 and in the third one, from 70 to 40. Since then the enterprise greatly improved competitiveness of its products. It developed the first brand of ecologically clean wallpaper in Russia. In 2000 and 2002, its products were selected for the All-Russia Top 100 Better Goods Show and for international exhibitions as well. The products have been used in several well-known museums in Moscow and Saint Petersburg, and in the museums of France and Beijing as well. Obviously, the enterprise has made a lot of accomplishments after privatization.[71]

Having analyzed the case the author would like to suggest several points. First, during the process of an insider's privatization, when managers occupy the majority seats in the board of directors, they may include representatives of employee owners in the board and have regards to the rights of the employee owners. While doing so, managers' value orientation might play an important role. Second, in a privatized enterprise fully controlled by insiders, corporate governance could be built both by manager's practices in accordance with the regulations of

[71] See website of the enterprise (http://corprussia.com/company/0632189)

company law and other legal requirements and by consensus between workers and managers about the rights of the majority of shareholders (98 percent of the shares of enterprise H were owned by employees and the managers did not obtain the shares from workers). Third, through control over the workplace, efforts to improve interaction and communication with workers, and keeping behavior and moral appropriate, managers would be able to develop a cooperative management-worker relationship; and employee-owners could be quite satisfied with their managers and may perceive the management-worker relationship better than ever.

The case suggests that a cooperative management-worker relationship could grow in a privatized firm where the socialism idea of workplace democracy was embraced by workers and supported by managers—a phenomenon that has yet to catch the attention of scholars in the field of Soviet/Russia studies. The author noticed that, among the eleven interviewed enterprises, some characteristics of enterprise H could also be found in enterprise G (will be further discussed below). This implies that the case of enterprise H might not be an isolated one in Russia.

4. Authoritarian Management-Worker Relationship after Privatization

In the eleven enterprises studied, only enterprise B was fully owned by managers, all other were partially owned by employees. The situation in enterprise H has already been analyzed, this section will look at the ten other enterprises (A-G, I, J and K).[72] Though the size, products and the

[72] All the information about the enterprises and opinions from interviewees are cited from my questionnaire No.1 to No.28, and No. 33 to No.44.

portion of shares owned by employees varied among these enterprises (see Table 6-7), there was one thing in common: the rights of the employees were disrespected (see Table 6-8).

Table 6-7 Employee Shares

Industrial Sector	Firm Size		
	Small	Medium	Large
Manufacture of measuring instruments	A (<15)	…	…
Manufacture of communication equipments and components	I (10)	B (0)	…
Manufacture of transportation Equipments	…	…	*C* (<50), D (98)
Food production	…	*E* (55)	**G** (29)
Textile industry	K (43)	F (<60)	…
Printing	J (30)	…	…

Note: Letters in the form represent interviewed enterprises. The numbers in parentheses are the percentage of shares held by employees. The bold letter means representatives of employee shareholders joined the board of directors. The latter in italic means that outsider board members occupy more than 40 percent of seats in the board of directors. According to their employment numbers in 1997, those enterprises with employees no more than 400 are listed as small, those with employees between 401 to 999 are listed as medium size, and those with 1,000 or more are listed as large. Detailed information is listed in Table A-1.

Source: My questionnaire No.1, No.5, No. 9, No.13, No.17, No.21, No.25, No.33, No.37, and No.41. The table includes the information of ten enterprises.

Table 6-8 Workers' Attitudes

Attitude towards Workplace Democracy	Attitudes towards Employee Ownership			
	Employee owners' rights were regarded	Employee owners' right were ignored	Shares obtained by managers or sold to others	Hard to Answer, not answered
Support the Idea	…	C2, C3, C4, D2, D3, D4, F2, G3, G4, J2, K4	B3, I4,	…
Electing Manager is not a Good Idea	…	E4, J4,	…	G2
It was not Really Practiced at the Workplace	…	A2, A4, K2	A3	…
The Result of the Policy was not Good	I2	E2, F4, I3, J3,	B2	…
Hard to Answer or Didn't Answer	…	E3, F3, K3	B4	…

Note: The Interviewees answered two questions: 1. "How do you evaluate Gorbachev's policy of workplace democracy? Do you think that this reform effectively improved the performance of your enterprise? Why?" 2. "Do you think that the employee ownership through privatization has given workers more rights, power and advantages? Why?"

Source: My questionnaire No.2, No.3, No.4, No.6, No.7, No.8, No.10, No.11, No.12, No.14, No.15, No.16, No.18, No.19, No.20, No.22, No.23, No.24, No.26, No.27, No.28, No.34, No.35, No.36, No.38, No.39, No.40, No.42, No.43 and No.44. Number of worker interviewees in ten enterprises = 30.

In the enterprises four types of insider owner's role could be identified.

First, managers obtained shares from workers and became exclusive owners of their enterprise. This took place in enterprise B, where workers used vouchers to buy shares of their enterprise, which were sold to their managers as they were subsequently requested. That was a medium-sized company which, in all likelihood, the managers used the funds of the enterprise or bank loans to the enterprise to buy the shares from workers, because managers' personal financial

assets were usually insufficient to cover the investment needed for the takeover.

Second, the rights of employee shareholders who held a large portion of shares were ignored, but outsider investors with much less shares could sit in the board of directors. Among the enterprises, enterprise C and E were the only two companies where more than 40 percent of seats of the board of directors were taken by outsider board members. In enterprise E all outsider owners were individuals who held only fifteen percent of shares in total, whereas employee shareholders held 55 percent, and managers, 30 percent. In enterprise C, outsider individuals and organizations held 30 percent of shares, but managers and employees together held 50 percent. Obviously, it is managers' purposive action, rather than the larger portion of shares held by outside owners, that has reduced the role of employee shareholders in the two enterprises. The worker interviewees of the two enterprises were quite dissatisfied with the consequence. For example, E2 said that "the stocks offered us nothing, except lip service."

Third, no matter how many shares employees possessed, there were either zero employee-shareholder representatives in the board of directors, or the board was poorly operated (enterprise A). The managers of enterprise D, F, I, J and K all took measures to exclude representatives of employee shareholders from the board of directors. While in enterprise F managers and workers held 60 percent of shares and in enterprise K workers held 43 percent, the situation in enterprise D could be seen as an extreme case where workers had 98 percent of shares but had no representatives in the board. Thus all worker interviewees in the six enterprises, except I2, said that employee ownership in their enterprises offered them no rights or advantages.

Fourth, representatives of employee owners had seats in the board of directors but they could

play only a small role. Among the enterprises, enterprise G was the only company which had representatives of employee shareholders in its board of directors. When answering the question "do you think that the employee ownership through privatization has given workers more rights, power and advantages, and why," G4 said, "Workers didn't receive more rights. I agree with the idea that workers are supposed to gain advantages. But only a small group of people became rich." And G3 explained that "to be a recipient of advantages, one needs protégé." The answers implied that only manager owners with protégé in the enterprise have benefited from the insider ownership.

The four types of consequences of privatization reflected what Gurkov and Maital had observed: "In the workers' view, privatization has not changed anything in their position; their newly acquired shareholders' rights remain an illusion."[73] While workers were disappointed with the results of insider's privatization, a lot of them seemingly showed a strong desire to play an active role as employees, as could be observed from their attitudes towards the workplace democracy policy (see Table 6-8). In 30 respondents of the ten enterprises, 26 answered the question, "how do you evaluate Gorbachev's policy of workplace democracy, do you think that this reform effectively improved the performance of your enterprise, and why?" The worker interviewees in enterprise C and D, and F2, G3, G4, J2, and K4 of enterprise F, G, J and K all liked the idea of workplace democracy; K2 and all the three worker interviewees in enterprise A supported the policy but regretted that it was not really implemented in their enterprises. The value

[73] Igor Gurkov, and Shlomo Maital, "Perceived Control and Performance in Russian Privatized Enterprises: Western Implications," *European Management Journal*, Vol.14, No.2, April 1996, 161.

orientation suggested that the workers care about the performance of their managers.

How did the managers do their job after privatization? From the viewpoint of Lawrence and Vlachoutsicos, the management style of Russian managers rooted deeply in the resilient culture of the Russian work community (*mir*), i.e. they were often strong personal leaders who practiced hands-on, walk-around, face-to-face management, and sometimes strong, top-down authority in making final decisions.[74] Some scholars thought that, in Russia "the principles underlying work organization in the socialist period had been theoretically those of Taylorism… The same Taylorist principles were followed during the transition."[75] Observing if evaluation of employees' performance was based on rules, regulations and records, or personal assessment of superiors,[76] the author found that among the enterprises, only three of them (F, G, I) have kept written record of everyone's job performance from 1987 to 1997; four of them (A-D) had never had such record, enterprise J stopped doing so after privatization, and two others (E, K) did not maintain a stable policy regarding the issue. Among the enterprises which had no regular record of employee's job performance, some are quite large (e.g. enterprise C and D). Without a record of employees' performance, particularly when the enterprises are large enough, evaluation of individual job performance could hardly be done by objective criterions; consequently, such evaluation would have to rely upon superiors' personal impression. Moreover, some managers paid no attention to employee's violation of rules. Of the enterprises, two (C and K) never conducted such assessment;

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[74] Paul Lawrence, and Charalambos Vlachoutsicos, "Joint Ventures in Russia: Put the Locals in Charge," *Harvard Business Review*, Vol.71, Jan.-Feb., 1993, No.1, 45.

[75] Roderick Martin, *Transforming Management in Central and Eastern Europe*, 114.

[76] The question is: "Does your enterprise keep a written record of everybody's job performance in 1987, 1992, and now?"

eight other carried it out routinely, yet in enterprises A and E the inspection became looser after privatization.[77] The worker interviewees in enterprise A, B, C, E, F and K also reported that rewards and punishment were used less frequent after privatization,[78] the worker interviewees in enterprise A, B, D, F, G, I, and K said that the workers with ability and willingness to work hard had fewer chances of being successful in the enterprises after privatization than before or had no chance at all,[79] and those in enterprises A, B, E and F thought their company's lay-off policy was carried out not based upon merit and those who were laid off did not really work poorly. It might be fair to say that management in those enterprises remained rough and far away from modern management methods based on rules, regulations and records.

After privatization, managers' autonomy increased in many enterprises. For instance, managers of seven enterprises (B, C, D, E, G, J, K) said that in 1997 they could make decisions without checking with anybody else,[80] among them enterprise C, G, J and K had more than 30 percent of shares in the hands of outsider owners; but managers of three enterprises (A, F and I) which had large outsider owners said that their autonomy in decision making decreased after privatization. The increased autonomy of the seven enterprises implied that government intervention in enterprises reduced drastically, and the large outsider owners did not necessarily

[77] The question is: "Are employees in your enterprise constantly checked on for rule violations in 1987, 1992, and now?"

[78] The question is: "Do you think that in your enterprise both punishment and rewards are used to influence employees' motivation, in 1987, 1992 and now?"

[79] The question is: "Do you think that any man with ability and willingness to work hard has a good chance of being successful in you enterprise in 1987, 1992 and now?"

[80] The question is: "Do you feel that a manager here can make his own decisions without checking with anybody else in 1987, 1992 and now?"

play active role to oversee managers. On the other hand, manager's autonomy was reinforced by the reducing role of labor unions. When asked about the role change of labor union before and after privatization,[81] the manager interviewees of three companies (B, C and F) replied that the labor union in their enterprises had been inactive since 1987, and in two companies (A and E) the role of labor unions was reduced from 1987 to 1997; in firm G, the manager interviewee said the labor union at the workplace remained very active, but worker interviewees said it has been weakened; moreover, in three enterprise (I, J and K), labor union was even dissolved after privatization (see Table A-3 in appendix). After the increase in their autonomy, some managers became very responsible in carrying out their duties, but others were not (see Table A-4 in appendix).[82]

Based on the interview data gathered, the author would like to point out that, as the managers have gained quite large autonomy and have gotten rid off the labor union, and the board of directors is often dominated by CEOs, who would in every probability become the real kings of their territories. Obviously, Russian workers had not united at the workplace to fight for their rights as owners of their enterprise; on the contrary, a lot of worker interviewees reported that the ties between workers became worse after privatization (see Table A-6 in appendix), and they passively waited for the rights to be offered by their managers. If their managers don't want to do so, then

[81] The question is: "Do you think that labor union in your enterprise is helpful for the performance of the enterprise, now and in 1987 and 1992?"

[82] The question is: "Do you think that most managerial personnel in your enterprise feel responsibility for achieving organization's goals, in 1987, 1992, and now?" The managers of enterprise F, G and K were thought by the interviewees in their enterprises always responsible; the managers of enterprise C and D became more responsible after privatization than before; the manager interviewees of enterprise B, E, and J thought they were either always responsible or became more responsible after privatization, but workers didn't think so; the managers of enterprise I became less responsible after privatization.

workers' ownership would very likely become symbolic. The phenomenon has also been found elsewhere. When Russell did his interview at a firm in Russia, he was told by two managers that they did not encourage their worker shareholders to be involved in managerial decision making at shareholder meeting, on board, or anywhere else. "They want their employees to view ownership as an incentive, not as a source of power."[83] Krueger also quoted in his 1995 interview in Russia the comment of a manager that workers cared only about salary, they would never become owners; the more shares the management owned, the more efficient his enterprise would be. A year later the manager said: "[P]rivatization is not very effective, workers don't understand the implications of business decisions…workers are really outsiders, they never cause any problems with management or the board of directors."[84]

As managers dominated their enterprises after privatization, how did they reconfigure management-worker relationship, and would the new relationship help improve performance of their firms? Krueger reported that before privatization factory directors went to shop-floor every day and any worker could go up to him and raise questions; but after privatization direct contacts between the directors and workers were reduced. An obvious sign of the change was the "termination of the practice of 'going to the people' and direct dialogue with ordinary workers."[85] My interviews focused on the issue, and found that after privatization most managers kept workers at a distance and often did not care about what workers thought and felt. When asked "do you think

[83] Raymond Russell, "Ownership and Employment in the New Russian Economy," manuscript, Jan. 10, 1996.

[84] Gary Krueger, *Enterprise Restructuring and the Role of Managers in Russia: Case Studies of Firms in Transition*, Armonk, NY, M. E. Sharpe, 2004, 101.

[85] Veronika Kabalina, Galina Monousava, and Valentina Vedeneeva, "Lenkon: Capitalism and Scientology," in Simon Clarke ed. *The Russian Enterprise in Transition: Case Studies*, UK, Edward Elgar, 1996, 233 and 236.

that it's important to get approval of the work group on important matters before going ahead," eight manager interviewees (A1, B1, C1, D1, F1, G1, J1 and K1) said they did not think so after privatization, and two (E1 and I1) thought in 1997 it became less important than before; but in their enterprises the worker interviewees either perceived the issue in an opposite way or reported that workers were not consulted at all when decisions on important matters were made. After privatization, some managers (A1, D1, E1 and I1) admitted that they declined to share with workers information on achieving organization's objectives, and some said they did share the information (B1, F1, J1, K1) but their workers often disagreed with that; on the other hand, a lot of manager interviewees (C1, D1, E1, F1, G1 and I1) thought interaction and communication aimed at achieving organization's objectives between management and workers either did not exist at the workplace or became less often after privatization, while B1 said he did maintain interaction with subordinates, the worker interviewees in his enterprise said that was not the case at all (see Table A-5 in appendix).

Whether workers had the initiative to make suggestions or proposals to managers was a traditional assessment in the Soviet workplace studies about management and worker's participation. Russian managers often denied that their workers lacked the initiative; however, after privatization when workers became owners, only worker interviewees of enterprise D and G stated that they still had the initiative, a lot of those of other enterprises said they no longer had the initiative or did not want to do that any more. While evaluating management-worker relationship, a lot of worker interviewees were quite cautious, but six manager interviewees (A1, B1, D1, E1, I1 and K1) frankly admitted that the relationship got worse after privatization; C1 refused to answer;

only G1 and J1 said the relationship was improved, but some of the worker interviewees in their enterprises disagreed (see Table A-6 in appendix). Beyond the regular working relations between managers and workers, the personal relations between the two parties in the enterprises, too, worsened after privatization, although a lot of manager interviewees (A1, B1, F1, G1, J1 and K1) admitted that, without good personal relations with subordinates, their management tasks could hardly be satisfactorily carried out.[86]

Given that workers' rights both as labor and owners were not respected, communication between managers and workers had largely been reduced, and the relationship between both sides worsened in the enterprises, how did the social atmosphere affect workers' working attitude and motivation? My findings can be depicted from several dimensions. First, in all the interviewed enterprises, there were worker interviewees reported that they longer reached the target of their job after privatization. Second, in nine enterprises some worker interviewees mentioned that most workers in their enterprises became less responsible for achieving organization's goals in 1997, while the worker interviewees of enterprise E did not say so, the manager interviewee affirmed that. Third, after they had become shareholders of their enterprises, the worker interviewees in enterprise A, B, E, F, G, I, and K either felt that their situation within the organization had not been improved or became worse. Fourth, all the worker interviewees except G2 reported that after privatization they either didn't work better or worked even worse than before (see Table A-7 in appendix).

[86] The question is: "How much can your management task be well carried if without good personal relations with subordinates in 1987, 1992, and now?"

The decline of workers' working motivation after privatization in Russia had caused attention of researchers. Schwartz points out that "many enterprises have been facing considerably more significant problems of motivation than during the Soviet period."[87] But previous literature rarely analyzes why workers' working motivation declined after privatization. The results of my interviews provided some clues to understanding the problem. Analysis of the factors affecting worker's working motivation (see Table A-8 in appendix) revealed the amount of wage affected the working motivation of most of the worker interviewees in all enterprises. When asked an open-ended question "in your opinion, how can workers have more working motivation," the worker interviewees in enterprise B, C, D, E, F, G, I, J and K replied with "higher and stable wage," but some of them were dissatisfied with managers' poor organization of production and labor (A3, A4 and F4), and A2 and B2 expressed that they declined to work for the current boss and would rather work for themselves or for working collective.

Moreover, two phenomena shown in Table A-8 are worth noticing. When asked if their social status at the workplace would affect their working motivation, many of the worker interviewees said Yes for 1987 and 1992; but for 1997, interviewees of enterprises A, B, C, E, F, I, J, K chose a special answer: "our social status at the workplace in 1997 was too low,"[88] while no one said so of their status in 1987 and 1992. The phenomenon could be seen as a reflection of workers' strong

[87] Gregory Schwarz, "The Social Organization of the Russian Industrial Enterprise in the Period of Transition," in Leo McCann, ed. *Russian Transformations: Challenging the Global Narrative*, London & New York, Routledge Curzon, 2004, 82.

[88] When designed the questionnaire, I didn't give this special answer as an option; but my Russian collaborators in Vox Pupuli thought adding such an option was necessary as they better knew opinion changes of Russian workers. Ultimately, in my interviews most worker interviewees chose this special answer.

discontent with their post-privatization social status at the workplace. By raising the issue when answering a question about working motivation, the worker interviewees actually implied that the discontent did negatively affect their working motivation. Another phenomenon is that at enterprise B, D, E, F, I, J and K the weakened trust of the worker interviewees in CEO negatively affected their motivation in 1997 (see Table 6-9). The two phenomena were interrelated and will be explored further.

Table 6-9 Trust in CEO and Workers' Working Motivation

If Trust in CEO Affect Working Motivation	Trust and Confidence in CEO			
	More Trust in 1997 than 1992	Less Trust In 1997 than 1992	Same as Before	Hard to Answer or Not Answered
Fully or somewhat Affect	C2, C4, G2, G3	B2, B3, D2, D3, D4, E2, F3, F4, I3, I4, J2, K3	E3, K2	C3, G4, J4
Not affect	…	A2, A3, A4, B4, E4	J3	I2
Hard to answer	…	K4	…	F2

Note: The Interviewees answered the following questions: 1. "Do you think that the trust and confidence in the General Director of your enterprise can influence your working motivation, in 1987, 1992 and now?" 2. "How is satisfying of the majority of workers at your workshop with the work of general director of your enterprise in 1987, 1992 and now?"
Source: My questionnaires. Number of worker interviewees = 30.

Before privatization, workers' trust and confidence in the general director was not an important factor affecting workers' working motivation, because in the Soviet era general directors were appointed by the party-state and workers were not at the position to appraise the appointments. Under the Soviet system, both managers and workers were defined by the official

propaganda machine as state employees with labor divisions, and nominally they were "comrades." Privatization completely altered the social status of the workers and the managers. When most enterprises were restructured through insider's privatization and most workers obtained shares of their own enterprises, the transition of workers from "comrade-working fellows" to "employee-shareholder" was supposed to improve their social status at the workplace. On the other hand, the social status transition of top managers from the "comrade-leaders" to CEO had involved in a lot of questionable approaches including asset stripping, which might undermine the image of CEO in workers' mind. Moreover, after privatization a lot of CEOs of privatized firms felt they were eventually free from state intervention and oversight of outsider investors, as well as potential pressure from the labor union, and no longer cared if the management-worker relationship at the workplace had worsened. Thus many worker interviewees felt after privatization their social status became even lower than before--an impression that would certainly have reduced workers' trust and confidence in CEOs. No matter whether the managers care about workers' rights and views or not, workers are concerned if the actions of managers are acceptable within the social norms, values and beliefs.[89] It was found that after privatization employees of all enterprises included in the case study paid attention to their managers' immoral and inappropriate behaviors (see Table A-9 in appendix). For example, B3 said that their managers spent too much money on office building construction; I3 complained that the CEO was dishonest; and J2, a staffer at a small printing company stated that the CEO traveled abroad too many times at the

[89] Mark Suchman, "Managing Legitimacy: Strategies and Institutional Approaches," *Academy of Management Review*, Vol.20 (1995), No.3, 571-610.

firm's expense.[90] Most of the workers interviewed thought that the authority of top managers would be weakened when their behavior was perceived as inappropriate by workers (see Table A-9 in appendix). After privatization the worker interviewees in eight enterprises (A, B, D, E, F, I, J, and K) either reported that the majority of the workers in their enterprises became less satisfied with their CEO in 1997 than before, or simply said the workers were almost dissatisfied with their CEO after privatization (see Table A-6 in appendix).

As management-worker relationship worsened and workers became more dissatisfied with their CEOs, would there be more conflicts between the two sides? My interview data revealed that the tension between managers and workers did not necessarily lead to more conflicts. At enterprise D and J, the worker interviewees reported an increase in the conflicts between the two sides, but in enterprise A, E and I the conflicts decreased, while in other enterprises the worker interviewees had inconsistent views about that (see Table A-10 in appendix). When asked "[I]f there were conflicts between managers and workers in your enterprise, and what were the main reasons," the interviewees recounted different causes of the conflicts at each enterprise. In enterprise A, B, F, G, and I, the worker interviewees reported that the conflicts were mainly caused by issues such as low wage and late payment. The manager interviewees B1 and I1 admitted that, eventually, the conflicts were caused by wage problem, whereas A1 thought the low wage was the result of workers' poor job performance. At enterprise E, both the manager and workers said conflicts were caused by the absence of necessary volume of production. Wage disparity between managers and

[90] It was cited from the answers of questionnaire No.7, No.35 and No.39 to an open-ended question, "What are the most effective ways to cut costs in your enterprise?"

workers was also a reason of the conflicts at enterprise G and J. At enterprise F and J, dismissal and layoff also led to the conflicts.[91] It seems that conflicts were prone to occur when workers' minimum needs for survival were not met. However, the workers in these enterprises did not unite to fight for their rights. The reason for this will be discussed in the next section.

Another important issue should also be analyzed: whether or not the paternalistic culture remains after privatization and if the paternalistic practices lubricate or damage management-worker relationship. Interpretations in terms of managers' conduct of paternalistic practices vary. While some viewed such practices from the neo-classical economics perspective and believed they would hurt efficiency of privatized enterprises, others thought they were reasonable. For example, Brown argues: "The fact that the government's social safety net is minimal has intensified this feeling among Russian managers;" but he admitted that "much of the variation in the intensity of paternalism among managers is unexplained."[92] In terms of the importance of paternalism during and after privatization, some emphasize its role in reshaping management-worker relationship, but others consider it to be a tactical approach. For instance, Southworth suggests that a "neo-paternalistic authority" has emerged, as it "resembles traditional authority in that the director exercises personal control, staff and personnel are loyal to the management."[93] Cook and Gimpelson suggest that the paternalism practices were not simply

[91] The information was collected from the answers of questionnaire No.1 to No.28 and No.33 to No.44 to an open-ended question "If there were conflicts between managers and workers in your enterprise, what are the main reasons?"

[92] David Brown, "Excess Labour and Managerial Shortage: Findings from a Survey in St. Petersburg," *Europe-Asia Studies*, Vol.48, No.5, 1996, 817.

[93] Caleb Southworth, "The Development of Post-Soviet Neo-Paternalism in Two Enterprises in Bashkortostan:

results of rational choice of some managers, but might also have originated from their beliefs and values. They identified two different types of managerial paternalism: "Although many managers are sincere in their traditional paternalism, others do not share their beliefs. Nevertheless, they often accept the importance of populist promises as a rather important element of their rationally calculated privatization strategy. In such cases, broad advertisement of the director's 'care for workers' well-being' was used to garner workers support…as soon as the managers got full control over the enterprise they may start pitiless mass dismissals."[94] The two authors focus on the employment issue, but don't touch another important aspect of the paternalism-social benefits.

What did Russian managers and workers really think about the post-privatization paternalism practices? My interviews and the VCIOM data provided a lot of information to help understand why and how paternalism is alive. From the interviews it was found that all manager and worker interviewees agreed on the idea that managers should protect workers, but a few manager and worker interviewees no longer thought an enterprise should solve personal problems for employees (see Table A-11 in appendix).

Obviously, the workers firmly believed that they should be protected by the organization they worked for, and their morale would be influenced by managers' promises of workers protection. When explaining why managers should protect workers, the interviewees gave three different

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How Familial-Type Management Moves Firms and Workers away from Labor Markets," in Leo McCann, ed. *Russian Transformations: Challenging the Global Narrative*, London & New York, Routledge Curzon, 2004, 194.

[94] Linda Cook, and Vladimir E. Gimpenson, "Exit and Voice in Russian Managers' Privatization Strategies," 475-476.

reasons.[95] The first and the most cited reason was a rational consideration. The manager interviewee of enterprise E said: “Certainly. Joint efforts get success. Social warranties in the life of working collective appear to support production development.” A4 answered that managers should protect workers, as they were supposed to retain workers, otherwise all would fall down consequently. G2 said that naturally managers were supposed to do so, thus people’s relations would be more efficient. G3 said: “Of course he should take care of (workers), when relationship in working collective improves they will also stand behind the managers.” B2 explained that managers were obliged to do so; if he could not do it, production would be affected, and workers would react negatively. B3 said the same: “If he doesn’t do so, subordinates would not do their best.” And E4 agreed: “Certainly. If he would not support us, we would not support him.”

The second was a concern based on the perception of social relations in the workplace. The manager interviewee of enterprise G said: “Contemporary managers certainly should show that they care for their subordinates, and see working collective and management as family, working together for the interest of their own enterprise.” C4 said that managers “should take care of those working under the managers, as we all work in the same collective.” The manager interviewee of enterprise I thought that, because workers were used to be taken care of and they now had some power at the workplace, managers should protect them. G4 believed that, managers should defend employees as they were owners. A3 considered the issue from the viewpoint of Marxism: managers should protect workers, “because we feed all of them.” The manager interviewee of

[95] The interviewees answered a question “do you think that managers should protect workers of their enterprise and why.” The answers cited below are selected from questionnaire No.3, No.4, No.5, No.6, No.7, No.9, No.12, No.15, No.17, No.18, No.20, No.25, No.26, No.27, No.28, No.40 and No.41.

enterprise C perceived it to be a manager's social obligation: "Certainly, so long as the governmental social protection is absent, this duty lies with the enterprise." And D3 saw the protection a favor of managers for workers.

The third concern was a moral one. B1 said that protecting workers was exactly the administrative and moral duty for managers. While the second and third concern might be the legacy of the paternalism culture, the first concern may not necessarily be related to that.

From the answers of the worker interviewees it could be found that most managers took some measures to protect workers' jobs. For example, A3 said that in his enterprise many redundant workers were retained, and J4 said those non-productive workers in his enterprise should have been dismissed. Practices hurting workers' well-being were also reported. For instance, in enterprise G, G3 mentioned that wage payment was often delayed, and G4 told that workers were dismissed for trivial mistakes, and working hours were extended without compensations. The manager interviewee of enterprise K said that, although he thought managers should protect workers, such measures were not available at his enterprise. E2 reported that at his enterprise managers did not do that either.

My interviews did not cover details of available fringe benefits from the workplace, but the VCIOM data could provide a nationwide picture about that (see Table 6-10). According to the surveys of the VCIOM, during and after the privatization process, real measures of worker protection shrank noticeably, and one-fourth of the survey respondents reported events of massive dismissal (the topic will be discussed more deeply in the next section), and about 60 percent of them reported that they didn't really receive any fringe benefits and the other 40 percent of them

mentioned that they received some goods and food at reduced prices, financial assistance, and free or cheap catering (see Table 6-10).

Table 6-10. Fringe Benefits Received

Types of Fringe Benefits	4/93 (%)	8/93 (%)	12/93 (%)	9/94 (%)
Housing accommodation	4	2	3	2
Paying and arranging vacations for adults and children	5	7	4	4
Paying medical treatment	10	8	8	7
Free catering (or at a reduced price)	14	9	9	7
Purchasing goods and food at reduced prices	21	13	20	9
Refreshment, additional training	6	4	4	3
Financial assistance in difficult life situations	14	12	11	11
Other	6	1	1	1
None	…	56	52	59
Hard to answer	31	5	7	8
Not answered	13	0	0	0

Note: The table is complied with the VCIOM data. The question is: "What specific assistance did you get from your enterprise (company, organization) during the last six months?" (Multiple choice)
Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), Moscow, Russia, Aspect Press, No.3, 1993, 52, No.2, 1994, 76; No.6, 1994, 72. Sample size: Apr. 1993 survey, 1,827; Aug. 1993 survey, 1,805; Dec. 1993 survey, 1,799; Sept. 1994 survey, 1,700.

Compared with the Soviet paternalistic practices, the range and scale of social protection for workers from the workplace became much smaller. As Bizyukov pointed out, "Very few enterprises are able to carry out a strong paternalistic policy. The majority of the enterprises fall

into the category of those who are able to carry out a not very strong paternalistic policy… One can confidently assert that practically every director would like to carry out a strong paternalistic policy, but not all of them are able to go far."[96] In many privatized enterprises paternalism is seemingly no longer a solid pillar of management- worker relationship if one evaluates it from the material dimension, though its ideological legacy would remain influential for years to come and some paternalistic practices may appear here and there.

In the enterprises where the author conducted interviews, after privatization most manager and worker interviewees agreed that, in order to improve the productivity and profitability of their enterprises, managers must make more efforts than workers.[97] Some worker interviewees even pointed out tasks that their managers did not do well. For instance, B4 mentioned that their managers should do more to get orders and to arrange sales of products. At enterprise D, D2 said his managers should make efforts to control expenses of the enterprise; D3 told that the managers should economize all productive resources, and timely calculate spare parts; and D4 suggested that the managers should work hard to attract clients and organize advertisement. E2 criticized that the current leadership in his enterprise was not really needed, as "it only waited for what we have all run up." In enterprise I, I3 said that the workers of the firm needed smart and respectable managers,

[96] Petr Bizyukov, "The Mechanism of Paternalistic Management of the Enterprise: The Limits of Paternalism," in Simon Clarke, ed., *Management and Industry in Russia: Formal and Informal Relations in the Period of Transition*, Hants, England, Edward Elgar, 1995, 117-118.

[97] The interviewees answered two open-ended questions: 1. "Do you think that efforts of managers and workers can improve the current productivity and profitability of your enterprise? Whose effort is more important?" 2. "What are the most effective ways to cut costs in your enterprise?" The answers cited below are selected from questionnaire No.3, 4, 5, 6, 7, 8, 9, 12, 14, 15, 16, 17, 18, 20, 25, 26, 27, 28, 35, 36, 40, 41 and No.43.

and I4 said that the enterprise needed introduction of advanced technologies. And K3 mentioned that in his enterprise power resources should be economized. From the complaints one could find that the workers were not satisfied with the performance of their managers; however, the managers had consolidated their power and seemingly lacked interests in communication with and taking suggestions and proposals from their workers (see the last row of Table A-6 in appendix).

Table 6-11. Features of Ten Interviewed Enterprises

Features	Relatively Better	Relatively Poorer
1. Keep Written Record of Workers' Performance	F, G, I	A, B, C, D, E, J, K
2. Rewards and Punishment Used	D, G, I, J	A, B, C, E, F, K
3. Capable Workers Could Get Success	C, E, J	A, B, D, F, G, I, K
4. Rights of Employee Shareholders Ignored	…	A, B, C, D, E, F, G, I, J, K
5. Labor Union Still Work?	D, G	A, B, C, E, F, I, J, K
6. Get Approval of Workers on Important Matters	…	A, B, C, D, E, F, G, I, J, K
7. Share Information with Workers	C, G	A, B, D, E, F, I, J, K
8. Communication between Managers and Workers	J, K	A, B, C, D, E, F, G, I,
9. Workers have Initiative to Make Suggestions	D, G	A, B, C, E, F, I, J, K
10. Evaluation of Management-Worker Relationship	G	A, B, D, E, I, K
11. Workers are Satisfied with CEO	C, G	A, B, D, E, F, I, K
12. Workers Feel their Social Status Too Low at the Workplace	D, G	A, B, C, E, F, I, J, K
13. Workers Trust in CEO Weakened	C, G	A, B, D, E, F, I, J, K
14. Managers are Satisfying with their Enterprise	…	A, B, C, F, J, K

Source: My questionnaires. More details are listed in appendix.

To sum up the ten enterprises analyzed above, the author listed fourteen aspects in Table 6-11. While the first three aspects refer to management approaches, the other eleven aspects are all about management-worker relationship. According to the reported status of each enterprise, some enterprises were doing better than others in certain aspects, and some were doing poor in all the aspects listed in the table. Thus a group of seven enterprises (A, B, E, F, I, J and K) was identified to be showing similar characteristics: the management-worker relationship in these enterprises had been reported as poor in all eleven aspects or at least in ten aspects. The CEOs of these enterprises seemed to have used a more or less similar authoritarian management approach to control the firms, and didn't really care, or had no wishes to improve the management-worker relationship and avert its negative impact on the performance of the firms. The management-worker relationship in these enterprises might be called as a post-communism authoritarian pattern, which arose from the Soviet management practices,[98] and reflected in the value orientation of the managers towards employee ownership and Gorbachev's workplace democracy policy (see Table 6-6).

The other three enterprises (C, D and G) differed to some extent from this authoritarian pattern. The management-worker relationship in enterprise G, where managers and workers maintained a better relationship in seven out of eleven aspects, might be considered much better than that in the seven enterprises, and was somewhat close to enterprise H. Enterprise C and D were midway between enterprise G and the seven poorer enterprises.

[98] See Donald Filtzer, Soviet Workers and Stalinist Industrialization (London, Pluto, 1986) and Soviet Workers and Destalinisation (Cambridge, UK, Cambridge University Press, 1992), and Deborah A. Kaple, Dream of a Red Factory: The Legacy of High Stalinism in China (New York and Oxford, Oxford University Press, 1994).

If the cooperative pattern in enterprise H could be perceived as a model of cooperative management-worker relations, the authoritarian pattern reflected more noticeably the authoritarianism features of the Soviet enterprise culture. Taking the earlier discussion about corporate governance of the interviewed enterprises into consideration, one might find that the majority ownership of employee shareholders may not prevent an enterprise from being dominated by the top managers with a strong value orientation for authoritarianism, and the democratization process in Russia seemingly did not really help alter the unbalanced social relations between managers and workers at the workplace.

5. More Tension but Fewer Conflicts at the Workplace, Why?

From the interviews the author found that the poorer social relations at the workplace under an authoritarian management did not necessarily lead to more conflicts between managers and workers. Why did the workers in the enterprises not fight against the managers they were not satisfied with? Indeed, during and after privatization, the nationwide opinion survey data of the VCIOM revealed that, although worker's economic condition was very poor and their job security was under threat, conflicts between managers and workers had significantly decreased, strikes had been fairly short and limited, and appeared to be directed against the government rather than managers.[99] In 1993 when the privatization just began, 45 percent of the respondents reported conflicts between management and workers at their workplaces; as the privatization completed in

[99] Penny Morvant, and Peter Rutland, “Russian Workers Face the Market”, Transition, June 28, 1996, 6-11.

mid 1994, the percentage decreased to 30 percent, and further declined from 1995 to 2001 (see Table 6-12).

Table 6-12. Conflicts between Management and Workers

Time	Almost or Never Had Conflicts (%)	Often or Sometimes Had Conflicts (%)
4/1993	43	46
8/1993	49	45
12/1993	52	41
4/1994	50	37
9/1994	53	31
3/1995	55	28
6/2001	62	13

Note: The table is complied with VCIOM data. The question is: "Are there any conflicts between management and working collectives at your workplace?"
Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.3, 1993, 44, No.2, 1994, 75; No.4, 1994, 63; No.6, 1994, 70; No.3, 1995, 88; No.6, 2001, 88. Sample size: The Apr. 1993 survey, 1,818; the Aug. 1993 survey, 1,805; the Dec. 1993 survey, 1,799; the Apr. 1994 survey, 2,935; the Sept. 1994 survey, 2,959; the Mar. 1995 survey, 1,980; the June 2001 survey, 1,207.

The author carefully read the national opinion survey data of the VCIOM and found more details are worth analyzing. First, a lot of managers took serious steps not to lay off workers. For example, according to the VCIOM data, about fifteen to twenty percent of the respondents reported that their managers tried to transfer workers to part time work (see Table 6-13). Such measures reduced the possibility of conflicts at the workplace.

Table 6-13. Managers' Measures to Prevent Mass Redundancy Dismissal

Managers' Measures	3/93 (%)	9/94 (%)	3/95 (%)	1/96 (%)	1/97 (%)	1/2000 (%)	6/2001 (%)
Doing nothing of the kind	31	31	46	21	28	31	10
Transferring workers to part time work	15	18	19	14	19	11	18
Granting unpaid leaves	24	25	21	21	27	12	16
Creating commercial Structures for the staff	4	2	3	2	3	2	2
Helping find job at other Enterprises	4	4	6	2	4	3	3
Search new suppliers and markets	14	14	9	13	11	12	29
Retraining employees	…	…	…	…	…	5	6
Produce new Products	…	…	…	…	…	6	17
Other measures	2	1	2	1	1	1	1
Hard to answer or Not Answered	31	32	19	44	29	36	35

Note: The question is: "Is management of the enterprise where you work undertaking any measures to prevent mass redundancy?" (Multiple choice)
Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, No.6, 1994, 72; No.3, 1995, 79; No.2, 1996, 89-90; No.2, 1997, 87; No.2, 2000, 71; No.6, 2001, 87. Sample size: The Mar. 1993 survey, 1,999; the Sept. 1994 survey, 1,700; the Mar. 1995 survey, 1,980; the Jan. 1996 survey, 2,426; the Jan. 1997 survey, 1,258; the Jan. 2000 survey, 2,407; the June 2001 survey, 1,207.

Second, during the privatization period, the threat of large-scale layoffs was high (see Table 6-14). In order to form an alliance with workers against outsider investors, many managers told workers that "if outsiders buy the enterprise mass dismissal will be unavoidable."[100] While about 20 to 25 percent of the employee respondents of the VCIOM surveys reported that massive layoffs

[100] Linda Cook, and Vladimir E. Gimpenson, "Exit and Voice in Russian Managers' Privatization Strategies," 475.

occurred (see Table 6-14), only about three percent of them reported that conflicts at the workplace between management and workers were caused by the dismissal actions[101] (see Table 6-16). One may thus conclude that most dismissed workers did not involve in organized struggles against such actions.

Table 6-14. Massive Dismissal

Questions & Answers	4/93 (%)	5/94 (%)	3/95 (%)	1/96 (%)	1/97 (%)	9/97 (%)	6/2001 (%)
Threat of Large-scale Redundancy							
Yes	46	43	36	28	37	29	18
No	40	40	43	52	46	43	41
Hard to answer	13	16	21	20	17	23	41
Not answered	1	1	0	…	0	5	…
Total	100	100	100	100	100	100	100
Massive Reduction of Workers							
Yes	22	26	21	20	26	23	11
No	68	66	70	70	65	61	73
Hard to answer	9	7	8	10	9	11	16
Not answered	1	1	1	0	0	5	0
Total	100	100	100	100	100	100	100

Note: The question 1 is: "In your company, is there a threat of a significant reduction in the work force?" The question 2 is: "During the last three months, has there been in your company (organization) a massive reduction (letting go) of workers?"

Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No. 2, 1993, 63; No.6, 1993, 49; No.3, 1994, 54; No.4, 1994, 70; No.6, 1994, 71; No.3, 1995, 79; No.2, 1996, 89; No.6, 1997, 85; No.6, 2001, 87. Sample size: The April 1993 survey, 1,818; the May 1994 survey, 2,975; the Mar. 1995 survey, 1,980; the Jan. 1996 survey, 2,426; the Jan. 1997 survey, 1,258; the Sept. 1997 survey, 1,261; the Jan. 2000 survey, 2,407; the June 2001 survey, 1,207.

[101] About 30 percent of respondents reported conflicts between management and workers at the workplace, among them only about ten percent thought the conflicts were caused by large scale dismissal.

Table 6-15. Workers' Response to Layoff

Workers' Responses	4/93 (%)	5/94 (%)	9/94 (%)	3/95 (%)	1/96 (%)	1/97 (%)
Alienation among people has arisen, "everyone stands for Oneself"	29	27	26	32	19	20
Conflicts connected to struggle for keeping job have begun	22	20	20	24	14	16
People have begun to look for other jobs and leave not waiting for redundancy	30	29	38	37	26	22
Many people have begun trying to come closer to managers, gain their support	19	12	14	18	12	12
People have begun more Tolerably treat each other	8	3	5	7	4	6
The collective's solidarity has become greater	5	2	2	8	3	1
Collective actions against Dismissals are being organized	2	1	1	3	3	1
People began working better	…	7	6	14	8	5
Other	2	1	2	2	1	1
No impact at all	…	…	…	…	…	28
Hard to answer or Not Answered	31	35	31	20	43	29

Note: The question is: "How has the threat of redundancy and fears of losing job affected the behavior of people working in your collective?" (Multiple choice)
Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No. 2, 1993, 63, No.6, 1994, 76-77, No.3, 1995, 79, No.2, 1996, 89, No.2, 1997, 87. Sample size: The April 1993 survey, 1,827; the May 1994 survey, 2,975; the Sept. 1994 survey, 1,700; the May 1995 survey, 1,980; the Jan. 1996 survey, 2,426; the Jan. 1997 survey, 1,258.

The VIOCM surveys provided information about workers' response to layoff: about 20% to 30% of the respondents reported that alienation among workers had arisen, and only three to seven percent of them mentioned that people became more tolerant of each other; while about fourteen to

twenty percent of the respondents answered there were "conflicts connected to struggle for keeping job" at the workplaces, only one to eight percent admitted that "solidarity of working collective became greater", and only one to three percent reported that at their workplace there were organized collective actions against dismissals; at the same time, 22 to 38 percent of the respondents said that "people began to look for other jobs", and twelve to nineteen percent mentioned that people tried to go closer to managers in order to retain their jobs. Obviously, under the threat of dismissal, more Russian workers chose individual actions over collective struggle, and more looked for personal help from managers than organizing activities against managers (see Table 6-15). Such preference could explain why the worsened management-worker relationship did not lead to more organized conflicts at the workplace.

Third, the main causes of the conflicts between managers and workers were wage issue, poor working conditions or lack of work, and unlawful actions of managers and bad attitudes toward workers (see Table 6-16). The dissatisfaction of workers with their mangers regarding the wage issue might not lead to workers' organized collective actions. Christensen so described the situation at the workplace: "Workers are understandably wary of taking action against their enterprise administrations when so much depends on the enterprise… if they are officially laid off or if the enterprise goes under, they stand to lose their apartments, access to health care and pension rights… Finding a job locally, particularly one that actually pays wages on time, has become increasingly difficult."[102]

[102] Paul Christensen, "Why Russia Lacks a Labor Movement," *Transitions*, December, 1997, 46-47.

Table 6-16. Reasons of Management-Labor Conflicts

Reasons of Conflicts	4/93 (%)	8/93 (%)	12/93 (%)	4/94 (%)	9/94 (%)	3/95 (%)	6/2001 (%)
Unfair distribution of wages, and low level of wages	36	32	29	38	29	24	8
Late payment of wages	…	…	…	…	…	32	6
Lack of work, stoppage, non-Rhythmic work	…	…	…	14	12	10	4
Bad working conditions	13	25	19	14	12	11	1
Shortage of staffs	14	13	10	…	…	…	…
Danger of dismissal, enforced Leave, firing of personnel	…	…	…	13	9	8	4
Threat of bankruptcy	…	…	…	…	…	…	2
Non-profitable condition of enterprise shareholding	…	…	…	…	…	…	1
Distribution of social benefits	13	9	6	9	6	6	2
Personal causes	18	16	14	…	…	…	…
Unlawful actions of managers And bad attitude toward workers	18	15	16	19	15	14	…
Lack of work discipline	…	…	…	8	7	7	…
Privatization of the enterprise	5	2	2	2	2	1	…
Organizing commercial Structure within the enterprise	1	1	1	1	1	0	…
Other	2	2	1	4	3	2	1
Hard to answer	10	5	7	30	46	39	…
Not answered	2	2	0	7	0	0	87

Note: The question is: “What are the most frequent reasons of the management-worker conflicts?” (Multiple choice)

Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial’nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.3, 1993, 44, No.2, 1994, 75, No.3, 1995, 88, No.6, 2001, 89. Sample size: April 1993 survey, 1,818; Aug. 1993 survey, 1,805; Dec. 1993 survey, 1,799; April 1994 survey, 2,935; Sept. 1994 survey, 2,959; Mar. 1995 survey, 1,980; June 2001 survey, 1,207.

Indeed, no matter how workers were dissatisfied with their managers, if they were not confident in finding alternative jobs in transitional recession, then their current workplace could be the only hope for survival, and workers were left at a weaker position in labor relations. Through interviews, the author found that, before privatization (in 1987), workers were "somewhat not bothered" or "not bothered at all" if they might not be able to find a full-time job once they left the current workplace, and were "fully or almost confident" to find a better full time job; however, after privatization in 1997, workers lost their confidence in finding a full-time job if they left or were laid off from current workplace and were "very or somewhat bothered" about that.

The VCIOM surveys got the same opinions. Table 6-17 showed that only about 40 to 54 percent of respondents were confident in finding another job corresponding to their profession if they lost the current one, while most of the respondents were neither confident nor certain. The percentages were quite stable from 1993 to 1997, and that of 2001 did not show significant differences. Moreover, in June of 2001, about 39 percent of respondents said, if they were offered a job in another residential area, they would unconditionally disagree to move to the new place.[103] In such situation competition among workers to keep one's current job may reduce the workers' willingness to unite for collective actions; and traditional goals of competition among working fellows such as promotion or better salaries could be replaced by the desire to keep their own job. If the job-retaining competition became widespread at the workplace, then relations among workers would very likely be damaged, and possibility for collective action dwindled.

[103] Intercenter and VCIOM, Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay:Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.6, 2001, 88.

Table 6-17. Employees' Worries about Job Finding

Employees' Response	Can find another job (%)	May find a job, only with great efforts (%)	No, can not find (%)	Hard to answer (%)	Not answered (%)	Total
April 1993	53	…	24	22	1	100
Aug. 1993	53	…	28	18	1	100
Dec. 1993	49	…	26	24	1	100
May 1994	40	…	31	27	2	100
Sept. 1994	50	…	29	20	1	100
Nov. 1994	48	…	27	24	1	100
March 1995	43	…	30	27	0	100
Jan. 1996	52	…	22	25	1	100
Jan. 1997	44	…	33	23	0	100
June 2001	35	22	25	18	-	100

Note: The question is: "If you lose job, could you find anther one corresponding to your profession?"
Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.3, 1993, 44, No. 2, 1994, 78, No.4, 1994, 70, No.6, 1994, 72, No.1, 1995, 79, No.3, 1995, 80, No.2, 1996, 90; No.2, 1997, 88, No.6, 2001, 87. Sample size: Mar. 1993 survey, 1,999; Aug. 1993 survey, 1,980; Dec. 1993 survey, 1,956; May 1994 survey, 2,975; Sept. 1994 survey, 1,700; Nov. 1994 survey, 1,712; Mar. 1995 survey, 1,980; Jan. 1996 survey, 2,426; Jan. 1997 survey, 1,258; June 2001 survey, 1,207.

As the Russian economy gradually improved, the conflicts at the workplace reduced noticeably. Nonetheless, the role of labor union at the workplace remained weak. In a survey of VCIOM in June 2001, 48 percent of the respondents said that, in terms of issues such as wage and work conditions, neither employees' organizations (labor unions, the Working Collective Council, and specially elected representative(s) of working collective) nor managers actually protected workers' interests and rights, and only 24 percent of them said that such organizations did protect workers' interests.[104]

[104] Ibid, 89.

6. Performance of the Privatized Enterprises

In Russia, while economic liberalization changed external environment of enterprises, privatization changed the internal relations of enterprises. After the dramatic changes, how did the privatized enterprises adapt to the new situation? Actually, during the voucher privatization process, perceptions of managers and employees about effects of privatization somewhat reflected a low expectation. While only 27 percent of managers were optimistic that privatization would improve economic situation of their enterprises, much fewer technicians and workers shared this view, and 28 percent of skilled workers were pessimistic about that (see Table 6-18).

Perrow states that in advanced market economies it is expected that managers should show their intelligence, ability, enthusiasm, honesty and fairness, as well as their willingness to learn from subordinates and the ability to take criticism and acknowledge mistakes.[105] My discussion about the post-privatization management-worker relationship in the interviewed enterprises suggests that such behaviors were exactly what the worker interviewees expected, but many Russian managers, except the managers in enterprise H, did not make sufficient efforts to adjust their authoritarian behavior to meet the expectations of their workers. Thus it would not be surprising that workers' dissatisfaction was high and their working motivation turned out to be low.

[105] Charles Perrow, *Complex Organization: A Critical Essay*, New York, McGraw-Hill, Inc., 1986, 59.

Table 6-18. Opinions about Effects of Privatization

Answers	All Respondents (%)	Manager (%)	Technician (%)	Office Clerk (%)	Skilled Worker (%)	Non-skilled Worker (%)
"Will improve"	12	27	11	21	7	6
"Didn't exert Much influence	41	45	41	28	41	53
"Situation will become worse"	23	11	19	23	28	21
"Hard to answer"	23	16	27	26	23	20
Did not answer	1	1	2	2	1	0
Total	100	100	100	100	100	100

Note: The question is: "If your company is privatized, do you think that its economic situation will improve, worsen, or stay the same?"
Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.6, 1994, 79. Survey time: Sept. 1994. Sample size: 1,700.

On the other hand, many Russian managers did not work hard to improve the performance of their enterprises. The VCIOM nationwide survey data show that, from 1993 to 2000, only about ten to sixteen percent of employee respondents reported that their managers did actively search for new supplies and markets of sales, and until June 2001, seven years after the voucher privatization was completed, the percentage increased to 29; moreover, only after 2000 did a small portion of enterprises begin to develop new products for market (see Table 6-13). In 2001, only five to seven percent of workers and thirteen percent of technicians perceived that the efforts of their managers had yielded positive results for their enterprises, although 22 percent of manager respondents thought they had already done enough; 16 to 22 percent of employee respondents thought that their managers were not really interested in improving the situation of enterprises as their personal

interests did not necessarily depend on effectiveness of the enterprises, although only seven percent of manager respondents admitted that; also, ten to eleven percent of manager and employee respondents said managerial administrations could have done more but managers lack competence and persistence; at the same time, about 42 to 48 percent of manager and employee respondents considered the poor national economic situation prevented managers from doing better (see Table 6-18). Such opinions have explained why the post-privatization progresses in enterprises were limited.

Table 6-19. Evaluation of Management

Evaluation	Manager (%)	Technician (%)	Skilled Worker (%)	Unskilled Worker (%)
Managers could have done more, but much depends on the situation in the country and not them	48	43	41	42
Managers could have done more, but they lack competence and Persistence	11	9	10	11
Managers are not interested in improving enterprise situation since financial security of managers does not depend on enterprises Effectiveness	7	16	22	19
Managers' efforts are already yielding positive results for the enterprise	22	13	7	5
Difficult to answer	12	19	20	23
Total	100	100	100	100

Note: The question is: "How would you evaluate your enterprise administration activity?"
Source: Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.6, 2001, 86. Survey time: June 2001. Sample size: 1,207.

The VCIOM survey in June 2001 actually touched on a very important issue: is profit maximization really the top concern of Russian managers? In my interviews some worker interviewees mentioned that their managers spent a lot of money in building new office or traveling abroad. The activities suggested that maximizing personal interests might also be a main concern of some managers. When managers have gained control over their enterprises, they could easily use the resources of the enterprises to meet their personal needs, even though the enterprises do not make many profits. After the privatization in Russia was done, the experts of VCIOM also noticed the problem, thus added an option in their June 2001 survey for employee respondents: "Administration isn't interested in improving enterprise situation since financial security of managers doesn't depend on enterprises effectiveness." The survey results show that, indeed, some employee respondents reported that there were managers who were not much interested in improving the performance of their enterprises, because, even though the performance of their enterprises was not good, they could still have their personal interests satisfied. The phenomenon implies that the motivation of managers to improve efficiency might not be strong enough, and they may not work hard as they are supposed to be.

Right after the Russian privatization program was completed, Western economists began to measure its effects. From the data of an in-depth survey in 394 manufacture firms, Earle and Esrtrin suggested in 1996: "Privatization seems to have a clear and substantial effect on productivity… Its effect on the restructuring of product lines and employment (layoffs) is much less clear… [W]orker-ownership is associated with less changes in the product mix and with fewer layoffs, while managerial ownership is associated with more of both, and outsider ownership with

more product changes but no difference in layoffs."[106] Using the panel data collected in 189 enterprises from 1992 to 1996, Russian scholars Perevalov, Gimadii and Dobrodei found that privatization "does not produce performance improvements, except for costs per unit of revenue and to some extent for productivity of labor," and "'on average' does not have any influence on employment… Employment reductions seem to be quite 'natural' given the output drop in transition and the high level of over-employment with which state-owned enterprises operated before they were privatized."[107] Reviewing the researches about the post-privatization enterprise performance, Moers concluded in 1999 that "privatization per se does not bring the better performance that many thought it would."[108] After 1998 when Russian economy had been improved, Estrin and Bevan arranged a survey and collected the data from 1998 to 2000 and conclude that "ownership and performance were not yet well correlated in Russia, and there is no evidence of outsider-owner firms outperforming insider-owned ones," although 75 percent of the firms in their sample were able to generate positive profits in their three sample years.[109]

The latest research about the privatization effects in Russia was contributed by Brown, Earle and Telegdy who conducted a four-country comparison of the productivity effects of privatization with longitudinal data. They included 14,620 Russian industrial firms (94 percent

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[106] John S. Earle, and Saul Estrin, "Privatization versus Competition: Changing Enterprise Behavior in Russia," International Institute for Applied Systems Analysis, *Working Paper*, No. 96-049, May 1996.

[107] Yurii Perevalov, Ilya Gimadii, and Vladimir Dobrodei, "Does Privatization Improve Performance of Industrial Enterprises? Empirical Evidence from Russia," *Post-Communism Economies*, Vol.12, No.3, 2000, 351, 356.

[108] Luc Moers, "What Determines Enterprise Performance in Russia? A Survey of the Evidence," Tinbergen Institute, Amsterdam, the Netherlands, *Tinbergen Institute Discussion Papers*, No.99-077/2, Sept. 22, 1999, 15.

[109] Saul Estrin, and Alan Bevan, "Determinants of Russian Enterprise Performance," *Comparative Economic Studies*, Vol.45, No.2, June 2003.

were privatized) in their sample, assembled annual data of the enterprises from 1985 to 2002, and analyzed the changes of productivity before and after privatization. The authors concluded that the positive impact of privatization was immediate in Hungary and Romania, and nearly immediate in Ukraine, but in Russia the impact remained negative until the fifth year after the privatization; on the other hand, although a five to fourteen percent of productivity improvement had finally been observed in Russia, the privatization effect was obviously poorer than that in Romania and Hungary, as a substantial positive effect of privatization on productivity was found in the latter two countries (15 to 50 percent in Romania and 8 to 28 percent in Hungary).[110]

Exploring the internal relationship of the privatized enterprises, I argue that the prior concern of Russian managers during the voucher privatization was to maintain their control over their organizations by forming an alliance with workers, rather than to seek for economic efficiency through selling shares to outside investors; once the managers consolidated their power, many of them have kept an authoritarian management approach they were used to, and the management-worker relationship could become worse than before and workers' motivation would become lower. While managers were often not very capable and their dominance over the enterprises without oversight might have reduced their motivation to improve the performance of their enterprises, and in many privatized enterprises cooperation between managers and workers for the improvement did not exist, the privatization in Russia could hardly reach a satisfactory outcome.

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[110] Brown, J. David, John S. Earle, and Álmos Telegdy, "The Productivity Effects of Privatization: Longitudinal Estimates from Hungary, Romania, Russia, and Ukraine," *Journal of Political Economy*, Vol. 114, No. 1, February 2006, 61-99.

Appendixes: Interview Data

Table A-1 Basic Information of the Eleven Enterprises

Enterprise	Industrial Sector	Employees in 1987	Employees in 1992	Employees in 1997
A	Manufacture of measuring instruments	3,680	1,800	400
B	Manufacture of non-metallic mineral products	1,600	1,600	623
C	Manufacture of transportation Equipments	1,500	2,500	1,000
D	Manufacture of transportation Equipments	4,500	5,000	4,000
E	Food production	1,400	1,200	700
F	Manufacture of lingerie	1,500	1,200	500
G	Food processing	1,500	2,000	2,500
H	Manufacture of paper and paperboard	500	450	280
I	Manufacture of communication equipments	900	700	260
J	Printing	550	450	330
K	Manufacture of textile	1,050	870	400

Table A-2 Basic Information of the Interviewees

Interviewee	Managers		Rank-and-File Worker	
	Occupation	Years at Current Workplace	Occupation	Years at Current Workplace
A1	Chief engineer	36		
A2			Clerk	15+
A3			Mechanical worker	15+
A4			Mechanical worker	15+
B1	Technical director	15+		
B2			Assembler	15+
B3			Worker	15+
B4			Worker	14
C1	Commercial-financial director	15+		
C2			Aassembler	15+
C3			Seamstress	15+

Table A-2 Basic Information of the Interviewees-----Continued

Interviewee	Managers		Rank-and-File Worker	
	Occupation	Years at Current Workplace	Occupation	Years at Current Workplace
C4			Worker	15+
D1	Technical director	15+		
D2			Metal worker	4
D3			Copper smith	9
D4			Worker	15+
E1	Director	9		
E2			Assembler	12
E3			Metal worker	15+
E4			Assembler	15+
F1	Deputy economic director	15+		
F2			Seamstress	15+
F3			Worker	15+
F4			Seamstress	15+
G1	Deputy general director	9		
G2			Stevedore	9
G3			Worker	15+
G4			Operator	15+
H1	Chief engineer	9		
H2			Operator	15+
H3			Machinist	15+
H4			Controller	15+
I1	Deputy director	15+		
I2			Worker	15+
I3			Milling-machine Operator	15+
I4			Metal worker	15+
J1	Commercial director	15+		
J2			Press operator	15+
J3			Electric equipment Operator	15+
J4			Processor	15+

Table A-2 Basic Information of the Interviewees-----Continued

Interviewee	Managers		Rank-and-File Worker	
	Occupation	Years at Current Workplace	Occupation	Years at Current Workplace
K1	General director	15+		
K2			Metal worker	15+
K3			Worker	15+
K4			Worker	13

Table A-3 Role of Labor Union at the Workplace

Year	Very Much	Somewhat	So so	Almost Not Or Not at All	No Labor Union	Hard to Answer or Not Answered
Managers' Answers						
1987	G1,	A1, D1, I1, J1	E1,	B1, C1, F1	…	K1
1992	G1	…	A1, D1, E1, I1, J1	B1, C1, F1	…	K1
1997	G1	…	D1	A1, B1, C1, E1, F1	I1, J1, K1	…
Workers' Answers	…	…	…	…	…	…
1987	A2, A3, B4, C4, D4, E3, G2, G4, I3, K4	A4, B2, B3, C2, C3, I2, I4	E2, E4, F2, F3, F4, J2, J3, J4, K2, K3	…	…	D2, D3, G3
1992	D4, G2, G4, K5	A3, B4, C4, D3, I2	A4, B3, C2, C3, D2, E3, F3, I3, J2, J3, J4, K2, K3	A1, B2, E2, E4, F2, I4	…	F4, G3
1997	…	C4, D3, D4, G2	D2, G4	A2, A3, A4, B2, B3, B4, C3, E2, E3, E4, F2, F3, F4, I2, I3, I4	J2, J3, J4, K2, K3, K4	C2, G3

Note: The question is: "Do you think that labor union in your enterprise is helpful for the performance of the

enterprise, now and in 1987 and 1992?" In ten enterprises 10 managers and 30 workers were interviewed.

Table A-4 Are Managers Responsible to Enterprise?

Year	Very Much	Somehow	So so	Almost not or Not at all	Hard to Answer
Managers' Answers					
1987	B1, F1, G1,	E1, I1, K1	A1, C1, D1	…	…
1992	B1, F1, G1,	E1, I1, K1	A1, C1, D1, J1	…	…
1997	B1, C1, F1, G1, J1	D1, E1, K1	A1, I1	…	…
Workers' Answers	…	…		…	…
1987	B2, B3, B4, C4, D4, F2, F3, G3, G4, K3	A3, C2, E2, E3, E4, F4, I2, I3, I4, J2, K2,	A4, G2, J3, J4	K4	A2, C3, D2, D3
1992	B3, B4, C4, D3, F2, G3, G4, K3	A3, C2,D2, D4, E3, F3, F4, G2, I2, I3, J2, K2	B2, I4, J3, J4	A4, E2, E4, K4	A2, C3,
1997	B4, C4, D3, F2, G2, G3, G4, K3	C2, D4,E3, F4, K2	B3, D2, I4, J3	A3, A4, B2, E2, E4, J2, K4	A2, C3, F3, I2, I3, J4,

Note: The question is: "Do you think that most managerial personnel in your enterprise feel responsibility for achieving organization's goals, in 1987, 1992, and now?" In ten enterprises 10 managers and 30 workers were interviewed.

Table A-5 Interaction between Managers and Workers

Questions	Answers of Manager and Worker Interviewees			
	More in 1997 than 1992 or Always Yes	Less in 1997 than 1992	Little or No Interaction in 1997	Hard to Answer or Not Answered
Q1. by manager interviewee	A1, B1, J1, K1	D1, I2,	C1, E1, F1, G1	…
Q1. by worker interviewee	A2, C4, D4, E3, G2, I4, J3, J4, K2, K3	A3, D2, I2, I3, J2	A1, B2, B3, B4, C3, D3, E2, E4, F4, K4	C2, F2, F3, G3, G4
Q2. by manager interviewee	B1, C1, F1, G1, J1, K1	D1, E1, I1	A1	…
Q2. by worker interviewee	A2, B3, C2, C4, D4, E3, G2, G3, G4, I4, J3, K2	B4, D2, J2, J4, K3	A3, A4, B2, C3, D3, E2, E4, F2, F3, F4, I2, I3, K4	…
Q3. by manager interviewee	…	E1, I1	A1, B1, C1, D1, F1, G1, J1, K1	…
Q3. by worker interviewee	A2, B2, B4, C2, C4, D3, D4, E2, E4, F2, F4, G2, G3, I4, J4, K4	D2, I2, J2	A3, A4, B3, C3, E3, G4, I3, J3, K3	F3, K2
Q4. by manager interviewee	B1, C1, E1, F1, G1, J1, K1	D1, I1	A1	…
Q4. by worker interviewee	B3, C2, C3, D2, D3, E3, G3, G4, I3, J3, K2	A2, A3, D4, G2, I2, I4, J2, K3	A4, B2, B4, C3, E2, E4, F2, F3, F4, J4, K4	…

Note: The Interviewees answered the following questions: 1. “Are there any interaction and communication aimed at achieving organization’s objectives between management and the rank and file workers in 1987, 1992 and now?” 2. “How does the management in your enterprise willingly share information aiming at achieving organization’s objectives with the rank and file workers in 1987, 1992, and now?” 3. “Do you think that it’s important to get approval of the work group on important matters before going ahead in 1987, 1992, and now?” 4. “Do you think that workers in your enterprise have initiative to make suggestions or proposals for achieving organization’ goal to top managers in 1987, 1992 and now?” In ten enterprises 10 managers and 30 workers were interviewed.

Table A-6 Assessment of Management-Worker Relations

Questions	Answers of Manager and Worker Interviewees			
	Better in 1997 than 1992	Worse in 1997 than 1992	Same as Before	Hard to Answer or Not Answered
Q1. by manager interviewee	G1, J1	A1, B1, D1, E1, I1, K1	…	C1, F1
Q1. by worker interviewee	C4, E2, E4, G2, G3, G4, I4, J3	A3, B2, D2, D3, D4, I3, J2, J4, K4	A2, A4, B3, B4, C3, K2, K4	C2, E3, F2, F3, F4, I2
Q2. by manager interviewee	G1, J1	A1, B1, D1, E1, I1, K1	F1	C1
Q2. by worker interviewee	C4, E3, G2, I4	A2, A3, A4, B2, B4, C3, D2, D4, E2, F3, G4, I3, J2	B3, K2, K3, K4	C2, D3, E4, F2, F4, G3, I2, J3, J4
Q3. by manager interviewee	G1, J1	A1, I1, K1	B1, C1, D1, E1, F1	…
Q.3 by worker interviewee	D2	A3, A4, B2, B3, B4, C2, C4, D4, E2, E4, F3, G4, I2, K2	A2, C3, E3, F2, F4, G2, G3, I3, J2, J3, J4, K3, K4	D3, I4
Q4. by worker interviewee	C2, C4, G2, G3	A2, A3, A4, B2, B3, B4, D2, D3, D4, E2, E4, F3, F4, I3, I4, J2, K3, K4	E3, J3, K2	C3, F2, G4, I2, J4

Note: The Interviewees answered the following questions: 1. “Do you think that the human relation among workers in your enterprise has improved in 1997 than in 1992 and 1987?” 2. “Do you think that the human relation between managers and workers in your enterprise has improved in 1997 than in 1992 and 1987?” 3. “Besides of the regular working relations, are there any personalized friendliness between superiors and subordinates in your enterprise in 1987, 1992, and now?” 4. “How is satisfying of the majority of workers at your workshop with the work of general director of your enterprise in 1987, 1992 and now?” In ten enterprises 10 managers and 30 workers were interviewed.

Table A-7 Worker's Working Attitudes

Questions	Answers of Manager and Worker Interviewees			
	Better in 1997 than 1992	Worse in 1997 than 1992	Same as Before	Hard to Answer or Not Answered
Q1. by worker Interviewee	…	A3, A4, B3, B4, C2, D4, E2, E4, F2, F3, G2, G4, I2, I3, I4, J2, J3, K3, K4	A2, B2, C3, C4, D2, D3, E3, F4, G3, J4, K2	…
Q2. by manager Interviewee	J1	B1, E1, I1,	A1, C1, D1, F1, G1, K1	…
Q2. by worker Interviewee	G2,	A3, B2, B3, C2, D2, D3, F3, G3, I2, J2, K4	A2, A4, B3, C4, D4, E2, E3, E4, F2, F4, G4, I3, I4, J3, J4, K2, K3	C3,
Q.3 by worker Interviewee	C2, C4, D2, D3, G2, J2, J3, J4, K2,	A2, A4, B4, E2, I3, I4, K4	A3, B2, B3, C3, D4, E4, F2, F3, F4, G3, G4, I2, K3	E3,
Q4. by worker Interviewee	G2,	A2, A3, A4, B4, E2, E3, E4, I2,	B2, B3, C2, C3, C4, D2, D3, D4, F2, F3, F4, G3, G4, I3, I4, J2, J3, J4, K2, K3, K4	…

Note: The Interviewees answered the following questions: 1. "Do you reach the target of your job in 1987, 1992 and now?" 2. "Do you think that most rank-and-file employees in your enterprise feel responsibility for achieving organization's goals in 1987, 1992, and now?" 3. "After became a shareholder of your enterprise, do you feel that your situation within the organization has been improved?" 4. "How do you usually work in 1987, 1992, and now?" In ten enterprises 10 managers and 30 workers were interviewed.

Table A-8 Factors Affecting Workers' Working Motivation in 1997

Questions	Answers of Worker Interviewees			
	Fully or Somehow Affect	Not Affect	Hard to Answer or Not Answered	Only for Q.1: "Now Our Social Status in Firm is Too Low"
Q1. Social Status	D2, D3, E3,	A3, C4, D4, G3, G4, J2,	…	A2, A4, B2, B3, B4, C2, C3, E2, E4, F2, F3, F4, G2, I2, I3, I4, J3, J4, K2, K3, K4
Q2. Amount of Wage	A2, A3, B2, B3, B4, C2, C3, C4, D2, D4, E2, E3, E4, F2, F3, F4, G2, G3, I2, I4, J2, J3, J4, K2, K3	A4, D3, G4, I3, K4	…	…

Note: The Interviewees answered the following questions: 1. "Do you think that your working motivation is determined by the desire for the social status in your enterprise in 1987, 1992, and now?" 2. "Do you think that your working motivation is determined by the amount of your wage in 1987, 1992, and now?" In ten enterprises 30 workers were interviewed.

Table A-9 Workers Care about Manager's Behavior in 1997

Questions	Answers of Worker Interviewees			
	Care about that Very Much	Somehow Mind	Don't Mind	Hard to Answer
Q1. Manager's Inappropriate Behavior	A2, A3, A4, B2, B3, B4, C2, C3, D2, D3, D4, E3, E4, F2, F3, F4, G2, G3, G4, I2, I3, I4, J2, J3, J4, K2, K3, K4	E2,	C4,	…
Q2. Manager's Moral	A2, B2, B3, C2, D2, D3, D4, E3, E4, F2, F4, G4, I2, I4, J4, K2, K3, K4	B4, C4, G2, J3,	A3, A4, F3, I3, J2	C3, E2, G3,

Note: The Interviewees answered the following questions: 1. "Do you think that the authority of top managers weakens when their behavior is perceived inappropriate by workers, in 1987, 1992 and now?" 2. "Do you think that keeping moral is important for a manager if he wants to exercise authority over his subordinates effectively, in 1987, 1992 and now?" In ten enterprises 30 workers were interviewed.

Table A-10. Resistance and Conflicts at the Workplace

Year	Very Much	A Lot	Some	Rarely	None	Hard to Answer
Q1. Managers' Answers						
1987	B1	D1, F1	C1, I1	A1	E1, G1, J1	K1
1992	B1	F1	C1, D1, I1	A1	E1, G1, J1	K1
1997	B1	F1	C1, G1	A1,D1,I1,J1	E1	K1
Q2. Managers' Answers						
1987	…	D1	A1, E1, I1, K1	B1,F1,G1,J1	…	C1
1992	…	A1	D1, E1, I1	B1, F1, G1, J1, K1	…	C1
1997	…		C1, D1, E1, I1	A1, B1, F1, G1, J1, K1	…	…
Q2. Workers' Answers	…	…		…		…
1987	I4	G4, I2	A2, A3, C3, G2, G3, I3, J3, K2, K3	A4, C4, J2	B2, B3, B4, C2, D4, E2, E3, E4, F2, F4, K4	D2, D3, F3, J4
1992	A4	A3, G4, I2, I4	C3, D2, D4, E3, G2, G3, I3,J3,K2,K3	C4, D3, J2	A2, B2, B3, B4, C2, E2, E4,F2,F4,K4	F3, J4
1997	D4, G4	J2, J4	B4, C3, D2, D3, G2, I2, I3,I4,J3,K3	A3, C4, G3, K2	A2, A4, B2, B3, C2, E2, E3, E4, F2, F4, K4	F3

Note: The Interviewees answered two questions: 1: "How much resistances from the bottom level to the goals set by management do you usually meet in 1987, 1992, and now?" 2: "Are there any conflicts between the management and workers in your enterprise in 1987, 1992, and now?"
In ten enterprises 10 managers and 30 workers were interviewed.

Table A-11 Perceptions about Protecting Workers in 1997

Questions	Answers of Interviewees			
	Yes, Certainly	Somehow Mind	Don't Mind	Hard to Answer
Q1. Manager Interviewee	A1, B1, C1, D1, E1, F1, G1, I1, J1, K1	…	…	…
Q1. Worker Interviewee	A2, A3, A4, B2, B3, B4, C2, C3, C4, D2, D3, D4, E2, E3, E4, F2, F3, F4, G2, G3, G4, I2, I3, I4, J2, J3, J4, K2, K3, K4	…	…	…
Q2. Manager Interviewee	B1, D1, E1, F1, G1, I1, J1	C1,	A1,	K1
Q1. Worker Interviewee	A2, B2, C2, C4, D2, D3, D4, E2, E3, E4, F2, F3, F4, G2, G3, G4, I3, I4, J2, J3, J4, K2, K4	A3, B4, C3,	A4,	B3, I2, K3

Note: The Interviewees answered the following questions: 1. "Do you think that managers should protect workers of their enterprise? Why?" 2. "Do you think that it's important to have the goals of your enterprise achieved by helping employees with their personal problems in 1987, 1992, and now?"
In ten enterprises 10 managers and 30 workers were interviewed.

Chapter 7

China's Long SOE Reform Process:

Policy Changes and the Unnamed Privatization

Privatization of SOEs in China has been a long journey. A large scale nationwide privatization started after 1997 and ended in approximately 2002 when most small- and medium-sized SOEs were privatized; after 2003, the privatization of large and medium SOEs was carried out, until 2009. Including its experimental stage from 1992 to 1996, the process lasted about 18 years. With hesitation, worries and wonders, the Chinese communist regime approved the privatization of most state-owned industrial enterprises in 1997. However, unlike voucher privatization in Russia, China's privatization did not have a program, nor was it properly regulated. Moreover, the core target of the privatization of small- and medium-sized SOEs in China was not to establish corporate governance, but to get rid of the heavy burden SOEs laid on the state. Consequently, while many SOE managers were enriched and the state lightened of its burden, SOE workers paid the price of institutional failure. Of all transitional societies, China might be the only country where a large-scale privatization was carried out under an authoritarian communist regime. Such a regime had been quite forceful in dismissing millions of SOE workers in a short period, but was ineffective in preventing privatization from being co-opted by corrupt officials and SOE managers.

The literature on China's state-owned industrial enterprise reform published in China does not usually analyze privatization of the enterprises, because the Chinese government does not

allow public discussion on the issue. Among the works published outside China on the subject,[1] some were written before China's privatization began, and thus did not explore the privatization process; others published recently often focus on the mechanics and results of privatization, with analyses of economic sample data, but do not look carefully at the critical socio-political aspects of the process. In particular, no scholars have discussed why the Chinese government would push forward privatization without identifying it as such, nor have any described what took place at the

[1] For example, Edward S. Steinfeld, *Forging Reform in China: The Fate of State-Owned Industry*, Cambridge, UK, Cambridge University Press, 1998; Nicholas Lardy, *China's Unfinished Economic Revolution*, Washington, DC, The Brookings Institute, 1998; Malcolm Warner, ed. *Changing Workplace Relations in the Chinese Economy*, London, UK, MacMillan Press, 2000; Anne S. Tsui, and Lau Chung-ming, *The Management of Enterprises in the People's Republic of China*, Norwell, MA, Kluwer Academic Publishers, 2002; Carsten Holz, *China's Industrial State-owned Enterprises: Between Profitability and Bankruptcy*, Singapore, World Scientific Publishing Co, 2003; Qian Sun, and Wilson Tong, "China Share Issue Privatization: The Extent of Its Success," *Journal of Financial Economics*, No.70, 2003, 183-222; Ross Garnaut, Song Ligang, Stoyan Tenev, and Yao Yang, *China's Ownership Transformation: Process, Outcomes, Prospects*, Washington, DC, the International Finance Corporation and the International Bank for Reconstruction and Development/ The World Bank, 2005; Zhang Xiaodan, *Bargain without Union: Paternalist Labor Relations in China's Reform Era*, manuscript of Ph.D. Dissertation, Dept. of Sociology, Columbia University, 2005; Jefferson Gary, and Su Jian, "Privatization and Restructuring in China: Evidence from Shareholding Ownership, 1995-2001," *Journal of Comparative Economics*, Vol.34, No.1, 2006, 146-66; Shahid Yusuf, Kaoru Nabeshima and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, Washington, DC, the International Bank for Reconstruction and Development/ The World Bank, 2006; Barry Naughton, *The Chinese Economy: Transitions and Growth*, Cambridge, MA, the MIT Press, 2007; Kellee S. Tsai, *Capitalism without Democracy: The Private Sector in Contemporary China*, Ithaca, NY, Cornell University Press, 2007; Loren Brandt, and Thomas G. Rawski, *China's Great Economic Transformation*, New York, NY, Cambridge University Press, 2008; Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," Seoul, South Korea, *Seoul Journal of Economics*, Vol.21, No.2, 2008, 311-331; Gan Jie, "Privatization in China: Experiences and Lessons," in James R. Barth, John A. Tatom, and Glenn Yago, eds. *China's Emerging Financial Markets: Challenges and Opportunities*, Berlin, Germany, and New York, NY, Springer, The Milken Institute Series on Financial Innovation and Economic Growth 8, 2008, 581-592; Ma Shu-yun, "China's Privatization: From Gradulism to Shock Therapy?" *Asian Survey*, Vol.48, No.2, 2008, 199-214; Zeng Jin, "Political Compromises: The Privatization of Small- and Medium-Sized Public Enterprises in China," *Journal of Chinese Political Science*, Vol.15, No.3, 2010, 257-282.

workplace as privatization was implemented. Without an in-depth analysis of the formation of privatization decisions in China, and the interaction between government officials and SOE managers,[2] and between managers and workers, one cannot understand why an authoritarian regime declined to regulate the process with a strong hand, and why the state did not stop the obviously spontaneous direction that privatization was being taken in.

This chapter will first report the result of China's "unnamed privatization." In order to explore why the Chinese government finally opened the door for a nationwide privatization at the end of 1997, the author will review what had changed and what had been left unchanged at the workplace during the years from 1992 to 1997, then discuss why most of the attempts of SOE reform in that period did not improve the performance of SOEs, before analyzing the decision-making process of privatization. It was the pressure of a coming financial crisis that led the government to choose getting rid of most SOEs in order to prevent the state-owned banking system from collapse, before adequate preparation for privatization had been made. In analyzing China's privatization policymaking, the author found that from 1997 to 2009 privatization was promoted with a fuzzy remit and vague direction, while rules and procedures to regulate privatization activities were often absent.

[2] Zeng analyzed how different privatization policies were locally made in three cities, as a result of political compromise among local officials, workers, and SOE managers. Her work offers convincing explanations of privatization decision-making at local levels, but does not explore the details of the privatization process at the workplace and what took place after privatization. See Zeng Jin, "Political Compromises: The Privatization of Small- and Medium-Sized Public Enterprises in China," *Journal of Chinese Political Science*, Vol.15, No.3, 2010, 257-282.

How were SOEs privatized in China during the reform decade from 1997 to 2009? Chinese official documents and party mouthpieces simply present the government's narratives, but these statements often do not reflect what actually happened at the enterprise level. So far, no researcher has provided a systematic analysis of China's spontaneous privatization. This author reviewed 130 cases collected from Chinese and English newspapers and online reports, and found that SOE managers and government officials regularly manipulated the process for their personal profit. It would be fair to say that privatization in China was steered into becoming a spontaneous process, giving great discretion and consequent benefit to SOE managers and corrupt officials, at great cost to workers.

1. Transforming the SOE System: The Unnamed Privatization in China

In world history there has never been a regime like the Chinese government, or one that adopted the approach it did to privatization: the government realized that at a practical level, aside from privatization, it had no other way of solving the problems of SOEs; on the other hand, it declined to admit that what had been done was privatization. As Huang suggests, "a doctrinal commitment to state ownership remains a first among equal governing principles in today's China. The primacy of state ownership can be circumvented and even shortchanged but cannot be openly and explicitly challenged."[3] Thus, despite 82 percent of state-owned industrial enterprises being

[3] Huang Yasheng, *Selling China: Foreign Direct Investment during the Reform Era*, New York, NY, Cambridge University Press, 2003, 350.

privatized within twelve years, the Chinese government still refuses to officially recognize that privatization has taken place.

In 1995 when the number of the state-owned industrial enterprises reached its peak in China, there were 118 thousand SOEs (see Table 7-1); among them 4,685 were large enterprises, 10,983 medium-size enterprises, and about 102,300 were small ones.[4] From then the number of SOEs shrank rapidly year by year. As of 2008, only 21,313 industrial enterprises remained state-owned or as state holding companies, while most were large- or medium-sized firms, and the employees of industrial SOEs fell to 18 million from 43 million in 1996.

Table 7-1 State Owned Industrial Enterprises and Employees

Year	Number of Enterprise		Number of Employees	
	Number (Thousand)	Change from Previous Year	Number (Thousand)	Change from Previous Year
1992	103.3		45,210	
1993	104.7	+1.4	44,980	-230
1994	102.2	-2.5	43,710	-1,270
1995	118.0	+16.2	43,970	+260
1996	113.8	-4.2	42,780	-1,190
1997	98.6	-15.2	40,400	-2,380
1998	64.7	-33.9	37,478	-2,922
1999	61.3	-3.4	33,946	-3,532
2000	53.5	-7.8	29,953	-3,993
2001	46.8	-6.7	26,751	-3,182
2002	41.1	-5.7	24,236	-2,515
2003	34.3	-6.8	21,629	-2,607
2004	35.6	+1.3	19,732	-1,887
2005	27.5	-8.1	18,749	-983
2006	25.0	-2.5	18,040	-709
2007	20.7	-4.3	17,430	-610
2008	21.3	+0.6	17,941	+511

Source: China's State Statistics Bureau, *Statistical Yearbook of China 1993*, 409; *China Industrial Economic*

[4] Jin Pei, *He Qu He Cong: Dangdai Zhongguo de Guoyou Qiye Wenti* (Toward where Are We Moving: The SOE Problem in China Today), Beijing, China, the China Today Press, 1997, 85.

Statistical Yearbook 1995, 3, 19; *Statistical Yearbook of China 1995*, 94; *Statistical Yearbook of China 1996*, 401; *Statistical Yearbook of China 1997*, 411; *Statistical Yearbook of China 1998*, 431; *Statistical Yearbook of China 1999*, 421; *Statistical Yearbook of China 2005*, 132 (employee numbers from 1992 to 1997); *Statistical Yearbook of China 2008*, 502 (number of SOE from 1998 to 2007), 504 (number of employees from 1998 to 2007); *Statistical Yearbook of China 2009*, 498, 501. Beijing, China, China Statistics Publishing House.

Nevertheless, recently Wu Bangguo, the Chairman of the Standing Committee of China's parliament (the National People's Congress), proclaimed in an official speech that "we do not carry out privatization," at the 2011 annual conference of the Congress.[5] Indeed, in its official discourse the Chinese government has never used the term "privatization" for its SOE reform programs; instead, in the past two decades it has created various terms such as "invigorating (*gaohuo*) enterprises," "building up a modern enterprise system" and "diversifying ownership" for the reforms in the earlier years, and the "restructuring the SOE system (*gaizhi*)" used later. Among them, some soon disappeared in the official discourse, but *gaizhi* became very popular over the past fifteen years. G*aizhi* means incorporating large enterprises and selling medium and small enterprises and/or organizing shareholding companies. Its very nature in China is actually similar to the privatization program commonly understood in the world. As Garnaut et al state: the tasks of *gaizhi* "include bankruptcies, liquidations, listings and delistings, debt-for-equity swaps, sales to private parties (domestic and foreign), and auctioning of state firms and their assets or liabilities. In many cases *gaizhi* has involved full privatization."[6]

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[5] Xinhua News Agency, the speech of Wu Bangguo, the Chairman of the Standing Committee of China's National People's Congress, at the 2nd meeting of the 4th Conference of the 11th National People's Congress, Mar. 10, 2011 (http://news.sina.com.cn/c/2011-03-10/094122087374.shtml).

[6] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 1.

Privatization is not an easy task in many countries, as Suleiman and Waterbury point out: "the process is by nature painful and politically dangerous."[7] It is particularly true for the Chinese government, since the communist regime had heavily relied upon the social contract institutionalized by the SOE system for political stability during the reform era of the 1980s and the first half of the 1990s. On the other hand, the government fully understood the necessity to further reform the SOE system due to its poor performance. Therefore, promoting SOE reform was considered a priority in the economic reform agenda of the 1990s. From 1992 to 1996, the government carefully explored various programs for enterprise reform within the framework of a socialist system. These efforts came to naught, but in the meantime, the rapidly increasing financial burdens brought by loss-making SOEs to the state-owned banking system alerted the regime to the fact that decisive steps had to be taken if the government wanted to prevent its banking system, and thus the political system, from collapse. It was these pragmatic considerations that forced the regime to make decisions favorable to privatization. It has to be pointed out that at that time, China's state banking system was not integrated into the world financial market, and the potential threat to the banking system was mainly caused by the huge amount of non-performing loans (NPL) by SOEs. Thus, as the discussion below shows, the domestic threat to China's banking system emerged much earlier than July 1997 when the Asian financial crisis took place.

[7] Ezra N. Suleiman, and John Waterbury, eds., *The Political Economy of Public Sector Reform and Privatization*, Boulder, CO, Westview Press, 1990, 2.

2. SOE Reform from 1991 to 1996: Turing Around, Limited Progress

After a nearly three-year economic recession after the crushing of the 1989 democracy movement, China's SOE reform was resumed in late 1991. A proximate cause for the government to decide to push forward with reform was the poor performance of SOEs. Hannan pointed out in 1995: "[B]y the later 1980s China's state-owned enterprises had changed their organizational form. Their administrative structure was significantly modified from the form that it had taken under China's centrally planned and directly administrated economy, but there was a problem: administrative reform had not produced either an expected or a desirable behavioral result."[8]

Table 7-2 Loss-Makers and Debt-Asset Ratio of Industrial SOEs

Year	Loss-makers in Industrial SOEs (%)	Debt-Asset Ratio of Industrial SOEs (%)
1980	…	38
1985	…	40
1990	28	58
1991	26	61
1992	23	62
1993	29	72
1994	39	83
1995	…	84
1996	46	90

Note: The data of SOEs at city and county level.
Source: The percentages of loss-makers: Beijing, China, *Jingji Guanli* (Economic Management), No.4, 1995, 15, *Jingji Cankao Bao* (Economic Information Daily), Nov.16, 1995, *Renmin Ribao* (People's Daily), Dec. 12, 1996.

[8] Kate Hannan, "Reforming China's State Enterprises, 1984-1993," *The Journal of Communist Studies and Transition Politics*, Vol.11, No.1, March 1995, 45.

The debt-asset ratios: Beijing, China, *Zhongguo Gaige Bao* (China Reform News), June 11 and June 21, 1996, Jan. 28 and Apr. 30, 1997, *Jingji Cankao Bao* (Economic Information Daily), Oct 31, 1996.

During the reform years of the 1980s and early 1990s, SOEs in China retained more profits and rapidly increased borrowing from the state banking system. They increased benefit distribution to employees, but failed to pay attention to cutting costs and improving the quality of products. The financial situation of SOEs gradually worsened, as profit rates were low, debts kept growing, and net assets shrunk. The debt-to-asset ratio of industrial SOEs in China increased from 40 percent in 1985 to 61 percent in 1991 (see Table 7-2). The Chinese government had to act to prevent SOEs, the pillar of the Chinese economy, from decline; thus new ideas and policies for SOE reform were introduced. In the first half of the 1990s it tried various enterprise reform policies, without fundamentally changing the ownership structure, and found them to be rather disappointing.

2.1 Vacillating Between Radical and Progressive Approaches

Under a communist authoritarian regime, reform was usually initiated by the central government then implemented through top-down administrative orders. Without political reform, workers' political participation was almost impossible in China. How enterprise reform could be carried out, and whether it should involve workers, had been a policy debate in China for years. Two ideas appeared during the period from 1991 to 1996, and China's enterprise reform policies moved back and forth between them: One emphasized that the target of reform was the SOE system rather than its workers, and that enterprise reform should allow workers to participate. The other saw SOE

workers as the key target of reform, and considered the workers' "iron rice bowl" a main factor leading to poor motivation and low productivity; the concern here was to put more pressure on workers so they would work harder.

Following the latter logic, the policy to "break up the 'iron rice bowl, iron employment status, and iron wages'" was promoted from the top in 1991 and 1992,[9] as a new initiative for enterprise reform. The All-China Federation of Trade Unions (ACFTU), the government's union mouthpiece, first published a report about an experiment in Xuzhou city of Jiangsu Province;[10] then the State Council recommended the policy,[11] and China's supreme leader Deng Xiaoping advocated it when visiting the Beijing Capital Steel Company.[12] Immediately the issue became a hot topic in the Chinese media. Some provinces organized a campaign to push the policy forward,[13] and some local governments even had media report a new case of "breaking up the three 'irons'" each day.[14] However, the propaganda caused labor conflicts at some workplaces; at one firm angry

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[9] Sun Jie, "*Pochu 'San Tie': 1992 Nian Qiye Gaige de 'Zhuxuanlu'* (Break up 'Three Irons'-the 'Main Melody' for Enterprise Reform in 1992)," Beijing, China, *Renmin Ribao* (People's Daily), Feb. 18, 1992.

[10] "*Xuzhou Liang Bai Jia Kuisun Qiye 'Po San Tie'* (200 Loss-Making Enterprises in Xuzhou City Broke up the 'Three Irons')," Beijing, China, *Gongren Ribao* (Workers' Daily), Jan. 16, 1992.

[11] Wu Jinglian, "*Wo Dui Zhongguo Jing Gai Qingshi de Kanfa* (My Views on China's Economic Reform)," New York, NY, *Shijie Ribao* (World Journal), July 8, 1992.

[12] Lau Pe-chiong, "*Difang Qiye de Weiji* (The Crisis of Local Enterprises in China)," Hong Kong, *Xingdao Ribao* (Sing-tao Daily), Aug. 22, 1992.

[13] For example, the Shaanxi provincial government organized a conference on Feb. 29, 1992 to mobilize a campaign in order to implement the policy of "Breaking up the 'Three Irons' and Transforming Enterprise System." See Yanzi, "*Fengyu Piaoyao Po San Tie-Shi Tan Zhongguo Jingji Tizhi Gaige de Genben Wenti* (Breaking up the 'Three Irons': Exploring the Core Issue of China's Economic Reform)," Beijing, China, *Jingji Gaige* (Economic Management), No. 2, 1993, 18.

[14] Chen Zhong, Huo Xinyi, Da Xinya, "*Jingying Jizhi Zhuanhuan Re Zhong de Leng Sisuo* (A Calm Thought about the Heat of Transforming SOE Management Mechanisms)," Beijing, China, *Jingji Cankao Bao* (Economic Information Daily), Aug. 26, 1992.

workers even defenestrated their director.[15] When stood opposed to the new slogans,[16] workers would use the traditional Marxist idea of "master of enterprise" to defend their position. For instance, a worker told a reporter in an interview, "we are the masters of enterprise and managers are supposed to be our servants, how could servants fire masters?"[17] Soon the official propaganda regarding the issue was cooled down and the policy was put aside.[18] Obviously, at that time the government was not really ready to take on the sociopolitical risks of the radical policy. In the meantime, enterprise reform was moved back to emphasizing worker rights and participation.

The "breaking up the three 'irons'" policy was picked up once again in 1994, with a new title, "reducing fat for SOEs" (downsizing), implemented in a progressive way. Large SOEs were encouraged to separate non-productive branches, such as hospitals, cafeterias, schools, kindergartens, retail stores, and cinemas, from the firms, so the service units could be operated independently; at the same time, employees of the service units were no longer paid by the factories. Some examples of such practices were introduced through the media.[19] In July of 1994, China's

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[15] Yanzi, "*Fengyu Piaoyao Po San Tie-Shi Tan Zhongguo Jingji Tizhi Gaige de Genben Wenti* (Breaking up the 'Three Irons': Exploring the Core Issue of China's Economic Reform)," *Jingji Gaige* (Economic Management), No. 2, 1993, 18.

[16] "*Mangmu 'Za San Tie,' Xuezhe Han Buyi* (Scholars Said Better Not 'Break up the Three Irons')," New York, NY, *Shijie Ribao* (World Journal), Aug. 19, 1992.

[17] Yanzi, "*Fengyu Piaoyao Po San Tie-Shi Tan Zhongguo Jingji Tizhi Gaige de Genben Wenti* (Breaking up the 'Three Irons': Exploring the Core Issue of China's Economic Reform)," 18.

[18] Mo Xinyuan, "*Wenbu Tuijin Qiye San Xiang Zhidu Gaige* (Steadily Push Forward Enterprise Reform)," *Renmin Ribao* (People's Daily), May 31, 1993.

[19] For instance, Gong Dafa, "*Wugang Tizhi Gaige Jingqiaoqiao Shou Shixiao: Shunli Boli Qi Wan Zhigong, Laodong Shengchanlu Dafudu Tigao* (The Reform in Wuhan Iron and Steel Factory Silently Reached Success: 70 Thousand Workers and Staff Downsized Smoothly, and Labor Productivity Increased)," *Renmin Ribao* (People's Daily), Jan. 12, 1994; Gong Dafa, "*Wugang Jianfei Ji* (A Report of Reducing Fat at Wuhan Iron and Steel Factory)," *Renmin Ribao* (People's Daily), June 16, 1994.

parliament enacted the Labor Law.[20] The law mentioned the requirements for minimum wages and working hours; but its main purpose was to implement work contracts, a silent revolution to get rid of the "iron rice bowl" by replacing the lifetime employment status of SOE workers with contracts. From January 1995 to May 1996, 89 percent of the staff and workers in China's enterprises signed work contracts.[21] The road to large-scale lay-offs in SOEs was thus quietly paved.

From 1996, under the slogan of "Reducing Redundancy to Increase Efficiency (*jianyuan zengxiao*)," more and more workers were laid off,[22] and unemployed SOE workers became a central concern in Chinese society. In order to calm the SOE workers, three central government offices—the ACFTU, the State Commission for Economy and Trade, and the State Commission for Economic Reform—reconfirmed in a document that enterprise reform should not weaken worker participation and democratic management.[23] That promise later turned out to be lip service.

One issue related to the "iron rice bowl" was the bankruptcy of poorly performing SOEs. As of 1995, about five to seven percent of 14,000 large- and medium-sized SOEs had stopped production for quite a long time, for various reasons, and had to rely on bank loans to pay wages

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[20] Wang Yantian, and Fu Gang, "*Zhonghua Renmin Gongheguo Laodongfa Chutai Shuping* (A Brief Introduction of the 'Labor Law of the People's Republic of China')," *Renmin Ribao* (People's Daily), July 29, 1994.

[21] "*Quanguo Jin Jiu Cheng Zhigong Shixing Laodong Hetongzhi* (Almost 90 Percent of Staff and Workers in China Signed Work Contracts)," *Renmin Ribao* (People's Daily), Aug. 7, 1996.

[22] Zhou Fang, Wang Zhenhong, and Li Chunlei, "*Dongbei Guoyou Daqiye Jian Ren Zeng Xiao* (Large SOEs in the Northeast Reduced Redundancy to Increase Efficiency)," *Renmin Ribao* (People's Daily), Sept. 1, 1996.

[23] Xinhua News Agency, "*Jingxing Xiandai Qiye Zhidu Shidian, Buneng Xueruo Zhigong Minzhu Guanli* (Experiments for the Modern Enterprise System should not Weaken Workers' Democratic Management)," Shanghai, China, *Jiefang Ribao* (Liberation Daily), June 14, 1996.

and interest.[24] Many small SOEs were in a similar position. China enacted the Bankruptcy Law in 1986, which says "an SOE can be declared bankrupt if it cannot repay its debt;" "however, many insolvent SOEs are being kept alive because creditors [mainly the state banks] do not initiate bankruptcy proceedings… The number of bankruptcies each year is limited by the size of banks' reserves against bad loans and by additional financial support from the government."[25] In China, bankruptcy was a difficult step to take. It not only involved complex financial arrangements, but also triggered labor conflicts as SOE employees would ask why they ought to pay the cost of losing their jobs because of mistakes made by managers that were selected and appointed by the government. While SOE workers still believed that under socialism there should be job security and they, as the "master of the enterprise," were not supposed to be fired, managers did not want their enterprises to go bankrupt either. Moreover, state banks also opposed the bankruptcy of SOEs because they were their only creditors and their bankruptcy could thus bring huge losses. The government also declined to push forward the bankruptcy of poorly performing enterprises because in China there was no unemployment insurance system, nationwide pension system, or medical insurance system: widespread bankruptcy without a social safety net may have simply led to social unrest.[26] For example, from 1991 to 1992 the bankruptcy of the Chongqing Textile Factory, decided by the city government, caused a series of confrontations between workers and government officials;

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[24] "*Shiixian Ziyuan Youhua Peizhi: Guojia Jing Mao Wei Fuzeren Tan Guoqi Jianbing* (Implementing Resource Optimizing Allocation: the Head of State Commission for Economy and Trade Talked about Merge of SOEs)," *Jingji Cankao Bao* (Economic Information Daily), June. 21, 1996.

[25] Carsten Holz, *China's Industrial State-owned Enterprises: Between Profitability and Bankruptcy*, Singapore, World Scientific Publishing Co, 2003, 258-259.

[26] Jiang Shijie, "*'Si' Qu 'Huo' Lai Hua Pochan: Guoyou Qiye Shenhua Gaige Silu Tan* ('Dead' or 'Alive,' the Options in Bankruptcy: How to Deepen SOE Reform)," *Renmin Ribao* (People's Daily), Jan. 30, 1995.

on June 16 and July 27, 1992, the head of the Textile Bureau of Chongqing city was detained twice by angry workers for a total of 37 hours.[27]

Actually, from 1989 to 1993, there were only 1,417 bankruptcy cases in China processed by the courts;[28] and as Yusuf, Nabeshima and Perkins noted, "in the second half of the 1990s, several thousands of state enterprises were declared bankrupt… Neither the creditors of the bankrupt enterprises nor the courts, however, played much of a role in deciding the fate of the enterprises."[29] In China, while both banks and enterprises were state-owned, bankruptcy proceedings were different from that in the West. Very often, SOE debtors were eager to apply for bankruptcy, whereas the creditors tried to prevent it because bad loans would then have to be written down. In Jilin Province, of 32 bankruptcy cases, 94 percent were initiated by debtors or the government offices that supervised the enterprises; the real purpose of the debtors who wanted to enter bankruptcy was to dodge debts, while 80 percent of their debts were bank loans.[30] When initiating bankruptcy proceedings, some SOEs did not notify their creditors until the courts declared the enterprises bankrupt.[31] On the other hand, branches of state banks had to be very careful with bankruptcy cases, as their potential losses could be large. The largest state bank, the China Industrial

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[27] Jin Pei, *He Qu He Cong: Dangdai Zhongguo de Guoyou Qiye Wenti* (Toward Where Are We Moving: The SOE Problem in China Today), 247-248.

[28] Wang Wuyi, "*Guanyu Woguo Guoyou Qiye Pochan Qingkuang de Yinsu Fenxi* (An Analysis about Bankruptcies of SOEs in China)," Beijing, China, *Jingji Yanjiu* (Research of Economics), No. 6, 1994, 42.

[29] Shahid Yusuf, Kaoru Nabeshima and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, Washington, DC, the International Bank for Reconstruction and Development/ The World Bank, 2006, 103.

[30] "*Qiye Pochan de Heidong* (The Black Hole in Bankruptcy Cases)," *Renmin Ribao* (People's Daily), July 31, 1993.

[31] Zheng Donghong, "*Pochan Tao Zhai* (Bankruptcy as a Method to Escape from Debts)," Beijing, China, *Zhongguo Gaige Bao* (China Reform News), Sept. 10, 1996.

and Commercial Bank, in just 1995 and 1996, lost 24 billion yuan in assets as a result of 5,128 closed bankruptcy cases, taking the hit for about 85 percent of the debts of the bankrupted enterprises.[32] The government then ordered that bankruptcy be put under control, and state bank creditors had to have a vote in the bankruptcy committee on each case.[33]

Moreover, local governments and some SOEs played another game together against the state banks. Under the banner of SOE reform or structural adjustment, a lot of SOEs moved their financial resources and the best quality equipment into newly established companies, but left the "mother enterprise" an empty shell with all the unpaid debts waiting for bankruptcy.[34] Such maneuvers were later used frequently in China's privatization.

2.2 Three SOE Reform Policies from 1992 to 1996

From 1992 to 1996, the Chinese government tried three reform measures to restructure SOEs. Although some measures involved ownership changes, the government refused to admit that they were means of privatization.[35]

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[32] Xue Xiaohe, "*He Wei 'Guifan Pochan': 'Jia Pochan, Zhen Tao Zhai' Tou Xi* (What is 'Regulating Bankruptcy': An Analysis of 'False Bankruptcy and Really Dodging Debts')," Beijing, China, *Jingji Ribao* (Economic Daily), Aug. 12, 1997.

[33] Zhu Jianhong, "*Qiye Jianbing Pochan you Xin Guiding* (The New Regulation about Merge and Bankruptcy of SOEs)," *Renmin Ribao* (People's Daily), July 31, 1996.

[34] Yongjun, Shaohui, "*Jingti Tao Zhai Xin Zhao: Qiye 'Liebian'* (Be Alert by the New Approach of Dodging Debts: Enterprise Disintegration)," *Jingji Cankao Bao* (Economic Information Daily), Feb. 24, 1994.

[35] Zhang Chengzhi, "*Siyouhua bushi Qiye Gaige de Fangxiang* (Privatization is not the Direction of Enterprise Reform)," *Zhongguo Gaige Bao* (China Reform News), July 11, 1995; Wang Zhongyu, "*Guoqi Gaige Buneng Zou Ziyouhua Daolu* (SOE Reform Can not Move forward toward Privatization)," *Zhongguo Gaige Bao* (China Reform News), Mar. 26, 1996.

First, employee shareholding in small and medium SOEs was introduced as an effective method of improving SOE performance. The reason the approach was adopted as an earlier policy option was so the government could publicize it as the "socialist cooperative economy,"[36] thus encountering less ideological obstacles, even though employee shareholding in SOEs is usually understood as simply privatization in the West. As of May 1992, 2,741 enterprises had arranged employee shareholding.[37] In 1992 the Chinese government further recommended the method because it could help SOEs raise funds from employees and increase the motivation and productivity of employee shareholders as well.[38]

In many provinces, employee shareholding was adopted as a key measure for enterprise reform. As of 1997, in Sichuan Province about 80 percent of small SOEs adopted the approach,[39] while in Jiangsu, Anhui, and Shandong Provinces the percentages were 80, 78 and over 50 percent respectively.[40] A lot of managers even forced workers to buy shares of their own

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[36] "*Rang Gufen Hezuo Zhi Gengjia Jiankang di Fazhan: Fang Guojia Tigai Wei Fu Zhuren Hong Hu* (Let Shareholding Cooperatives Develop Healthier: An Interview to Hong Hu, Deputy Director of the State Commission for Economic Reform)," *Zhongguo Gaige Bao* (China Reform News), Aug. 8, 1997.

[37] Zhou Changxin, "*Zhongguo Gufenzhi Gaige Chu Jian Chengxiao* (The Reform of Shareholding Cooperatives Appeared Effective in China)," Beijing, China, *Renmin Ribao, Haiwai Ban* (People's Daily, Overseas Version), May 20, 1992.

[38] The State Commission of Economic Reform, the State Commission of Planning, Ministry of Finance, The People's Bank of China, The Production Office of the State Council, "*Gufenzhi Qiye Shidian Banfa* (The Regulation for Experiment of Shareholding Company, May 15, 1992), " *Renmin Ribao* (People's Daily), June 19, 1992.

[39] Shi Benxiu, "*Sichuan Ba Cheng Guoyou Xiaoqiye 'Gai Xing'* (80 percent of Small SOEs in Sichuan Province are no Longer State-owned)," *Zhongguo Gaige Bao* (China Reform News), Dec. 11, 1997.

[40] Wang Ruozhu, Niu Wenwen, and Zhang Laimin, "*Qiye Pian: Ta Shang Zhidu Chuangxin zhi Lu* (On Enterprises: The Road toward Institutional Innovation)," *Zhongguo Gaige Bao* (China Reform News), Aug. 5, 1997.

enterprises with a "buy shares or dismissal" policy.[41] The main purpose of employee shareholding was not to turn sole state ownership into partial employee ownership, but to collect funds from employees to fill fiscal shortfalls.[42] Employee shareholder rights were not clarified or protected, and private ownership in such cases was nominal. Not only did many managers not regard the requests of employee shareholders, the government did not respect the ownership rights of employees either. Some government offices still appointed managers, intervened in decisions of employee shareholding companies, ordered them to turn over revenue,[43] and when employee shareholders thought their managers were incapable of improving the performance of their enterprise, their opinions were often ignored.[44] Most employee shareholders did not have any sense of being an owner with legal rights; they simply saw their stake in the enterprise as a loan and hoped to get the investment back through dividends as soon as possible.

However, in Zhucheng city of Shandong Province a variation appeared that attracted the attention of some Western scholars.[45] The city government fully privatized most small SOEs

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[41] Li Shengming, "*Dui Gufenzhi you 'Si Danxin'* (The Four Worries of Workers about Employee Shareholding)," *Zhongguo Gaige Bao* (China Reform News), Nov. 18, 1997.

[42] Xinhua News Agency, "*Tigai Wei Fuzeren Tan Jinnian Jingji Tizhi Gaige Renwu* (The Head of the State Commission for Economic Reform Talked about Tasks of Economic Reform in This Year)," *Renmin Ribao* (People's Daily), Feb. 18, 1992.

[43] Zang Chuanzhi, Lin Yu, and Liu Juan, "*Zhengfu Zhineng Da Zhuanbian: Ji Lu Gan Chengshi Gufen Hezuozhi Diaocha* (An Investigation of Shareholding Cooperative System in Three Provinces: Transforming Government Functions)," *Jingji Cankao Bao* (Economic Information Daily), Oct. 30, 1997.

[44] Wang Wei, "*Benbao 'Shui Lai Dang Changzhang, Zhigong You Quan Tiao' Baodao Yinqi Fanxiang: Gufen Hezuozhi Qiye Huhuan Hao Dangjia* (Shareholding Cooperative Companies Look for Good Managers: Responses to Our Report 'Who could be the Director? Employee Shareholders Ought to Have Rights to Select')," Shanghai, China, *Jiefang Ribao* (Liberation Daily), Nov. 30, 1997.

[45] For example, Ross Garnaut et al, *China's Ownership Transformation: Process, Outcomes, Prospects* (Washington, DC, the International Finance Corporation and the International Bank for Reconstruction and

through employee shareholding in 1993.[46] In Zhucheng, the congress of shareholders was allowed to elect top managers, and fourteen percent of former general directors and 24 percent of former deputy directors lost their positions,[47] despite that the election was still under the control of the local branch of the communist party.[48]

Another policy, Merger and Asset Reorganization *(jianbing chongzu)*, was to encourage the SOEs with better performance to merge other loss-making SOEs, so the latter would not fall into bankruptcy. From February 1994 the Chinese government began the experiment with large- and medium-sized SOEs in 18 cities under the slogan "optimizing asset structure." From 1994 to 1996, about 1,436 SOEs were merged into other SOEs; the debts of the merged companies were rearranged, assets reallocated and employees reappointed or laid off.[49] The core concern of the

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Development/ The World Bank, 2005), 4; Barry Naughton, *The Chinese Economy: Transitions and Growth* (Cambridge, MA, the MIT Press, 2007), 323.

[46] Huang Shaoan, and Wei Jian, "*Guoyou Zhong Xiao Qiye Shichanghua Gaige ji Zhengfu Zai Gaige Jincheng Zhong de Juese: Yi Shandong Zhucheng Guoyou Zhong Xiao Qiye Gaige Zuowei Anli* (The Market-Oriented Reform of Medium- and Small-sized SOEs and the Role of Government in the Reform: Case Studies of Medium- and Small-sized SOE Reform in Zhucheng of Shandong Province," Beijing, China, *Jingji Yanjiu* (Economic Research), No.10, 2000; Han Shinan, "*Gaige Kaifang Sanshi Nian: Zhucheng Gexing Shizhang 'Chen Mai Guang'* (Thirty Years for Reform and Opening: The Major of Zhucheng City, Chen Sold-off," Jinan, China, *Qilu Wanbao* (Qilu Evening News), Oct.22, 2008 .

[47] Gao Liang, "*Difang Zhengfu Lingdao Guoqi Gaige de Chenggong Anli (Zhucheng)* (A Successful Case of SOE Reform under the Leadership of Local Government (Zhucheng))," Beijing, China, *Jingji Guanli Wenzhai* (Economic Management Digest), No. 16, Aug. 1999.

[48] Huang Shaoan, and Wei Jian, "*Guoyou Zhong Xiao Qiye Shichanghua Gaige ji Zhengfu Zai Gaige Jincheng Zhong de Juese: Yi Shandong Zhucheng Guoyou Zhong Xiao Qiye Gaige Zuowei Anli* (The Market-Oriented Reform of Medium- and Small-sized SOEs and the Role of Government in the Reform: Case Studies of Medium- and Small-sized SOE Reform in Zhucheng of Shandong Province."

[49] "*Shiixian Ziyuan Youhua Peizhi: Guojia Jing Mao Wei Fuzeren Tan Guoqi Jianbing* (Implementing Resource Optimizing Allocation: the Head of State Commission for Economy and Trade Talked about Merger of SOEs)," *Jingji Cankao Bao* (Economic Information Daily), June. 21, 1996; Wang Ruozhu, Yang Guomin and Niu Wenwen, "*Zhongguo Jingji Yinglai Chongzu Shidai* (China's Economy Welcomes an Era of Enterprise

policy was to prevent the assets of the loss-makers from vanishing. Obviously, it was not easy to find an SOE to absorb the whole factory of a loss-maker. Therefore, in order to save some poor enterprises from bankruptcy, local governments got involved in the "forced marriage" of SOEs. A later report about the results of the "asset reorganization" mentioned a series of problems in implementation: for example, some enterprises were forced to merge factories by administrative order, and the merger selected only the good quality assets and left the rest, along with the redundant workers, to local governments, and so on.[50] When some loss-making SOEs sought new partners, they might consider non-SOE candidates—then the "asset reorganization" might lead to ownership changes.

The third policy referred to the experiments of "establishing a modern enterprise system" in large SOEs. Lardy writes that in November of 1993 the Third Plenum of the Fourteenth Chinese Communist Party Congress endorsed the creation of a modern enterprise system. The key features of this initiative were its approval of the development of diversified forms of ownership, which would compete on equal terms in the marketplace, and the introduction of a framework for modern corporate governance of state-owned firms.[51] Holz states that the modern enterprise system encompasses four elements: "clearly allocated property rights, clear rights and responsibilities, separation of government and enterprise, and scientific management."[52] In December of 1993,

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Reorganization)", *Jingji Ribao* (Economic Daily), Dec. 31, 1997.

[50] Zhong Shi, "'*La Lang Pei' Zhineng Gei Guoqi Bang Daomang* ('Forced Marriage' Does not Help SOEs)," *Zhongguo Gaige Bao* (China Reform News), May 14, 1998.

[51] Nicholas Lardy, *China's Unfinished Economic Revolution*, Washington, DC, the Brookings Institution. 1998, 23-24.

[52] Carsten Holz, *China's Industrial State-owned Enterprises: Between Profitability and Bankruptcy*, 245.

China's Company Law was enacted to legalize the experiments of the policy.[53] Although it regulates the operations of existing private firms, the law was not really legislated for privatizing SOEs; instead it served more for improving corporate governance of SOEs. Clarke thinks that the company law was designed primarily to address problems within the state sector: "The need of nonstate actors for a convenient form in which to conduct business occupies a very low priority in the minds of state policymakers, and the Company Law is thus clearly concerned more with regulating and suppressing than with fostering and nurturing." Moreover, the need to provide for the special circumstances of state-sector enterprises ended up hijacking the company law, so that instead of state-sector enterprises being made more efficient by being forced to follow the rules for private-sector enterprises (the original ambition), potential private-sector enterprises were hamstrung by having to follow rules that made sense only in a heavily state-invested economy.[54]

In November 1994, the Chinese government selected 100 large SOEs for the experiment. The 100 enterprises were requested to submit their reform programs, and at the end of 1997 they were approved and moved forward. Hu pointed out that the modern enterprise system in the West was the natural result of the development of shareholding companies organized upon private ownership; but in China it was established upside-down, while the system was seen as a way to stop large SOEs from going bankrupt. In China the system could only have been built through the consent of SOEs and government bosses, where private ownership was a second thought, or where ownership rights

[53] Xinhua News Agency, "*Zhonghua Renmin Gongheguo Gongsi Fa* (The Company Law of the People's Republic of China)," *Renmin Ribao* (People's Daily), Dec. 31, 1993.

[54] Donald Clarke, "Corporate Governance in China: An Overview", *China Economic Review*, No.14, 2003.

were only poorly defined.[55] His observation implies that the policy itself was ambiguous.

One of the key problems in establishing corporate governance in China was the question of who could really control a shareholding company. As shareholders' rights were often ignored or marginalized, offices of governments and the communist party constantly intervened in the operations of shareholding companies. A 1994 survey of 371 shareholding companies, of which 62 were listed on Chinese or Hong Kong stock markets, reported heavy political influence over key appointments. When selecting a chairman of the board of directors and general director (CEO), the selection processes of 45 percent of the chairmen and 41 percent of the CEOs were suffered government or party intervention. This was done in three ways: the board of directors might elect and/or appoint nominees, but need final approval from the party; nominees were provided by the party, then the board of directors elected or appointed them; or the party or government office would simply appoint their people and have the board of directors approve it.[56] An issue in terms of effective corporate governance emerged in China: how to properly define the relationship between the board of directors and the committee of the communist party in shareholding companies. According to the company law, the board of directors of a shareholding company is supposed to have all authority to make final decisions; but China's Constitution regulates that the communist party is always above the board. Besides the party committee in enterprises, there were two other

[55] Hu Peizhao, "*Woguo Xiandai Qiye Zhidu Nixiang Shengzhang de Zhang'ai* (The Obstacles for the Reversely Growing Modern Enterprise System in China)," Beijing, China, *Jingji Yanjiu* (Economic Research), No.7, 1994, 15.

[56] The Chinese Entrepreneurs Survey System (CESS), "*Dui Zhongguo Gufenzhi Qiye Fazhan de Diaocha yu Fenxi* (A Survey and Analysis of the Development of China's Shareholding Companies)," Beijing, China, *Guanli Shijie* (Management World), No.4, 1994, 144-145.

bodies designated by the government for "socialist workplace democracy": the labor union controlled by the party, and the Congress of Workers and Staff. The latter two bodies, together with the committee of the communist party, were called in China the "Old Three Bodies," in contrast to the "New Three Bodies" of modern corporate governance (the board of directors, the supervisory board,[57] and the congress of shareholders). How to deal with the relationship between the "New Three Bodies" and the "Old Three Bodies" was a serious challenge in China.[58] This issue never had to be addressed in other transitional countries. It was not a theoretical question of corporate governance, but an unusual real world problem that arose when privatization was carried out by a communist regime, and it remains unsolved in China today. The remaining active role of the communist party committee, and the traditional operation of the official labor union in enterprises, undermines the corporate governance of LLSCs in China, particularly that of large LLSCs.

3. Changes and Stasis in SOE Management

From 1992 to 1996 SOE reform was a core concern in China policy circle, and changes could be observed in SOE management. First of all, the qualification of the CEOs of SOEs was gradually

[57] The articles 52-54 and 124-126 of China's company law regulates that larger LLCs and all LLSCs should establish supervisory boards; it consists of more than three representatives of shareholders and employees, and is in charge of overseeing the financial situation of the company, and the behavior of managers. U.S. readers may not be familiar with the concept of the supervisory board found in China. See "*Zhonghua Renmin Gongheguo Gongsi Fa* (the Company Law of the People's Republic of China)," *Renmin Ribao* (People's Daily), Dec. 31, 1993.

[58] Lu Changchong, "*Gongsi Zhili Jigou ji Xin Lao San Hui Guanxi Lun* (On the Institutions of Corporate Governance and the Relations between the 'New Three Bodies' and 'Old Three Bodies')," Beijing, China, *Jingji Yanjiu* (Economic Research), No.11, 1994, 10-17.

improved. Before reform many managers were promoted from the ranks of workers, usually having completed a middle school education—many were still in managerial positions during the reform era; in 1996 and 1997, about 32 to 36 percent of the interviewed CEOs were originally workers (see Table 7-3). However, since the 1980s, in most situations, new CEOs were no longer selected from workers. The Chinese Entrepreneur Survey System (CESS) reported that, from 1993 to 1997, only a few workers were directly promoted to CEO; during those years fewer and fewer CEOs were selected from among technicians, but more were promoted from managerial staff (see Table 7-4). The change suggested that the emphasis in CEO selection changed from being familiar with technology to understanding management.

Table 7-3 First Job of CEOs in Life Career

Job	1996 (%)	1997 (%)
Party official or staff for political control	5	5
Technician	36	32
Managerial staff	11	8
Worker	31	39
Other	17	16
Total	100	100

Source: The CESS, "*Xianjieduan Woguo Qiye Jingyingzhe de Zhiye Liudong yu Zhiyehua Quxiang: 1996 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Carrier Mobility and Professionalization of China's Managers: A 1996 Special Report on Development of Chinese Entrepreneurship)," Beijing, China, *Guanli Shijie* (Management World), No.3, 1996, 132; the CESS, "*Suzhi yu Peixun, Biange Shidai de Zhongguo Qiye Jingying Guanli Zhe: 1998 Zhongguo Qiye Jingying Guanli Zhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Qualification and Training, the Chinese Managers in the Reform Era: A 1998 Special Report on Development of Chinese Entreprenuership)," *Guanli Shijie* (Management World), No.4, 1998, 137. Sample size of the surveys: 1996, 2,735 (73 percent were SOEs); 1997, 2,415 (64 percent were SOEs).

Table 7-4 Latest Job before Appointed to be CEO

Job	1993 (%)	1994 (%)	1996 (%)	1997 (%)
Party official or staff for political control	24	22	32	27
Technician	39	32	20	17
Managerial staff	35	45	42	43
Worker	1	0	1	3
Other	1	1	5	10
Total	100	100	100	100

Source: The CESS, "*Xianjieduan Woguo Qiyejia Duiwu de Xingwei Tezheng Diaocha Fenxi: 1995 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Behaviors of China's Entrepreneurs: A 1995 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1995, 153; The CESS, "*Xianjieduan Woguo Qiye Jingyingzhe de Zhiye Liudong yu Zhiyehua Quxiang: 1996 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Carrier Mobility and Professionalization of China's Managers: A 1996 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1996, 132; the CESS, "*Suzhi yu Peixun, Biange Shidai de Zhongguo Qiye Jingying Guanli Zhe: 1998 Zhongguo Qiye Jingying Guanli Zhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Qualification and Training, the Chinese Managers in the Reform Era: A 1998 Special Report on Development of Chinese Entreprenuership)," *Guanli Shijie* (Management World), No.4, 1998, 137. Sample size of the surveys: 1993, 2,620; 1994, 2,756; 1996, 2,735; 1997, 2,415.

On the other hand, about a quarter of the recently appointed CEOs were former communist party officials. Obviously, political control and political skills in dealing with workers was still considered an important CEO selection criterion. Analyzing the career background of the CEOs, the author found that the majority had a first job as either a worker or technician; many were then promoted to management or communist party offices at the workplace, and finally they were appointed by the government office to CEO. The typical career route implied that political loyalty to the communist party was of central importance to promotion.

Table 7-5 Education of SOE Directors

Education Completed	1993 (%)	1997 (%)	1999 (%)
College and above	40	48	45
Other forms of higher education	37	51	47
High school or professional school	20		
Middle school or below	3	1	8
Total	100	100	100

Source: The CESS, "*Zhongguo Qiyejia Xianzhuang Fenxi ji Qiyejia dui Qiye Jingying Huanjing de Pingjia* (Analysis of Current Status of Chinese Entrepreneurs and Their Evaluations about Managerial Environment)," *Guanli Shijie* (Management World), No.6, 1993, 128; the CESS, "*Suzhi yu Peixun, Biange Shidai de Zhongguo Qiye Jingying Guanli Zhe: 1998 Zhongguo Qiye Jingying Guanli Zhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Qualification and Training, the Chinese Managers in the Reform Era: A 1998 Special Report on Development of Chinese Entreprenuership)," *Guanli Shijie* (Management World), No.4, 1998, 140; the CESS, "*Yingjie Zhishi Jingji Tiaozhan: Shiji zhi Jiao de Zhongguo Qiye Jingyingzhe: 1999, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Welcome the Challenges of Knowledge Economy, The Chinese Managers toward the New Century: A 1999 Special Report on Development of Chinese Entreprenuership)," Apr. 1999 (www.ceoinchina.com/Item/450.aspx). Sample size of the surveys: 1993, 2,620; 1997, 2,415; 1999, 3,180.

Education backgrounds also became important in CEO selection during the reform years. Among the interviewed CEOs of SOEs, 40 to 45 percent had completed higher education (see Table 7-5). During the Cultural Revolution from 1966 to 1976, normal college education was interrupted; only after 1978 were management majors in some colleges reinstated, but at the time those older than 26 were no longer eligible to take the college entrance exam. In other words, as more than 80 percent the CEOs were older than 26 years old (see Table 7-6) in 1978, it is very unlikely that they could have completed formal college education during the reform era. Therefore, when the interviewed CEOs reported in the 1990s that they had received college training, they had either

graduated before the Cultural Revolution—of which about 70 percent majored in science and technology[59]—or undertook higher education while working. Among the latter group, about half studied courses related to management.[60]

Table 7-6 Age of SOE CEOs

Age	(%)
Under 40	12
41-51	43
Above 51	45
Total	100

Source: The CESS, "*Zhongguo Qiyejia Xianzhuang Fenxi ji Qiyejia dui Qiye Jingying Huanjing de Pingjia* (Analysis of Current Status of Chinese Entrepreneurs and Their Evaluations about Managerial Environment)," *Guanli Shijie* (Management World), No.6, 1993, 128. Sample size was 2,620.

The improvement of CEO qualifications in China was not the result of market selection; instead, it was guided by government policy, as most CEOs were still under the strict control of the administrative branches of the government. About 86 to 92 percent of them were directly appointed by administrative offices and were accountable to those offices (see Table 7-7). The traditional method of controlling management personnel in the planned economy obviously remained alive in the reform period. Managers generally cared little about the evaluation of the bureau of state assets administration, indicating that the role of the office was more or less nominal; at the same time, two

[59] The CESS, "*Suzhi yu Peixun, Biange Shidai de Zhongguo Qiye Jingying Guanli Zhe: 1998 Zhongguo Qiye Jingying Guanli Zhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Qualification and Training, the Chinese Managers in the Reform Era: A 1998 Special Report on Development of Chinese Entreprenuership)," *Guanli Shijie* (Management World), No.4, 1998, 141.

[60] Ibid.

thirds of them most cared about the evaluations of the administrative offices that appointed them (see Table 7-8).

Table 7-7 How CEOs of SOEs were Appointed

Method of Selecting and Appointing	1993 (%)	1994 (%)	1997 (%)
Appointed by Administrative offices	92	86	91
Elected by the Congress of Workers and Staff, then appointed by administrative offices	4	7	4
Recruited by administrative offices through competition	3.	2	
Appointed by the board of directors	0	3	4
Other	1	2	1
Total	100	100	100

Source: The CESS, "*Xianjieduan Woguo Qiyejia Duiwu de Xingwei Tezheng Diaocha Fenxi: 1995 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Behaviors of China's Entrepreneurs: A 1995 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1995, 161; The CESS, "*Suzhi yu Peixun, Biange Shidai de Zhongguo Qiye Jingying Guanli Zhe: 1998 Zhongguo Qiye Jingying Guanli Zhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Qualification and Training, the Chinese Managers in the Reform Era: A 1998 Special Report on Development of Chinese Entreprenuership)," *Guanli Shijie* (Management World), No.4, 1998, 137. Sample size of the surveys: 1993, 2,620; 1994, 2,756; 1997, 2,415.

It is worth noting that, although the CEOs in the SOE system were called entrepreneurs in China, whether they would become good swimmers in a market economy remains a question. This author found that in 1993, about 55 percent of the directors were born after 1943 (see Table 7-6), meaning that their socialization took place during the Mao era (from 1949 to 1976). This is a generation that has never experienced China's market economy, which was destroyed by the communist regime after 1949; however, in the reform years they were given a difficult task: to build

up a modern enterprise system, with little knowledge or training. The other portion (45 percent) of the CEOs belonged to an older generation that would soon retire. They may have had their own difficulties in learning modern technologies like computers and the Internet needed in a market-oriented transition.

Table 7-8 Evaluations SOE CEOs Are Most Concerned with

Evaluation	%
Evaluation of administrative office	67
Evaluation of employees	20
Evaluation of owners	5
Social reputation	4
Evaluation of bureau of the state assets administration	1
Other	3
Total	100

Note: The CEO respondents answered the question "Whose Evaluation are You Most Concerned with?"
Source: The CESS, "*Xianjieduan Woguo Qiye Jingyingzhe de Zhiye Liudong yu Zhiyehua Quxiang: 1996 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Carrier Mobility and Professionalization of China's Managers: A 1996 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1996, 131. Sample size was 2,735.

It is worth noting that, although the CEOs in the SOE system were called entrepreneurs in China, whether they could become good swimmers in a market economy was somewhat questionable. From the age structure of the CEOs this author found that in 1993 about 55 percent of the directors were born after 1943 (see Table 7-6) and their socialization was done during the Mao era (from 1949 to 1976). This is a generation that has never experienced China's market economy which was destroyed by the communist regime after 1949; however, in the reform years they were

given an uneasy task to build up a modern enterprise system with little preparation in knowledge and training. The other portion (45 percent) of the CEOs belongs to an older generation which would soon retire. They may have difficulties in learning modern technologies such as the use of computer and the internet or new knowledge for a market-oriented transition.

Table 7-9 Autonomy of SOE Managers

Field of Decision Making	1993 (%)	1994 (%)
Production	89	94
Pricing	76	74
Sale	89	91
Purchase	91	95
Export & import	15	26
Investment	39	61
Profit distribution	64	74
Assets management	29	47
Merge	23	40
Labor management	44	61
Hiring & firing	54	73
Wage and bonus	70	86
Adjusting internal Organization	79	91
Refuse to pay arbitrary administrative charges	7	10

Note: Multiple choices.

Source: The CESS, "*Hongguan Gaige yu Qiye Fazhan, Qiyejia de Fanying yu Qiwang: 1994 Nian Zhongguo Qiyejia Wenjuan Diaocha Zhu Baogao* (Macroeconomic Reform and Enterprise Development, Managers' Responses and Expectations: A 1994 Report of the Survey among Entrepreneurs)," *Guanli Shijie* (Management World), No.1, 1995, 158. Sample size of the surveys: 1993, 2,620; 1994, 2,756.

China's enterprise reform from 1984 to the mid 1990s offered CEOs a high degree of autonomy in economic decisions, and helped to improve their managerial skills. Table 7-9 shows that, by 1994, 85 to 95 percent of SOE managers enjoyed autonomous decision making in production, sales, procurement, employee compensation, and internal organization adjustment; 60 to 75 percent had autonomy in pricing, investment, profit distribution, labor management, and hiring and firing; but their autonomy in foreign trade, asset management, and enterprise mergers was limited. Managers were appointed by government offices, and could not refuse to pay arbitrary administrative charges.

As a part of enterprise reform measures, most CEOs were required to sign a contract with government offices for management goals, such as an increase in production, sales, and profit. Consequently, the views and goals of the CEOs changed somewhat. As Table 7-10 shows, between 37 and 41 percent considered maximizing profit and increasing market share as their most important goal, while 26 to 31 percent thought establishing the reputation and expanding the size of their enterprise were the important goals. However, the percentages were not really high; in other words, more than 50 percent of the CEOs did not pay much attention to maximizing profit and increasing market share. On the other hand, about 48 percent considered increasing employees' income the most important goal. Analyzing the distribution of working time of CEOs, the author found that 45 to 57 percent spent most of their time looking for new opportunities in enterprise development and sales, 27 to 36 percent spent most of their the time on internal management, while nine to fifteen percent spent most of their time coordinating with government offices (see Table 7-11).

Table 7-10 Goals of SOE Managers

Goals	(%)
Increase employees' income	48
Maximize profit	41
Increase market share	37
Establish enterprise' reputation	31
Expand size of enterprise	26
Accomplish contracted management goals	17

Note: SOE managers answered a question: "What are the Most Important Management Goals in Your Opinion?" (Multiple choices).

Source: The CESS, "*Xianjieduan Woguo Qiyejia Duiwu de Xingwei Tezheng Diaocha Fenxi: 1995 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Behaviors of China's Entrepreneurs: A 1995 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1995, 160. Sample size: 2,756.

Table 7-11 Working Time Distribution of SOE CEOs

The Task that Occupies CEO's Time Most	1994 (%)	1996 (%)
Looking for new opportunities for enterprise development	43	…
Internal management	27	36
Sales	15	45
Coordinate with government offices	9	15
Construction project or technical upgrading project	4	-
Developing new products	-	4
Other	2	0
Total	100	100

Note: The CEOs answered a question: "What is the task that occupies your time most?"

Source: The CESS, "*Xianjieduan Woguo Qiyejia Duiwu de Xingwei Tezheng Diaocha Fenxi: 1995 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Behaviors of China's Entrepreneurs: A 1995 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1995, 160; the CESS, "*Xianjieduan Woguo Qiye Jingyingzhe de Zhiye Liudong yu Zhiyehua Quxiang: 1996 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Carrier Mobility and Professionalization of China's Managers: A 1996 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1996, 130. Sample size of the surveys: 1994, 2,756; 1996, 2,735.

A group of Chinese scholars found political mobilization and the use of "model workers," approaches to management and social control from the Soviet Union and Maoist era, were still used in some SOEs in the reform era. They reported that 23 percent of workers interviewed in their surveys thought their managers still used political mobilization as a key method to maintain worker motivation, and 40 percent said that their managers identified "model workers" for others to emulate. On the other hand, 29 percent of worker interviewees thought their managers tightened labor discipline in an authoritarian fashion.[61] In that regard, Zhao and Nichols reported that in the SOEs where they conducted interviews, the workload increased, working hours became longer, attendance controls were tightened, monetary sanctions and penalties were instituted, holidays were denied, and sick leave restricted, but "at the level of the labour process there is in fact little evidence of Taylorism or scientific management."[62] The changes in management approaches before privatization are important for researchers, because the approaches were widely employed years later, after SOEs were privatized in China, and such practices largely reconfigured the post-privatization management-worker relationship. Moreover, the authoritarian management approach in China was quite similar to that adopted by Russian managers after that country's privatization. More details on this will be discussed in chapter nine.

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[61] Zhang Qizi, "*Guoyou Qiye Zhigong dui Qiye Neibu Guanli ji Zishen Zhuangkuang de Pingjia* (The Evaluation of SOE Workers to Management and Their Own Status)," Beijing, China, *Lingdao Canyue* (Reference Materials for Leaders), No.19, 1999, 19-20. The publication was an internal circulated material, published by the Chinese Academy of Social Sciences. The survey was done in 23 SOEs of six cities by a research group of enterprise management in the Institute of Industrial Economy of the Chinese Academy of Social Sciences; and 2,678 workers were interviewed in the survey.

[62] Zhao Minghua, and Theo Nichols, "Management Control of Labour in State-owned Enterprises: Cases from the Textile Industry," *The China Journal*, No. 36, 1996, 20.

Under the planned economy SOE managers could not decide for themselves how to spend the revenues from their enterprises—this was a means of reducing the potential for corruption. After their autonomy was expanded significantly during the 1990s, the corruption of SOE managers became widespread. Two phenomena were then often discussed in China's media: "poor temple but rich monk" and "the 58-years-old phenomenon." The former referred to luxury consumption by managers as their enterprises fall bankrupt or fail to pay wages;[63] the latter involved self-enrichment by SOE managers who were seizing the last chance before retirement age. A typical case was the director of an SOE who was once honored as a National Excellent Entrepreneur, but fled China and settled down in the Philippines in 1995 with $500,000 stolen from his enterprise.[64] According to an estimate by the official labor union of Chongqing city, half of SOE losses were caused by managerial corruption.[65] In China the corruption of SOE managers before privatization carried high risks, but the privatization policies implemented from 1997 opened the door for asset stripping and, under the banner of "enterprise reform," many such activities were tolerated by the government.

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[63] Zhai Xiangdong, "*Cong 'Qiong Miao Fu Fangzhang' Shuo Qi* (About 'Poor Temple but Rich Monk)," *Renmin Ribao* (People's Daily), Apr. 5, 1996.

[64] Shen Weili, "*'Wushiba Sui Xianxiang' de Lilun Sikao: Guoyou Qiye Jianli Jingyingzhe Jiandu yu Jili Jizhi de Duice Fenxi* (A Theoretical Thinking about the '58-Year-Old Phenomenon': Analysis about Establishing Overseeing and Incentive System for SOE Managers)," *Zhongguo Gaige Bao* (China Reform News), Sept. 13, 1996.

[65] Qiao Jian, "*1996-1997 Nian Zhongguo Zhigong Zhuangkuang de Fenxi yu Yuce* (An Analysis and Forecasting about the Status of Chinese Workers and Staff in 1996-1997)," in Jiang Liu, Lu Xieyi, Shan Pianlun, Li Peilin, Huang Ping, and Lu Jianhua, eds. *Shehui Lanpishu: 1996-1997 Nian Zhongguo Shehui Xingshi Fenxi yu Yuce* (A Blue Book on Society: Analysis and Forecasting of China's Social Situation in 1996-1997), Beijing, China, China Social Sciences Press, 1997, 261.

4. Workers' Attitudes towards Enterprise Reform and Managers

In a socialist country where long-term ideological propaganda insisted that SOE managers and workers were both "masters of enterprise" with different divisions of labor, workers were particularly sensitive to managerial corruption or luxury consumption and the changing status of workers at the workplace. SOE employees were also placed in a situation of decades-long, structured dependence, relying on the socialist commitments of the state for lifelong employment and benefits. If that commitment was abandoned, how would SOE employees react? As the enterprise reform policies of the Chinese government finally targeted SOE workers, what were their attitudes towards the changes? This section will discuss how SOE workers thought of their managers in the ongoing enterprise reform.

Five nationwide opinion surveys organized by the All-China Federation of Trade Unions (ACFTU) showed that opinions of Chinese SOE workers had dramatically changed during the reform period (see Table 7-12). The orthodox political indoctrination of the communist party, with its empty slogans such as "realizing communism," attracted less and less workers, as the percentage of those who asserted the ideas dropped from 29 percent in 1982 to 15 percent in 1996. There were also far fewer respondents who answered that their highest ideal was "realizing communism" than there were communist party members in the pool of respondents, suggesting that many party members who were workers did not support the official propaganda. After 1986 only about twelve to fourteen percent of the worker respondents were interested in the propaganda slogans, such as "work for modernization" and "strive for Chinese socialism," and

from 1982 to 1992 only 20 to 26 percent of the respondents were impressed by the slogan for patriotic political mobilization ("work for a stronger and prosperous motherland").

Table 7-12 Workers' Opinions on Political and Social Issues

Highest Ideal in Life	1982 (%)	1986 (%)	1992 (%)	3/1996 (%)	6/1996 (%)
Happy family & stable life	6	11	40	29	23
Career development to realize personal value	…	…	10	19	26
More wealth	5	7	7	11	14
Realizing communism	29	25	13	17	15
Work for modernization	19	13	…	…	…
Work for stronger and prosperous motherland	22	20	26	…	…
Serve for society	…	…	3	…	…
Strive for Chinese socialism	…	…	…	12	14
Be a good worker	8	10	…	…	…
Have a good job	5	7	…	8	4
Higher social status	1	2	…	2	1
Have a beautiful wife	1	1	…	…	…
Other	1	2	0	2	1
Do not know	3	2	1	0	2
Total	100	100	100	100	100
Membership of the Communist Party	...	...	33	27	23
Membership of the Communist Youth League	…	…	8	19	24

Source: An Yuanchao, "An Important Problem Alerting us: Observing the Value Changes of Chinese Working Class from Five Opinion Surveys," in *The Forum of Workers' Movement (Gongyun Luntan*, Beijing, China, the All-China Federation of Trade Union (ACFTU)), No.11, 1996, pp.47-56; An, Yuanchao, "The Surveys about Value Changes of Chinese Working Class," Beijing, China, *Contemporary Thoughts (Dangdai Sichao)*, Feb. 1997, pp.15-23. The 1982 survey was done by the Research Dept. of the CCP headquarter and the ACFTU, sample size was 16,733; the 1986 and 1992 surveys were done by the ACFTU, and sample size was 647,112 and 48,532; and the March and June surveys in 1996 were done by the Dept. of Propaganda and Education of the ACFTU, sample size was 3,192 and 5,292.

Reading the data in Table 7-12, the author found that during the reform era, individualism and materialism gradually replaced the communist ideology that many had been indoctrinated with, and more and more workers thought that their family life, career development, and wealth were their grounding values. The percentage of such responses increased from 26 percent in 1982 to 68 percent in 1996. It is worth noting that the difference between the majority of the answers actually given in the surveys, and the politically correct responses—and the very low percentage of those who answered "do not know"—suggested that the interviewees were probably being frank when telling their opinions in interview. This may be due the fact that after the Mao era, loyalty to communist ideology was much less emphasized, and, during the reform years, materialism was no longer attacked by the propaganda machine, and was even used as an instrument of market reform. But increasing individualism and materialism did not suggest that SOE workers would seek economic independence from SOEs; on the contrary, their attitudes toward economic reform were largely influenced by policies. In fact it was exactly these changes in attitude, and the post-1996 privatization policies that had significantly negative impacts on worker interests, that caused widespread labor protests in the first decade of the 21st century in China.

Table 7-13 Employment Status of SOE Employees

Employment Status	%
Employed	96
Off-Position but not fired	3
Unemployed	1
Reemployed after dismissal	0
Other	0
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The

Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), Beijing, China, Xiyuan Press, 1999, 1302. Sample size, 32,105.

The ACFTU organized another nationwide opinion survey in the summer of 1997, right before the Chinese government took a radical step in the privatization of SOEs. The survey data provides rich information about the circumstances at the workplace and workers' attitudes toward reform policies. Below the author will use the data to analyze the employment status of SOE workers, worker income satisfaction, job satisfaction, work motivation, attitudes towards reform policies, and evaluation of management. In the summer of 1997 relatively few SOE employees were laid off (see Table 7-13); but the feeling of job insecurity among workers was relatively high—32 percent of respondents worried about it (see Table 7-14). Table 7-15 shows that sixteen percent of respondents received 400 to 500 yuan per month ($48 to $60), and 40 percent received 500-800 ($60 to $97); however, seventeen percent of interviewees reported that they were paid late (see Table 7-16), while 23 percent said that their income had recently decreased (see Table 7-17). The late payments and lower wages reflected the poor financial situation of a lot of SOEs. At the same time, 91 percent of interviewees perceived large or very large disparity in income distribution (see Table 7-18). Such perceptions undermined their confidence in the reform policies advocated by the regime.

Table 7-14 The Possibility of Being Laid-off

Possibility	%
Very likely	8
Likely	24
Hard to say	34
Less likely	19
Impossible	15
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1470. Sample size: 29,927.

Table 7-15 Monthly Income of SOE Employees

Income Level (Yuan)	%
100 and below	1
100-150	1
151-200	2
201-300	6
301-400	12
401-500	16
501-800	40
801-1,000	12
1,000 and above	10
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1329. Sample size: 29,732.

Table 7-16 Late Payment of Wage in SOEs

Answer	%
Late Payments Did not Occurred	83
Late Payments Occurred	17
Total	100
If Yes, How Long:	
1 month	21
2 months	37
3 months	15
4 months	7
5 months	3
6 months	4
More than 6 months	13
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1344, 1347-1348. Sample size, 30,288.

Table 7-17 Perceptions of Income Level Changes among SOE Employees

Types of Changes	%
Decrease a lot	5
Somehow decrease	18
No change	18
Somehow increase	55
Increase a lot	4
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1377. Sample size, 31,765.

Table 7-18 Perceptions of Disparity of Income Distribution

Perceptions	%
Very small disparity	1
Relatively small disparity	2
No disparity	6
Relatively large disparity	45
Very large disparity	46
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1386. Sample size, 31,927.

Table 7-19 Factors Negatively Affecting Working Motivation

Factor	%
Low income & benefits	41
Poor working conditions	8
Poor human relations	4
Poor enterprise prospects	15
Hopeless in carrier development	8
Managers involved in corruption	8
Unfair distribution of wages & bonuses	7
Bad personal health	3
CEOs did their jobs poorly	2
Other	4
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1533-1534, Sample size, 6,980.

Among the various factors that negatively affected worker motivation, low income and benefits, and poor enterprise prospects were two key factors of concern (see Table 7-19). Two thirds of the interviewees had never changed jobs (see Table 7-20). Interestingly, if they had to change jobs, 58 percent said they would want to work at government offices, or

government-sponsored cultural or educational institutions, where social status is high, duties light, and jobs secure; 22 percent wanted to move to other SOEs; thirteen percent would have moved to joint-venture enterprises (see Table 7-21). Obviously, such attitudes in job selection were not realistic; however it implied that if they lost their current positions at SOEs, they might not be psychologically prepared to find jobs with a lower social status.

Table 7-20 Records of Job Changes across Workplaces

Type	%
Never changed	66
Once	22
Twice	7
Three times	3
Four times	1
Five times or more	1
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1407-1408 Sample size, 30,624.

Table 7-21 Preferred Workplace if Change Jobs

Preferred Workplace	%
Government office	42
SOE	22
Rural enterprise	1
Joint-Venture Enterprise	13
Urban township-owned enterprise	0
Cultural and educational Institutions	16
Private enterprise	2
Do own business	3
Other	1
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The

Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1419-1420. Sample size, 30,514.

In terms of reform policies, worker respondents were most concerned with establishing pension insurance and medical insurance systems (see Table 7-22). SOE employees then relied upon the reimbursement arrangements for medical expenditures at the workplace, but more than 60 percent of respondents felt the reimbursement limit set by their work organizations was too low (see Table 7-23). About 30 percent of respondents reported that their workplaces did not participate in the new pension insurance system (see Table 7-24), and most interviewees whose workplaces participated in the basic pension insurance system worried that the payments from the system might be too low to cover their retirement needs (see Table 7-25). Clearly, if SOE employees were dismissed they may very likely have fallen into financial difficulty.

Table 7-22 Concerns about Social Security Issues

Types of Concerns	%
Pension insurance	70
Medical insurance	24
Unemployment insurance	6
Workplace injury insurance	0
Employee birth benefits	0
Total	100

Note: Respondents answered a question: "What part of social security system are you most concerned with?"
Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1563-1564. Sample size, 31,748.

Table 7-23 Affordability of Medical Expenditures

Answers	%
Can not Afford	22
Hardly Afford	40
Could Afford	38
Total	100

Note: Respondents answered a question: “Can You afford the reimbursement limit set by your work unit for medical expenditures?”
Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1473. Sample size, 29,866.

Table 7-24 Availability of Basic Pension Insurance

Answer	%
Yes	71
No	17
Do not know	12
Total	100

Note: Respondents answered a question: “Does your work unit participate in the basic pension insurance program?”
Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1476. Sample size, 31,058.

Table 7-25 Availability of Basic Pension Insurance

Answer	%
No	16
Hard to say	56
Somewhat	22
Yes	6
Total	100

Note: Respondents answered a question: “Could the basic pension insurance program your work unit participates in cover your primary needs for retirement life?”
Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1479. Sample size, 25,001.

Table 7-26 Confidence in SOE Reform

Answer	%
No confidence	4
Insufficient confidence	11
Hard to say	16
Some confidence	23
Have confidence	37
Have strong confidence	9
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1593-1594. Sample size, 30,188.

Chinese SOE workers were overall not very confident in the enterprise reform that had been implemented: 37 percent of interviewees were “confident,” 23 percent had “some confidence” and the rest none at all (see Table 7-26). As mentioned above, employee shareholding was an important reform policy, but only 37 percent of the SOE respondents thought it helpful for company development (see Table 7-27).

Table 7-27 Attitudes toward Employee Shareholding

Answers	%
No	5
Hard to say	58
Yes	37
Total	100

Note: Worker respondents answered a question: “Do you think that employee shareholding helps enterprise development?”
Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1569. Sample size, 28,668.

Although SOE managers were given quite a lot of autonomy, they were seemingly incapable of making significant improvements within the framework of the enterprise reform policies. About twenty percent of the interviewees thought their managers were not qualified, 27 percent of them thought their managers could not improve the low motivation of workers, and eight percent thought their managers made wrong decisions (see Table 7-28). At the same time, 26 percent of respondents indicated that their previous status as "master of enterprise" had decreased somewhat or very much during the reform era (see Table 7-29). A report from the official trade union of Henan Province noted that in a lot of loss-making SOEs, where workers could not receive wages, managers paid themselves full wages, bonuses, and subsidies, and rode around in luxury cars.[66] Such phenomena increased worker discontent. It must also be noted that the practice of tightening work discipline and putting more pressure on workers met with some resistance. According to the 1994 survey of the CESS, many of the interviewed managers reported that their lives had been threatened, or they had been attacked, by workers in response to such practices (see Table 7-30).

[66] The Trade Union of Henan Province, "*Guanyu Wo Sheng Zhigong dui Gaige Chengshou Nengli de Diaocha Baogao* (An Investigation Report about Workers' Endurance in Reform in Our Province)," Beijing, China, *Zhongguo Gongyun* (Workers' Movement in China), No.1, 1994, 10.

Table 7-28 Evaluation of Management

Evaluation	%
Our CEO should have not been appointed	12
Managers made wrong decisions	9
Made employees' working motivation low	27
Unfair distribution of wage and bonus	7
Poor qualification of managers	7
Current government policies not good	17
Other	21
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1575-1576. Sample size, 27,530.

Table 7-29 Attitudes towards Workers' Status as Master of Enterprise

Evaluation	%
Very much decreased	10
Somehow decreased	16
Hard to say	16
No change	24
Somehow increased	30
Largely increased	4
Total	100

Source: Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha: Shuju Juan* (The Survey of the Status of Chinese Staff and Workers in 1997: The Data Volume), 1698-1699. Sample size, 30,401).

Table 7-30 Frequency of Life Threat to SOE Manager

Answer	%
Never	46
Once	11
Twice	12
Three times and more	30
Not answered	1
Total	100

Note: Manager respondents answered a question: "Have You Ever been Threatened or Hurt at the Workplace?"

Source: The CESS, "*Xianjieduan Woguo Qiyejia Duiwu de Xingwei Tezheng Diaocha Fenxi: 1995 Nian Zhongguo Qiyejia Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Behaviors of China's Entrepreneurs: A 1995 Special Report on Development of Chinese Entrepreneurship)," *Guanli Shijie* (Management World), No.3, 1995, 163.

5. The Policymaking of Privatization in China

The Chinese government initiated a nationwide privatization of industrial SOEs in late 1997, but not because it had finally completed a blueprint for reform. Actually, the privatization policy had only fuzzy goals and unclear methods, and the government did not really know where the reform would ultimately go. To implement the policy the government decided to lay off millions of SOE workers, although a necessary precondition for the massive layoff, the establishment of an urgently needed social security system, had not been achieved. So far almost no observers of China's privatization have evaluated this unusual policymaking process and its contexts. This author argues that the reason the Chinese government made the decision so hastily was that a potential domestic financial crisis caused by the state-owned industries troubled the regime, and it thus chose radical SOE reform program as a way to rid itself of the burden.

5.1 The Coming Threat of Financial Crisis and Obstacles to Privatization

From 1992 to 1996, the financial status of state-owned industries rapidly deteriorated, despite the Chinese government trying various reform policies. One of the reasons was the increasing production costs due to price liberalization and the growing expenditures to maintain the social contract discussed in Chapter four. Another reason was the high tax rate. Although China made

great progresses in dismantling the planned economy from the 1980s, and no longer needed a large government apparatus to directly control economic activity, its bureaucratic system kept expanding and consuming more of the state's financial resources. China's official statistics showed that the number of government cadres grew from five million to eleven million between 1980 and 1997, and government expenditures rose from seven billion yuan in 1980 to 114 billion yuan in 1997, about a five-fold increase.[67] The tax rate was correspondingly high, averaging 86 percent from 1980 to 1993 for the state-owned industries.[68] Remaining SOE profits could only pay the medical expenses of staff and workers, and the enterprises did not have capital for investment, instead relying heavily on loans from state banks. Yusuf et al noticed that the profits of industrial SOEs from 1996 to 1998 fell to two percent of their gross value of outputs, and the losses of SOEs rose to over three percent of their gross outputs; low profitability, in turn, meant that nonperforming loans to the state enterprises continued to accumulate in state commercial banks.[69] It should be pointed out that the low profit rate could partly be the result of profits being concealed through accounting tricks by SOE managers to avoid high tax rates.

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[67] The number of cadres included all the people working in the offices of governments and the communist party at all levels. The government expenditures were cited from the item "expenses of government administration" from the fiscal budget. After deducting the inflation factor by using GDP deflator (323 Percent from 1981 to 1997), the increase of the government expenditures at constant prices was 525 percent from 1981 to 1997. During the period, the annual average wage of the cadres increased from 800 yuan to 5,526 yuan, an increase of two-fold after deducted inflation influence. About 85 percent of the increase of the government expenditures could be explained by the increase of cadre numbers and wages. See *Zhongguo Tongji Nianjian 1998* (Statistical Yearbook of China 1998), compiled by China's State Statistics Bureau, Beijing, China, the China Statistics Publishing House, 1998, 55, 57, 133, 161 and 276.

[68] Yang Peixin, "*Dui Guoyou Qiye Gaige Wenti de Tantao* (An Exploration of SOE Reform)," Beijing, China, *Zhongguo Gongye Jingji* (China's Industrial Economy), No.7, 1995, 70.

[69] Yusuf Shahid, et al, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 77-78.

From 1993 discussions about the rapidly growing debt-asset ratio of SOEs became a hot topic in Chinese policy circles, reflecting increasing worry about the financial sustainability of state-owned industries and the state banking system.[70] The debt-asset ratio of state-owned industries rose from 58 percent in 1990 to a dangerous level of 90 percent in 1996 (see Table 7-2). A 1996 report revealed that in more than 20,000 SOEs in 18 cities the debt-asset ratio of fifteen percent of the enterprises was already higher than 100 percent.[71] The debt-to-asset ratio in companies in Western European countries and North America was usually 45 to 60 percent, and Japan about 62 percent;[72] an average 90 percent debt-asset ratio in China implied that if the trend continued for another two to three years, the debts of the state-owned industrials would exceed their assets. The Chinese government became alert to the danger and determined that it must act, before a crisis. Moreover, the Asian financial crisis in 1997 reminded the government that when the financial health of their main debtors was extremely poor, the stability of China's state banking system and that of the regime might be shaken.

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[70] Yang Peixin, "*Dui Guoyou Qiye Gaige Wenti de Tantao* (An Exploration of SOE Reform)," 70; Guo Shuqing, "*Jiji Cujin Cunliang Zichan de Liudong he Chongzu* (Actively Promote Reorganization of State Assets)," *Zhongguo Gaige Bao* (China Reform News), Aug. 18, 1995; Zhang Jing, "*Guoyou Jingji Zhaiwu Chongzu Shizaibixing* (It is Necessary to Reorganize Debts of the State-owned Economy)," *Jingji Cankao Bao* (Economic Information Daily), Oct. 31, 1996; Chen Zengjun, "*Guoqi Zhaiwu: Guimo Daodi you Duo Da?* (How Large were the Debts of SOEs)?" *Jingji Ribao* (Economic Daily), Jan. 23, 1997; Gao Shangquan, "*Guoyou Qiye Zhidu Chuangxin yu Ziben Shichang Fazhan* (Institutional Innovation of SOE System and Development of Capital Market)," *Jingji Cankao Bao* (Economic Information Daily), Sept. 30, 1997.

[71] Liu Hongcan, and Zhan Zhongde, "*Pochan Da Zhendang* (The Shock of Bankruptcy)," *Jingji Cankao Bao* (Economic Information Daily), Aug. 3, 1996.

[72] Li Pumin, "*Guoyou Qiye Zichan zhong Zhaiwu Bilu Wenti de Chubu Fenxi* (An Analysis of the Debt Ratio in SOE Assets)," Beijing, China, *Zhongguo Gongye Jingji* (China Industrial Economy), No.6, 1995, 19; Jia Huaqiang, "*GuoQi: Shui Lai 'Da Gong Fang Jian'* (Who Could Provide Loans to SOEs)?" *Zhongguo Gaige Bao* (China Reform News), Apr. 30, 1997.

From the beginning of 1997 media in China began to report frankly on the accumulating problems of SOE debts, losses, and redundant labor, as a means of agitating for further SOE reforms. For instance, the deputy director of the State Commission for Economic Reform published an article in which he admitted that the problems of SOEs had not improved over the past few years. He said: "If we do not deeply grasp reform… the debts of all SOEs might exceed their assets, and there would appear two serious consequences: the first would be more and more laid-off employees… and the second is that accumulated non-performing loans could exceed a safe limit in the state banking system… thus influencing the stability of the whole economy."[73]

Another important concern that precipitated the government to make the decision to privatize was the urgent need to join the World Trade Organization (WTO). As more foreign direct investment (FDI) flowed into China during the 1990s, China had to join the WTO in order to get favorable trade conditions for expanding its exports to the world market, particularly to the U.S. market. Actually, since May 1997, the Chinese government had already begun secret negotiations with the U.S. government for China to join the WTO.[74] As part of meeting some WTO requirements, the Chinese government had to privatize SOEs.

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[73] Yang Qixian, "*Zhidu Chuangxin! Zhidu Chuangxin! Zhidu Chuangxin!* (Institutional Innovation! Institutional Innovation! Institutional Innovation!" *Jiefang Ribao* (Liberation Daily), Jan. 8, 1997; the article was republished on *Zhongguo Gaige Bao* (China Reform News) on June 2, 1997, with a different title "*Shenhua Guoyou Qiye Gaige Ke Bu Rong Huan* (Deepening SOE Reform is of Great Urgency)."

[74] Zhao Yining, "*Zhu Rongji Zongli Jueduan Zhong Mei Tanpan de Gushi* (The Story about How Premier Zhu Made Decisions for the Sino-US WTO Negotiation)," Guangzhou, China, *Ershiyi Shiji Jingji Baodao* (The 21st Century Economic Report), Nov. 19, 2011).

5.2 China's Privatization Policy: "Grasp the Big, Let Go of the Small"

1997 was the turning point in China's SOE reforms, when the Chinese government realized that the critical moment for making decisions on privatization had come. If the state wanted to prevent the banking system from collapse, it could no longer wait. Chinese leaders finally approved a radical policy for SOE reform and paved the road for the privatization of industrial SOEs, although "privatization" as such was not mentioned at all.

In September 1997, the Chinese government announced its new decision of "Escaping Difficulties within Three Years" (meant to run from 1998-2000), through the "Grasp the Big, Let Go of the Small" (*zhuada fangxiao*) policy.[75] The new policies did not include a clear-cut program for the operation of the new round of the SOE reform, nor explain how the process would be regulated, nor outline the possible activities that might take place once the policy was implemented. The most important and explicit expression of the new decision was that the central government would focus on restructuring and consolidating the strategically important large SOEs; at the same time, implicitly, the decision suggested that the state could no longer save all other SOEs, and they should try to "enliven" (*gaohuo*) themselves by any means—privatization not excluded. Although the government officially never used the term "privatization" in its propaganda, in October 1997, China's Premier of the State Council, Li Peng, told the director of the World Bank that "China could sell a small portion of SOEs."[76] In other words, China's privatization of SOEs

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[75] "*Jingji Gongzuo de Yi Xiang Poqie Renwu* (An Urgent Task in Managing SOEs)," *Jingji Ribao* (Economic Daily), Oct. 23, 1997.

[76] "*Zhongguo Keyi Jiang Guoqi Yi Xiao Bufen Chushou* (China Can Sell a Small Portion of SOEs)," *Zhongguo Gaige Bao* (China Reform News), Oct. 15, 1997.

was not a secret to foreigners, but for ordinary Chinese SOE reform was something else.

At the end of 1997, the Chinese central administration held a national economic work conference and set up a goal for SOE reform: "Within three years, get most of the 16,000 large and medium size SOEs out of difficulty through reform, reorganization, restructuring and management improvement, and strive to build up a modern enterprise system for SOEs before the end of the 20th century; at the same time, free more than 52,000 small SOEs for enlivening."[77] The official conference documentation contains a lot of policy terms—reform, reorganization, restructuring, management improvement— which had been used for years in China. No new approach was being advised. When referring to the enlivening of small SOEs, the policy did not explain how they would be freed for enlivening. Actually, behind the official discourse, a new policy was being offered: the central administration would no longer regulate what the small SOEs could or could not do. It was precisely in this manner that the central government let SOE managers and local governments look for solutions by themselves, thus quietly opening the door for the privatization of small SOEs as local players chose whatever methods suited them to "enliven" the ailing enterprises.

[77] "*Nuli Shixian Guoqi Gaige Sannian Mubiao* (Work Hard to Realize the Three-year Goal of SOE Reform)," *Jingji Ribao* (Economic Daily), Jan. 5, 1998.

6. How Did the Chinese Government Overcome the Obstacles to *Gaizhi*?

The Chinese government encountered thee dilemmas when attempting to carry out privatization: it would create an enormous numbers of unemployed workers, there was no money to pay SOE debts, and no money to pay social security benefits for SOE workers. These issues were central obstacles in China's privatization. Some officials made estimates of the huge expenses: if the state wanted to bring the debt-asset ratio down by 20 percent, with available fiscal revenue it would take more than 40 years; if the government wanted to pay every laid-off worker unemployment compensation equal to two years of wages, and set up a nationwide pension system, it would need 1,330 billion yuan, almost twice the fiscal revenue of 1996.[78] The cost analysis suggested that the Chinese government simply did not have the money to pay for privatization. As obtaining sufficient resources to settle debts and set up a pension system turned out to be an impossible mission, the government chose an approach that would cost the budget little: removing the fiscal burden from the state and setting them on the shoulders of SOE managers and workers. A democratic regime would face stiff social resistance if it tried to adopt such an irresponsible policy; but an authoritarian communist party has advantages, not being fettered by elections, and able to restrict press reporting and political speech. Although cadres in the official labor unions in China tried to defend the interests of SOE workers by proclaiming that the workers were "master" of their

[78] Gao Shangquan (Deputy Director of State Commission for Economic Reform), "*Guoyou Qiye Zhidu Chuangxin yu Ziben Shichang Fazhan* (Institutional Innovation of SOE System and Development of Capital Market)," *Jingji Cankao Bao* (Economic Information Daily), Sept. 30, 1997.

enterprise[79] and should not be targeted by the reform,[80] their influence was gradually marginalized and their voice silenced by the central government after 1997.

6.1 The Nationwide Lay-off Policy and Social Responses

To reduce redundant labor and pave the road for privatization, the Chinese government laid off millions of SOE workers. In 1998, the Chinese central government declared that the key point of "escaping the [SOE] difficulties within three years" was to reduce redundant labor, and chose the textile industry (many enterprises in the industry were SOEs) as a breakthrough point for implementing a new policy named "reducing redundancy to increase efficiency" (*jianyuan zengxiao).*[81] The policy clearly suggested that only when redundant labor was removed could China's SOEs smoothly move forward for transformation and benefit from improved efficiency. It emphasized that redundant labor laid behind inefficiency in SOEs, but refused to acknowledge the failures of the SOE system, the wrong decisions of the government,[82] and enterprise

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[79] Su Liqing (Chairman of the Zhejiang Province Federation of Trade Union), "*Gongren Zhurenweng Diwei de Ruogan Kanfa* (Several Points about the Master Position of Workers)," Beijing, China, *Gongyun Luntan* (Forum for Labor Movement), No. 10, 1996, 41-46.

[80] The Research Association of the ACFTU, "*Tuijin Guoyou Qiye Gaqige zhong de Jiege Wenti* (Several Issues to be Concerned about in Promoting SOE Reform)," *Gongyun Luntan* (Forum for Labor Movement), No. 11, 1996, 1-4.

[81] The State Commission for Economy and Trade of China, "*Guanyu 1998 Nian Guoyou Qiye Gaige he Fazhan Gongzuo de Yijian* (On the Work of SOE Reform and Development in 1998)," *Jingji Ribao* (Economic Daily), June 22, 1998.

[82] For example, under Mao's leadership, in order to prevent China's national economy from being destroyed by a possible Sino-Soviet war, from early 1960s to early 1970s a lot of SOEs were established in mountain areas of the hinterland provinces. They were usually far away from industrial centers, consumer market and raw materials, and had poor transportation conditions; moreover, isolated in small towns, the SOEs had to develop their own service facilities for employees. Therefore, the production costs of the SOEs were usually very high.

mismanagement. SOE employees would be scapegoated and made to pay for the failures of state socialism. Ultimately, it was the state and SOE managers that "escaped the difficulties" of SOEs; but workers and their families were thrown into long-term economic difficulties. Chan writes: "Today the tacit consensus, too embarrassing to be openly expressed by a regime that still calls itself socialist, is that workers must be sacrificial lambs for the nation's economic advancement. In the Communist Party, the government, and intellectual circles, almost all policy proponents have chosen to leave labor issues out of their blueprints for China's development."[83]

Table 7-31 Urban Public Opinions: Top Eight Concerns

Concerns	1993 (%)	1994 (%)	3/1995 (%)	11/1995 (%)	10/1996 (%)	12/1997 (%)
Income/wage system reform	11	12	30	…	…	…
Housing system reform	15	18	…	21	18	…
Anti-corruption	13	…	39	31	23	88
Price reform	11	14	…	…	…	…
Inflation	10	21	66	35	21	35
Children's education	8	…	32	26	14	…
Maintain public order	6	11	37	52	48	77
Gap between rich & poor	6	7	…	…	…	…
Pollution	…	…	21	…	…	84
Social security system	…	…	…	11	31	67
Unemployment/Lay off	…	…	22	…	15	93
SOE bankruptcy	…	…	…	7	7	92

Note: Multiple choices.

In the first half of the 1970s, Mao ordered to develop local small industries in each county, therefore in many provinces small SOEs were established in every county, and these small SOEs usually produced similar low quality products with high costs for textile, chemical fertilizer and machine-tool industries. Under the planned economy, these SOEs survived; but after market-oriented reforms were initiated they could hardly compete with the enterprises in industrial centers, thus became loss makers. The performance failure of the SOEs was related to the location mistakes made by governments; workers were innocent.

[83] Anita Chan, and Robert, A. Senser, "China's Troubled Workers," *Foreign Affairs*, March/Apr. 1997, 116.

Source: Yuan Yue, "*1996-1997 Nian Zhongguo Chengshi Shehui Wending yu Fazhan Zhuangkuang de Gongzhong Xintai Fenxi* (An Analysis about Public Opinions in Terms of Stability and Development of Chinese Urban Society in 1996-1997)," in Jiang Liu, Lu Xieyi, Shan Pianlun, Li Peilin, Huang Ping and Lu Jianhua, eds. *Shehui Lanpishu: 1996-1997 Nian Zhongguo Shehui Xingshi Fenxi yu Yuce* (Blue Book on Society: Analysis and Forecasting of China's Social Situation in 1996-1997), Beijing, China, China Social Sciences Press, 1997, 81; "*Zhongguo Shimin Guanzhu Redian You Bian* (Top Concerns of Chinese People Have Changed)," Beijing, China, *Zhongguo Shichang Jingji Bao* (Chinese Market Economy News), Feb.6, 1998. All the surveys were done by China's Zero Point Public Opinion Survey Company, a government licensed company for public opinion survey. The surveys from 1993 to 1996 were done in large cities such as Beijing, Shanghai, Guangzhou, Wuhan, Ha'erbin; and the 1997 survey was done in 10 cities including Beijing, Shanghai, Guangzhou, Chengdu, Nanning, Wuhan, Xi'an, Jinan, Shenyang, Xiamen with a sample size of 5,000 interviewees.

Before privatization, in Chinese urban society most employed people worked for SOEs, government sponsored organizations, or government offices. Because SOE reform measures could greatly influence the living status of most urban families, in Chinese cities many paid attention to the reform measures. From 1993 to 1997, among of the top twelve concerns that Chinese urban respondents expressed in public opinion surveys, half referred to the consequences of SOE reforms, such as the reform of the wage system, housing system reform, anti-corruption, social security issues, unemployment, and bankruptcy (see Table 7-31). At the end of 1997, the "reducing redundancy to increase efficiency" and *gaizhi* policies caused panic in China. A public opinion survey showed that 92 to 93 percent of urban respondents said that they worried about unemployment and SOE bankruptcy, and two thirds were concerned that the social security system would not be robust enough to support them (see Table 7-31). It was in such social circumstances that China began its privatization.

6.2 The Debt-Equity Swap Policy

The second obstacle to privatization in China was the huge debts of SOEs and the equivalent nonperforming loans (NPLs) in the state banking system. According to Garnaut, et al, "NPLs were officially estimated at 25 percent of outstanding loans, but the true share is likely to be higher."[84] Lardy points out: "China cannot allocate losses to private shareholders via bank liquidation for the simple reason that China's banks are state owned. There are no private shareholders to absorb losses. Even if they were privately owned… liquidation really would mean the allocation of losses to depositors."[85] To solve the issue the Chinese government introduced the American model of the Resolution Trust Corporation (RTC)[86] and formed four asset management companies (AMC) in Aug. 1999,[87] to take over more than $170 billion in NPLs from the big four state-owned banks.[88] But soon, new NPLs emerged on the balance sheets of the banks, and, "according to the recent data from the central bank, after $170 billion in NPLs were removed to the AMCs, the percentage of NPLs in outstanding loans from banks remains as high as 25 percent, which implies a great danger."[89] In 2005 the four AMCs once again took over $170 billion worth of NPLs from the four banks.

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[84] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 48.

[85] Nicholas Lardy, *China's Unfinished Economic Revolution*, Washington, DC, the Brookings Institute. 1998, 147.

[86] RTC was a U.S. Government-owned asset management company and charged with liquidating the assets of S&Ls, formed after the savings and loan crisis of the 1980s.

[87] Rong Yue, "*Zhuai Zhuan Gu: Guoqi Jiekun de Yi Ji Liangyao* (The Debt-Asset Swap: A Recipe for Solving SOE Financial Difficulties," *Zhongguo Gaige Bao* (China Reform News), Aug. 4, 1999.

[88] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 6.

[89] Wu Jinglian, "Market Economy is Supposed to be an Economy Based on Trust and Rule of Law," a speech on April 7, 2002, Shanghai, China, *Wenhui Bao* (Wenhui Daily), Apr. 8, 2002; also in Wu Jinglian ed. *Zhuangui Zhongguo* (China in Transition), Chengdu, China, Sichuan People's Press, 2002, 332.

Although the AMCs helped the state-owned banks clean their balance sheets, the performance of the AMCs was still quite controversial in China.[90] As a part of the AMC program, the debt-equity swap (*zhai zhuan gu*) was chosen as a key means of reducing the debt burden of large SOEs. Garnaut, et al out: "580 SOEs, accounting for about 40 percent of the state sector's assets and sales, have been selected for debt-equity swaps… Debt-equity swaps were introduced by the central government in 1999 to alleviate the huge nonperforming loan problem."[91] The first step of the debt-equity swap in China was for the banks to recategorize their NPLs to SOEs as equity investments: so the SOEs no longer serviced the debts and their balance sheets were primed for listing on the stock market. Then the NPLs were transferred from the state-owned commercial banks to the state-owned AMCs, and the AMCs paid the banks with a loan from the central bank, so state-owned commercial banks' balance sheets were also cleaned up for initial public offerings (IPO). Finally, after their balance sheets were cleaned up, both the SOEs and the banks were able to raise capital through the stock market to improve their poor financial situation. It was also assumed that, after the debt-equity swap, the AMCs would become large shareholders in SOEs and improve corporate governance and, after the performance of the industrial enterprises was improved and their stock prices went up, be able to sell off their equity stake and make back the investment.[92] China's central government was advocating this approach in the media at the end of the 1990s.

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[90] Zhang Yuzhe, and Wen Xiu, "*Zichan Guanli Gongsi Qilu* (The Wrong Way of the Transformation of AMCs in China)," *Caijing* (Finance and Economy Magazine), No. 10, May 12, 2008, 77-80.

[91] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 48.

[92] Chen Yan, "*Zhengfu Shi Chu 'Shashoujian': Jiedu Zhai Zhuan Gu* (The Best Weapon of the Government: Interpreting the Debt-Equity Swap)," *Jingji Ribao* (Economic Daily), Sept. 9, 1999; Zhao Haikuan, "*Zhai Zhuan Gu: Zhenxing Guoqi Xian Shuguang* (The Debt-Equity Swap: The Dawn for Saving SOEs)," *Jingji Ribao* (Economic Daily), Sept. 13, 1999.

The most controversial issue in this debt-equity swap process in China was whether the approach could really produce a new system for large industrial SOEs, or whether it simply served as a state-sponsored debt laundering for stock market listing. An author pointed out that: "The critical thing for the success of the debt-equity swap is to have the industrial enterprises reorganized by the AMCs."[93] Some officials and scholars expressed their concern that this approach might simply become an opportunity for SOEs to offload their debt burdens, and nothing more, as the policy focus was mainly on reducing the financial risks in the banking system and of large SOEs.[94] Indeed, ten years later, it turns out that the results have been unsatisfying indeed, much worse than what the government originally expected.[95] AMCs have played little active role in improving the corporate governance of industrial SOEs with which they performed the debt-equity swaps.[96]

The debt-equity swap plan was only available for selected large SOEs, and most SOEs had to look for other financing options to solve their debt problems.

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[93] Du Jun, "*Zhai Zhuan Gu: Da Han Zhi Nian Wang Yun Ni* (The Debt-Equity Swap: Expecting Rains during the Draught)," *Zhongguo Gaige Bao* (China Reform News), Nov. 15, 1999.

[94] "'*Zhai Zhuan Gu' Ying Zhuan Chu Xin Jizhi* (The 'Debt-Equity Swap' Should Produce a New System for the Enterprises)," *Zhongguo Gaige Bao* (China Reform News), Oct. 19, 1999; Yan Ruqi, "*Zhai Zhuan Gu: Hao Juben Geng Xuyao Hao Daoyan* (The Debt-Equity Swap: A Good Libretto Really Needs a Good Director)," *Zhongguo Gaige Bao* (China Reform News), Nov. 1, 1999.

[95] Lin Huawei, and Cheng Jie, "*Zichan Guanli Gongsi Jiaoxun* (The Lessons of the AMCs in China)," Beijing, China, *Caijing* (Finance and Economy Magazine), No. 14, July 11, 2005, 52-54.

[96] Zhang Yuzhe, and Wen Xiu, "*Zichan Guanli Gongsi Qilu* (The Wrong Way of the Transformation of AMCs in China)," 78.

6.3 The Unresolved Issue Regarding Social Safety Net

The third obstacle to privatization was the absence of a social security system. China's social security system was different from that of the former Soviet Union. From the 1930s the Soviet Union established a state-sponsored system: urban residents could receive a pension equal to half of the average wage of workers, but its increase was not linked to inflation;[97] unemployment benefits were available;[98] medical services were provided by the state (though the budget, facilities and training of physicians were insufficient);[99] and in the 1970s income supplements for low-income families and cash allowances for children were added. The Soviet social security system was later extended to cover collective farm peasantry,[100] thus "by the end of 1970s the Soviet social security system covered all industries and social groups."[101] In China, a state sponsored social security system that just covered pensions and medical services was only available for the employees of government offices and state-funded institutions, such as colleges, media organizations, hospitals, schools, etc.; but the employees of private enterprises and the majority of the Chinese population—the peasants—never had such privileges, while the pensions and medical expenditures of SOE employees were paid for by each enterprise. Until the 1990s there was no unemployment

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[97] David Lane, *Soviet Society under Perestroika*, London and New York, Routledge, 1992, 344-345; Alec Nove, *The Soviet Economic System*, Boston, MA, Unwin Hyman Inc, 1986, 229; Mervyn Matthews, "Elitism in Postcommunist Russia: Some Interim Comments," in James R. Millar, and Sharon L. Wolchik, eds. *The Soviet Legacy of Communism*, the Woodrow Wilson Center Press and Cambridge University Press, 1994, 326-327.

[98] William Moskoff, "Unemployment in the Former Soviet Union," in James R. Millar, and Sharon L. Wolchik, eds. *The Soviet Legacy of Communism*, 365-366.

[99] David E. Powell, "Aging and the Elderly," in Anthony Jones, Walter D. Connor, and David E. Powell, eds. *Soviet Social Problems*, Boulder, CO, Westview Press, 1991, 175-177.

[100] Linda J. Cook, *The Soviet Social Contract and Why It Failed: Welfare Policy and Workers' Politics from Brezhnev to Yeltsin*,. Cambridge, MA, Harvard University Press, 1993, 49.

[101] David Lane, *Soviet Society under Perestroika*, 339.

insurance in China. Moreover, from the 1950s to the first half of the 1990s, neither the state nor SOEs had deposited or invested a single *fen* (a cent) for future payments of pensions and unemployment benefits to SOE employees; the state was thus able to extract the largest possible share from SOEs for its daily expenses.

During the reform years a nationwide social security system was urgently needed, and the state was obligated to provide pension, medical expenditures, unemployment benefits, low-income family subsidies, etc., to the employees of the bankrupted or privatized SOEs. Such expenditures might be understood as a liability of the state owed to SOE employees, because in past decades, in order to extract the maximum financial resources for various industrial and military projects, the state had kept the wages of SOE employees very low, meaning employees were unable to save enough money for their retirement—but the government effectively promised through institutionalized arrangements (the social and economic dependence on enterprise[102]) that it would provide lifetime-employment, free medical services, and pensions for all SOE employees. By the time the privatization policy tore up the social contract maintained for decades in China, a social security system for former SOE employees had not yet been established. From the early 1990s to the beginning of the 21st century, the government failed to make sufficient effort to establish such a system. Instead, it allowed eleven relatively rich state-owned industries, such as railway services, postal services and the state banking system, to establish their own social security systems, and expected local governments to take over the social security liabilities of other poorer SOEs

[102] Andrew Walder, *Communist Neo-Traditionalism: Work and Authority in Chinese Industry*, Berkeley, CA, University of California Press, 1986, 14-17.

previously controlled by central ministries. When more and more SOE employees were laid off, the State Council of China ordered in a decree that the laid-off employees should still be attached to their previous work organizations, and the enterprises were responsible for supporting a basic living.[103] At the same time, through the "letting go of the small" policy, the central government actually removed its obligations of arranging the social security payments for the laid-off and on-post workers, and placed those responsibilities on the shoulders of SOE managers and local governments.

While the central government did not take responsibility for establishing a nationwide social security system, local governments lacked financial resources to do so, because a reform of the tax regulations in 1994 significantly increased the share of fiscal revenues received by the central administration and reduced that given to local governments. At that time, most SOEs were in poor financial straits and did not have sufficient resources to pay currently due and future social security expenditures. The SOE's burdens looked like this: the total annual expenditures of the basic social security payments, including pensions, medical expenses and unemployment compensation were 60 percent of the total amount of employees' average wage; of which, the contributions of current workers could only cover about 15 percent, with the rest of the financial burden being the liability of the enterprise.[104] Therefore, from the point of view of SOE managers and local governments, the top priority of SOE transformation became how to find money to pay the social security costs.

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[103] The No.111 Decree of the State Council of China, "*Guoyou Qiye Fuyu Zhigong Anzhi Guiding* (The Regulation for Helping Settle down the SOE Redundant Employees)," *Renmin Ribao* (People's Daily), Apr. 28, 1993.

[104] Niu Renliang, "*Guanyu Chongjian Woguo Shehui Baozhang Zhidu de Jige Wenti* (Several Issues on Re-establishing Social Security System in China)," *Renmin Ribao* (People's Daily), March 8, 1995.

The author would like to suggest that, since the central government laid its obligations and liabilities of the social security payments on the shoulders SOE managers and local governments, a consensus was established between the central government and local governments and SOE managers, i.e. if the central government did not provide financial resources for the payments, it had to allow local governments and SOE managers to handle problems in whatever way they saw fit. At the same time, the only thing that would motivate SOE managers and local officials to solve these problems was the potential for personal profit in a spontaneous privatization.

7. Deregulating Privatization of Small SOEs and Controlling that of Large SOEs

From the end of 1997 "transforming the SOE system" became a popular slogan in China, though it was never clarified to what kind of new system the small SOEs were being transformed. Huang writes: "'Letting go of the small' meant that the government vowed support for privatization of small SOEs… These methods include straightforward sales to private investors, managerial restructuring, alliances with other firms, mergers, leasing, managerial contracting, and employee stock options."[105] During the period from 1998 to 2003, the Chinese government at different levels paid most attention to the fund shortage for *gaizhi*; but, "[N]o rules or procedures for regulating transactions of state assets were set up, while selling off SOE assets became a heat wave."[106]

[105] Huang Yasheng, *Selling China: Foreign Direct Investment during the Reform Era*, New York,, Cambridge University Press, 2003, 131.

[106] Xie Heng, "*Shi Wan Yi Guoyou Zichan Chongzu de Caifu Jihui* (The Opportunities in Reorganizing 10 Trillion State Assets)," Beijing, China, *Sanlian Shenghuo Zhoukan* (Life Week Magazine), No.47, Dec. 15,

Naughton points out that the entire *gaizhi* process was highly decentralized and run by local governments: since there had never been a clearly articulated rationale for the privatization, or even an announcement that privatization had been adopted as a policy, the privatization had gone forward at a pace selected by local governments and, implicitly, firm managers; locals did not have a rationale for holding on to SOEs, they only had an instruction to maintain the state's interests; thus, the privatization was delayed or accelerated according to local interests, and this fact inevitably opened up a wide scope of abuse.[107]

Occasionally, some abuse cases were reported by media, and the central government responded by sending investigation groups around the country. It seemed that the central government preferred dealing with the problems case by case, rather than setting up rules as early as possible to prevent similar abuses from taking place elsewhere. For example, at the end of 1999 the city government of Changsha in Hunan Province carried out a program to privatize some SOEs into the hands of managers and workers of the enterprises. A key policy offered by the local privatization program was that all SOE assets accumulated after 1984 were defined as properties collectively owned by insiders. The policy gave quite a large portion of assets of SOEs in the city as gifts to insiders, as a convenient means of implementing the privatization.[108] After media in China exposed the case, an investigation group from the central government went to the city in May 2001, and

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2003, 28-31.

[107] Barry Naughton, *The Chinese Economy: Transitions and Growth*, Cambridge, MY, the MIT Press, 2007, 324.

[108] Fang Dafeng, "*Changsha: Hui Bie Guoqi* (Changsha: Good Bye to SOEs)," *Caijing* (Finance and Economy Magazine), No.9, Sept. 5, 2000; Shi Dong and Zhao Xiaojian, "*Shi Wan Yi Guozi Zouxiang* (How Have Ten trillion State Assets been Managed)," *Caijing* (Finance and Economy Magazine), No.22, Nov. 20, 2002, 34.

concluded that "the willingness for reform is good, but the method of distributing SOE assets to insiders at discounted prices is incorrect."[109] Then the local government changed the privatization program of two large SOEs, and no longer allowed insiders to obtain SOE assets at discounted prices.[110] But the central government did not take any further steps to set up regulations for privatizations taking place across China. It meant that, even after the conclusion of the above investigation was widely reported, similar practices still took place around the country. This will be discussed more fully in chapter eight.

Moreover, after privatization was initiated nationwide, the Chinese central government in 1998 made a surprising decision: It shut down the Bureau of State Assets Administration, at the time it was most needed. The Bureau and its local offices were established in 1988 to improve the chaotic status of the state assets administration in China; it functioned under the State Council as a ministry, and was in charge of protecting and overseeing public properties and approving transactions of state assets. However, in 1998, exactly when many local governments and SOE managers were selling off small and medium-sized SOEs, and the appraisals and transactions of huge amounts of SOE assets needed approvals, the Bureau and its local offices were shut down and a part of its functions were transferred to the State Assets Appraisal Office under the Division of SOEs in the Ministry of Finance. After the Bureau was closed, only the asset transactions of a few large SOEs were reported

[109] "*Zhu Rongji Zongli Guanxin Changsha Guoqi Gaizhi bing Geiyu Zhishi* (Primier Zhu Rongji Cares about the SOE Privatization in Changsha city and Gave Instructions)," *Ershiyi Shiji Jingji Baodao* (The 21st Century Economic Report), Sept. 10, 2001.

[110] Fang Dafeng, "*Changsha: Hui Bie Guoqi* (Changsha: Good Bye to SOEs);" "*Zhu Rongji Zongli Guanxin Changsha Guoqi Gaizhi bing Geiyu Zhishi* (Primier Zhu Rongji Cares about the SOE Privatization in Changsha city and Gave Instructions)."

to the office for approval.[111] Later, the State Assets Appraisal Office was also closed.[112] Consequently, after 1998 at different local levels, no government office was responsible for state assets administration,[113] and there emerged a nationwide institutional vacuum of oversight of SOE asset appraisals and transactions. In 2007, a Chinese scholar stated that the overall sense of privatization in China could be described with three terms: unnamed, lawless, and disorderly (though he did not provide data to support the conclusion).[114]

Unlike in Russia where the central government established offices of the State Property Committee for privatization, and the privatization program of each SOE was sent to the offices for appraisal and approval, the Chinese central government shut down the only governmental branch that was in charge of state assets administration, thus devolving power to local government officials who could then, along with SOE managers, engage in unsupervised asset stripping. During the late 1990s and the early years of the first decade of the 21st century, the issue of the institutional vacuum in administering state assets was a hot topic in China's policy circles; the central government was obviously aware of the problem and promised many times that it would solve it. But the central government did not take any action before the privatization of small SOEs was done. During the

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[111] Shi Dong and Zhao Xiaojian, "*Shi Wan Yi Guozi Zouxiang* (How Have Ten trillion State Assets been Managed)," *Caijing* (Finance and Economy Magazine), No.22, Nov. 20, 2002, 25-26.

[112] Li Hongbing, "*Caizhengbu Jianyi Zanting MBO* (The Ministry of Finance Suggested Temporarily Stopping MBO)," *Ershiyi Shiji Jingji Baodao* (The 21st Century Economic Report), Mar. 27, 2003.

[113] There were three exceptions. In Shanghai and Wuhan city the State Assets Administration Commission was established in 1993 and 1994; and in Shenzhen city the State Assets Investment and Administration Company was established in 1992. See Shi Dong and Zhao Xiaojian, "*Shi Wan Yi Guozi Zouxiang* (How Have Ten trillion State Assets been Managed)," *Caijing* (Finance and Economy Magazine), No.22, Nov. 20, 2002, 27, 29.

[114] Hu Jingbei, "*Guoqi Siyouhua Xu Lifa Jiejue* (SOE Privatization should be Regulated by Laws)," May, 11, 2007 (http://finance.sina.com.cn/economist/jingjixueren/20070511/11563583536.shtml*)*.

period in which the state assets administration was absent, there were no regulations or detailed policies for guiding privatization. SOE managers and local government officials were thus free from guidance or regulation. Was the negligence of China's central administration in regulating and overseeing the privatization process a purposeful arrangement for conveniently speeding up privatization at local levels? So far, no one, neither scholars in China nor observers outside, have asked this.

The official denial of privatization made it difficult for the central government to formally regulate various possible privatization approaches, making it much more likely that a nationwide, spontaneous privatization would take place. This is a rare case in the transitional societies that have implemented privatization policies. Unlike most governments, the authoritarian Chinese central administration did not want to discuss the details of its privatization policy or direct the process ahead of time, nor did it analyze and predict possible outcomes of the policy. As the Chinese government did not really know what the consequences of the "enlivening" process would be, its determination in pushing forward the policy implied that it was not much interested in how the new enterprise institutions could be built up to replace the old SOE system; instead, it was primarily concerned with protecting itself from financial losses and relieving the regime from the burdens of the SOE system. Therefore, the core issue of the "enlivening" process became how to find financial resources to arrange social security payments for SOE workers, or how to calm the workers down and keep them quiet if financial resources were not sufficient and their payments were cut.

Actually, the Chinese central government was aware of the possibilities of asset stripping by SOE managers, but did not make sufficient effort to try to stop such activities. In June 1998, an instruction from the State Commission for Economy and Trade simply mentioned that "shares of enterprises should not be concentrated into hands of a small group of people," and "no one is allowed to take the opportunity of *gaizhi* to evade debts,"[115] but no punishment measures were set forth as national policy. In August 1998, the newspaper of the Chinese Communist Party reported: some local authorities did not assess SOEs' assets values and arbitrarily cut sale prices; some took the sell-off opportunity to dodge their debts to the state banks; some even gave away SOE assets to private individuals under the smoke screen of a sell-off; in particular, some CEOs of the incorporatized SOEs did not make any payments out of their pocket for the company stocks they personally acquired, instead, they shifted the SOEs' business earnings to pay for their personal acquisitions.[116] But the central government did not respond by issuing the regulations that would have been necessary to prevent asset stripping. It was only in February of 1999 that the State Commission for Economy and Trade, the Ministry of Finance, and the People's Bank of China distributed a notice that mentioned that "selling small SOEs should not be the only approach to reform, and the abnormal behaviors should be controlled and supervised."[117] Again, no sanctions

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[115] The State Commission for Economy and Trade, "*Guanyu 1998 Nian Guoyou Qiye Gaige he Fazhan Gongzuo de Yijian* (The Instruction for SOE Reform and Development in 1998)," *Jingji Ribao* (Economic Daily), June 22, 1998.

[116] *Renmin Ribao* (People's Daily), Aug. 5, 1998; quoted from Ding Xueliang, "Who Gets What, How: When Chinese State-owned Enterprises Become Shareholding Companies," *Problems of Post-Communism*, May/June, 1999, 32-33.

[117] The State Commission for Economy and Trade, the Ministry of Finance and the Central Bank, "*Guanyu Chushou Guoyou Xiaoxing Qiye zhong Ruogan Wenti Yijian de Tongzhi* (A Notice about Several Suggestions

were declared against the "abnormal behavior," and the suggestions were seen by asset-stripping managers and officials at the local level as nothing more than whistles in the wind.

When the three-year goal of SOE reform silently opened the door for SOE privatization, China had a fragile legal environment and a central government that failed to monitor and regulate. Local government officials and SOE managers could then form alliances to manipulate the process for their own interests, with the only social force able to prevent them being the SOE workers. The World Bank once suggested: "Slower privatization is viable (although not necessarily optional) if the government, or workers themselves, are strong enough to assert control over enterprises and prevent managers from stealing assets." [118] However, the Chinese central government did just the opposite: being reluctant to set up a scheme for formal privatization, it encouraged local governments and SOE managers to rush into informal privatization, while simultaneously excluding workers from the process.

In China's process of economic reform, new policies were often implemented through political campaigns. After the central government declared the new round of the SOE reform, immediately a campaign of "enlivening" (*gaohuo*) SOEs was pushed forward all over China, and a wave of "replacing SOEs with private enterprises" was observed. Chinese cadres in local governments and SOEs were used to sensing changes in the political winds and took the lead in the campaigns, not necessarily because they fully understood the policies, but because they wanted to show their loyalty and ambition and thus gain promotion. On the other hand, not all policies were

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for Selling Small SOEs)," *Zhongguo Gaige Bao* (China Reform News), Feb. 25, 1999.

[118] The World Bank, *World Developing Report 1996: From Plan to Market*, New York, NY, Oxford University Press, 1996, 50.

smoothly carried out at lower levels; those that might damage or challenge the interests of the lower level cadres and SOE managers would encounter resistance and moved forward very slowly. When a reform campaign is warmly welcomed and quickly pushed forward by local cadres and SOE managers, one cannot simply look at what the official documents say—the key is to examine what incentivizes their behavior.

The slogan of "escaping the SOE difficulties" was the regime's plan to free itself of the burdens of SOEs. The idea was firmly supported by local governments because most small and medium size SOEs were in their hands, and supporting them had long been a headache. At the same time, SOE managers found a wealth of opportunities to gain ownership of their enterprises and get rich through asset stripping. Moreover, the new policy of "reducing redundancy to increase efficiency" actually terminated SOEs' long-term obligations to protect employees, and destroyed the dependence of SOE workers on the state, offering managers the power to lay off workers as they saw fit. Once workers became the target of privatization, rather than participants in it, managers were liberated from oversight. Under the threat of being laid off, employees were vulnerable and in no position to challenge management, particularly as the latter undertook its self-enrichment under the banner of implementing the policies of the central government. In that context, resistance from workers could have been labeled as political opposition to the decisions of the communist party.

China's privatization policy for large SOEs was different to that for small and medium size SOEs. After the privatization of small SOEs was almost completed in 2002, the central government put the privatization of large SOEs on the agenda—and things proceeded fairly quickly.

The government was keen to regulate the privatization of large SOEs because it wanted to maximize the revenue it was obtaining through the monopolization of strategic industries; maintaining partial public ownership of these large firms was also useful for keeping some of the trappings of socialism. Full privatization of large SOEs in China has rarely been approved; instead, most are transformed through ownership diversification, where the government maintains a majority share position and controlling foreign investors are excluded.

In preparing for the privatization of large SOEs, in June 2003 the government established the State Assets Supervision and Administration Commission (SASAC). Its mission was to "carry out the government's functions as investor in and owner of state assets, and thus separate these tasks from the government's role as public manager of society as a whole."[119] Then, two regulations, "The Interim Measures of Managing Enterprise Property Rights Transfer" (also called the No. 3 decree) and "The Suggestions on Regulating SOE *Gaizhi*," were drafted by SASAC.[120] The latter was issued on Nov. 30, 2003 by the Office of the State Council in its No. 96 document, and published in the media in December 2003. In it the government listed a procedure for SOE *gaizhi*: each *gaizhi* project should be discussed by the Congress of Workers and Staff and be approved by a government office, the assets of the *gaizhi* enterprise should be appraised and its debts audited.[121] So far, China's legislative body has never issued any law to regulate the activities of the nationwide

[119] Barry Naughtong, *The Chinese Economy: Transitions and Growth*, 316.

[120] "China's Website for SOE *Gaizhi*", "*Guoqi Gaizhi zhong de Yixie Changjian Wenti* (Common Issues in SOE *Gaizhi* (Aug. 20, 2004)" (http://www.gaizhi.cn/html/2005-12-29/20051229134943.htm).

[121] The State Assets Supervision and Administration Commission (SASAC), "*Guanyu Guifan Guoyou Qiye Gaizhi Gongzuo de Yijian* (The Suggestions on Regulating SOE *Gaizhi*)" Nov. 30, 2003 (http://www.sasac.gov.cn/gzjg/xcgz/200408100189.htm).

large-scale privatization process. Whether the 2003 regulations effectively restrain spontaneous and questionable activities in the privatization will be analyzed below.

Chapter 8

The Spontaneous Privatization Process in China: Interaction among Participants and their Approaches

In contrast to the process of privatization in other transition societies, China's might be the most spontaneous. When the policy "letting go of the small" was carried out, answers to two key questions, viz. where should the small SOEs go, and who should become the owners of the privatized enterprises, had never been clarified by the Chinese government. The OECD once cautiously expressed its concern: in China "some small SOEs may have been privatized informally."[1] Actually, during the privatization period that lasted for a decade, no clear-cut nationwide privatization scheme or policy was designed; local policies varied across provinces, cities, and even differed between two districts in the same city. As proper regulations for privatization were absent, asset stripping frequently occurred and caused a lot of labor protests.

China's nationwide privatization started in 1997. Accourding to Guo, Gan and Xu, by the end of 2005, 63 percent of SOEs had been privatized.[2] As of 2009, privatization of industrial enterprises was almost completed in China. So far, details of the privatization or *gaizhi* process in China are a black box. If a researcher wants to find out how many SOEs were privatized, by what means, whether they were then registered as new firms, and if so what kind, the official data is

[1] Carsten Holz, *China's Industrial State-owned Enterprises: Between Profitability and Bankruptcy*, Singapore, World Scientific Publishing Co, 2003, 267.

[2] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," *Seoul Journal of Economics*, 2008, Vol.21, No.21, 9.

not available. The Chinese government does not seem to have any systematic annual record of the progress of privatization. Neither the Chinese central administration nor any local government has ever released a report to the public about the privatization process. What was addressed in China's official documents about the *gaizhi* process appeared to be quite different from what actually took place; so context analysis of government documents often does not help understand what SOE managers actually did in privatization. Comparing the official documents with media reports about privatization, the author found a lot of controversies or problems, which provides clues for exploring the complicated operations of SOE managers during those years.

Privatization might be analyzed simply as an asset transaction, as many economists see it. But this ignores the social process in which parties interact at the workplace for different interests. Details of the social aspects of the privatization process in China, such as who was able to make decisions, how outside purchasers were motivated and selected, how insider manager and outside purchaser colluded, and the results of a privatization plan at an SOE, could provide opportunities to better understand and evaluate privatization. Given the difficulty of carrying out a survey for investigating informal or spontaneous privatization even for academic purposes, the author instead focuses on a number of case studies to illustrate the real privatization process in China as it really took place. Privatization cases were occasionally reported in the country's media. The author began to collect such cases from 1997 from a variety of Chinese and English newspapers and journals and from online reports, and kept tracing the progress in each case until no further developments were observed. When a case caused nationwide attention, there might be several reports from different media; but some cases had only one report. Only those cases with

complete information about the privatization process were analyzed. All together, materials from 130 cases are used in the following discussion. They were collected from media reports, but not through a sampling procedure. The cases took place in 30 out of China's 31 provinces and municipalities,[3] among them two were in 1994, 51 occurred from 1998 to 2003, and 77 from 2004 to 2011. In the 130 cases, some were seen as successful privatization in China without obviously questionable problems,[4] a few were seemingly plausible,[5] while the majority referred to various problems involving asset stripping. About one third of the cases involved workers' discontent or protests. Only in a few cases was the misconduct of managers corrected by government offices.

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[3] The geographic distribution of the 130 cases is hereby listed: Anhui province, 3; Beijing Municipality, 4; Chongqing Municipality, 5; Fujian province, 1; Gansu province, 1; Guangdong province, 5; Guangxi Autonomous Region, 4; Guizhou province, 1; Hainan province, 1; Hebei province, 4; Heilongjiang province, 7; Henan province, 13; Hubei province, 10; Hunan province, 7; Jiangsu province, 13; Jiangxi province, 1; Jilin province, 2; Liaoning province, 6; Neimenggu Autonomous Region, 2; Ningxia Autonomous Region, 2; Qinghai province, 1; Shaanxi province, 1; Shandong province 9; Shanghai municipality, 2; Shanxi province, 4; Sichuan province, 15; Tianjin municipality, 1; Xinjiang Autonomous Region, 1; Yunnan province, 1; Zhejiang province 3. Only in Tibetan Autonomous Region, where industries were less developed, was no privatization case found.

[4] For example, a private company, Jianlong Group, which caused the incident at the Tonghua Steel Co. where the CEO from the Group was beaten to death by angry workers, was reported to be successful in taking over the Zunhua Steel Factory and Kuancheng Iron Mine in Hebei province and the Mingcheng Steel Factory in Jilin province. See "*Jianlong Chongzu Tonggang Jituan Zai Diaocha* (The Reinvestigation of the Taking over of Tonghua Steel Co. by Jianlong Group)," Beijing, China, *Xin Jing Bao* (The New BeiJing Daily), Aug. 14, 2009.

[5] For example, in a case in November 2000 in Shenyang city of Liaoning province, the private Huacheng Inc. took over the state-owned Shenyang Jinbei Automobile Co., while the former provided 943 million yuan to two state-owned companies whose trustee was the local government office for state assets administration to purchase the shares of the automobile company, and the private Huacheng Inc. became a dominant shareholder of Shenyang Jinbei Co.; later, litigation against the CEO of Huacheng Inc. was filed, and the CEO fled China. Part of the story was discussed by reporters in 2001. See Wang Shuo, and Ren Bo, "*Huangchen Migong* (The Huacheng Perplexing Maze)," Beijing, China, *Caijing* (the Finance and Economy Magazine), No.4, 2001, 21-34.

Analyzing the practices used by SOE managers and government officials in the cases, the author categorizes the privatization approaches into two groups, i.e. insider's privatization (such as management buyout (MBO) and employee shareholding) and outsider's privatization (e.g. foreign mergers and acquisitions (M&A), domestic outsider's takeover, and having LLSCs listed on the stock market). China's privatization approaches are much more diversified and complicated than in Russia, and cover most possible methods. This chapter first discusses two general issues, who participated in privatization in China, and how SOE assets were evaluated. It then introduces each vector with case materials, illustrating how the various parties interacted in the process, and finally analyzes a unique phenomenon, the purposefully incomplete privatization in Shanghai, from which one may come understand the sorts of difficulties local governments encountered.

The author found that, although many private industrial enterprises grew up for years as the result of economic liberalization implemented before the privatization, and China has successfully absorbed huge amount of foreign direct investment (FDI), the privatization in China was still dominated by insiders. Half of the privatized industrial SOEs were taken over by SOE managers, with foreign M&A playing only a small role, and many industrial SOEs were privatized by domestic companies or individuals for non-industrial purposes. Generally speaking, the privatization of small- and medium-sized SOEs from 1997 to 2002 was indeed a spontaneous process, largely manipulated by SOE managers and government officials for their personal profit; the privatization of large SOEs from 2003 to 2009 was more closely directed by local government offices, but features of spontaneous privatization were frequently exposed. Ultimately, the

privatization in China enriched managers, but did not help much in restructuring industrial SOEs.

1. Participants in China's Privatization

Local government officials, SOE managers, and domestic or overseas investors are three key players in China's privatization process (see Table 8-1). A significant difference between the privatization in China and in Russia was that in the latter case local governments were not much directly involved in the process-an alliance of SOE managers and workers against outside investors was formed, to make the process more favorable to insiders. In China, local government officials and SOE managers, sometimes together with outside investors, formed an alliance to manipulate the process against workers' interests and demands. Ding writes, "how many SOEs can be converted into joint-stock companies, which enterprises to select for restructuring, how to organize the ownership structure of company stocks, and how to set share prices are decided by the government departments… Moreover, most of the crucial decisions are made behind closed doors."[6] Based on her fieldwork in three cities, Zeng points out that "local officials' pursuit of economic efficiency was outweighed by a mixture of their concern for personal political careers, private material gain, and social stability;" at the same time, they "were facing the time pressure to privatize a large number of local enterprises in a relatively short period of time," thus "their top priority in the privatization

[6] Ding Xueliang, "Who Gets What, How: When Chinese State-owned Enterprises Become Shareholding Companies," *Problems of Post-Communism*, May/June, 1999, 39.

process was to get the job done while maintaining social stability."[7] SOE managers, particularly those of small SOEs, played a crucial role in determining how their enterprises were privatized. With their tremendous advantages in the flawed monitoring and supervisory environment, many SOE managers executed illicit privatization operations and became the *de jure* or *de facto* majority shareholders of their companies without having to compensate the state proportionately.[8]

In China's coastal areas and some inland provinces, the privatization process sometimes had a unique participant, the overseas Chinese businessmen from Hong Kong and Taiwan, and Japanese and Korean companies as well, who knew well the Chinese officialdom culture and were sophisticated in making deals with officials and SOE managers. Huang points out that the primary benefits of China's FDI inflows had less to do with the provision of marketing access and know-how transfers, technology diffusion, or access to export channels; instead, the FDI inflows was of great benefit to China's privatization.[9] Local governments and SOE managers were both interested in seeking foreign investors, because, when foreign investors participated in the privatization of some SOEs, the enterprises could become eligible for many different kinds of preferential treatment after they were turned into Sino-foreign joint ventures.[10] However, the

[7] Zeng Jin, "Political Compromises: The Privatization of Small- and Medium-Sized Public Enterprises in China," *Journal of Chinese Political Science*, Vol.15, No.3, 2010, 280.

[8] Ding Xueliang, "Who Gets What, How: When Chinese State-owned Enterprises Become Shareholding Companies," 39.

[9] Huang Yasheng, *Selling China: Foreign Direct Investment during the Reform Era*, New York, NY, Cambridge University Press, 2003, xvi.

[10] Ding Xueliang, "Who Gets What, How: When Chinese State-owned Enterprises Become Shareholding Companies," 33-34.

foreign investors could leave many of the liabilities of the SOEs behind.[11]

The privatization of large SOEs was dominated by government offices and SOE managers. In the northern and western provinces where economic development moved forward more slowly, large SOEs often could not find investors and their privatization was thus pushed forward by governments.[12] In April 2004 China's Deputy Premier Huang Ju ordered that SOE *gaizhi* must speed up; it was reported that, without effective regulating, the *gaizhi* activities of a lot of large SOEs caused problems.[13] Following the order from the central government, local governments actively pushed forward the privatization of large SOEs. For instance, the leaders of Heilongjiang province treated SOEs like ice blocks, selling them as fast as possible; the provincial government was also counseled to "let the most beautiful daughter get married first" and "force the not-ugly daughters to get married immediately."[14] In Ha'erbin city of the province, there were still 1,500 SOEs in 2004, and the city government decided that 90 percent of the enterprises had to start *gaizhi* in 2005 and 70 percent of them must have the *gaizhi* done within the year; in the process, the city

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[11] Shahid Yusuf, Kaoru Nabeshima, and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, Washington, DC, the International Bank for Reconstruction and Development/ the World Bank, 2006, 107.

[12] "*Sheng guoyou qiye gaige zhuanti diaoyan zu* (The Research Group of SOE Reform of Heilongjiang Province)," "*Guanyu Wo Sheng Difang Guoyou Qiye Gaige de Diaoyan Baogao* (An Investigation Report about the SOE Reform in Our Province), Harbin, China, the Assets Supervision and Administration Commission of Heilongjiang Province, Sept. 4, 2007 (www.hljgzw.gov.cn/data/xwxx/news/20070904153105100); E Pan, "*Wang Min Zhizheng Jilin Wu Nian, Tuidong Guoqi Gaige, bei Chengwei Wang Dadan* (Wang Min Has Governed Jilin Province for Five Years, and is called 'Wang Brave' for His Efforts to Promote SOE Reform)," Beijing, China, *Xiaokang Zazhi* (The Better-off Magazine), No.1, 2010.

[13] Qiu Xin, "*Jiangsu Guoqi Gaige Fubai Yanzhong, Huang Ju Nan Ci Qi Ze* (The SOE Reform in Jiangsu Province Caused a Lot of Corruption, and Huang Ju is Responsible)," Hong Kong, China, *Yazhou Shibao* (Asia Times), Nov. 4, 2004.

[14] Zhao Weimin, and Long Hao, "*Xi Gang Gaizhi Mituan* (the *Gaizhi* Puzzle at the Xilin Steel Group)," Beijing, China, *Zhongguo Jingji Shibao* (China Economic Times), Feb. 22, 2010.

government chose an approach named "breaking down each factory for privatization," which meant to sell the best parts of the SOEs to domestic or foreign potential investors.[15] The governor of Jilin Province requested at the beginning of 2005 that 816 SOEs in the province be restructured within the year;[16] he told SOE managers in July 2005 that *gaizhi* must be completed within five months, and if an SOE failed to do it, its CEO would be removed.[17] Appointed by government, SOE managers had to obey the order.[18]

The role of government in privatization is an important issue. The Chinese central government did not prepare or provide a formal privatization scheme for all SOEs; instead, it only gave fuzzy rermit and an unclear direction, and allowed local governments and SOE managers to select their own approaches to privatization while the rules or procedures to regulate the process were absent. The basic position of the central government from 1997 to 2003 was not to intervene in the ongoing privatization process, and to respond only when significant corruption or labor disputes took place (often simultaneously) and were reported to the central government. In other words, during this period the central administration preferred an *ex post facto* response, rather than to setting up clear rules in advance. Therefore, local governments and SOE managers could act freely

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[15] Yang Ming, "*Waizi Qing Qu Jinghua, Zai Zao Ha Yi Gong Ji Wu Keneng* (Foreign Investors Took the Best Part of an SOE, and Ha'erbin First Machinery Tools Factory Could No Longer be Restructured)," Beijing, China, *Zhongguo Gongye Bao* (The China Industrial News), Dec. 19, 2005.

[16] Zhou Zhenhua, and Zhang Lu, "*Tong Gang Beiju* (The Tragedy at the Tonghua Steel)," Beijing, China, *Zhongguo Xinwen Zhoukan* (The China Newsweek), Aug. 5, 2009.

[17] Wang Jianjun, "*Tong Gang Beiju de Luoji* (The Logic behind the Tragedy at the Tonghua Steel)," Beijing, China, *Liaowang Xinwen Zhoukan* (The Outlook Weekly), Aug. 10, 2009.

[18] In China, such administrative orders were called "political tasks," which meant that, whether it reasonable or not, one had to follow the order and complete it immediately, even without proper preparation. See Wang Jianjun, "*Tong Gang Beiju de Luoji* (The Logic behind the Tragedy at the Tonghua Steel)."

in a space with no clear boundaries. However, after 2003, when large SOEs were privatized, the central government changed its attitude and became quite active in controlling the privatization of large SOEs. Table 8-1 shows that, in 1998, in 69 percent of the interviewed SOEs, *gaizhi* was initiated by governments; however, SOE managers became more active in the following years; a 2006 survey found that in 42 percent of the interviewed SOEs *gaizhi* was initiated by managers. From 1998 to 2006 employees and other parties only played a small role; and the role of the central government in the survey in 2006 was negligible.[19]

Table 8-1 Who Initiated *Gaizhi*?

The Party Initiating *Gaizhi*	1998 (%)	2004 (%)	2006 (%)
Governments	69	68	58
Firm management	24	12	42
Employees	2	12	0
Other	5	8	…
Total	100	100	100

Source: The 1998 survey data was cited from Ross Garnaut, Song Ligang, Stoyan Tenev, and Yao Yang, *China's Ownership Transformation: Process, Outcomes, Prospects* (Washington, DC, the International Finance Corporation and the International Bank for Reconstruction and Development/ The World Bank, 2005), 38. The survey was carried out by China's State Bureau of Statistics in 57,881 enterprises. The 2005 survey data was cited from Liu Xiaoxuan, and Liu Shaojia, "*Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (The Investigation and Research Report on SOE Gaizhi and Restructuring)," May 2005 (www.sachina.edu.cn/download.php?optype=channel&channelid). Its sample size was 2,696, of them 60 percent were large- and medium-sized enterprises, and 40 percent were small. About 23 percent of the interviewed former SOEs refused to fill and submit questionnaire—most of those were fully privatized SOEs. The 2006 survey data was cited from Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China" (Seoul, South Korea, *Seoul Journal of Economics*, Vol.21, No.2, 2008), 319. Its sample size was 898.

[19] Ibid.

In China, quite often, privatization of an SOE was simply a game behind closed doors among local officials, SOE managers, and outside investors who had good personal relations with them. Information on each *gaizhi* plan was often not available to all potential investors, and privatization operations and transactions of SOE assets were not transparent to the public. According to Liu and Liu, more than half of *gaizhi* plans were not open to the public for attracting all potential investors (see Table 8-2). In other words, in the privatization process many officials and SOE managers did not really care if they could find the best investors to privatize their SOEs; they preferred a closed operation that they could manipulate. Obviously, such operations provided the managers with more opportunities for asset stripping, and the officials more chances for rent seeking. The reason a lot of government officials supported the spontaneous privatization was that they could personally benefit from it.

Table 8-2 Method of Releasing Informaiton of *Gaizhi* Project

Method	%
Circulated in enterprise only	58
Published in media	20
Press conference for potential investors	6
Posted on the internet	2
Released in asset transaction offices	14
Total	100

Source: Liu Xiaoxuan, and Liu Shaojia, "*Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (The Investigation and Research Report on SOE Gaizhi and Restructuring)," May 2005.

It has to be pointed out that since 2003 China's central government has issued regulations and suggestions for the privatization of large SOEs, but the regulations were often ignored by local governments and SOE managers. Case materials that many of the practices of managers and local governments after 2003 obviously violated the regulations of the central government but were not halted, and responsible local officials and SOE managers were not punished. A lot of local governments even firmly stood at the side of SOE managers and outside investors against workers. For example, the major of Yangzhou city in Jiangsu Province declared in June 2003 that, in order to implement *gaizhi*, government offices in the city were not allowed to accept or hear any appeals or complaints regarding privatization, and private law firms were prohibited from taking any case about labor disputes in privatization, or their attorney and firm licenses would be suspended.[20]

2. How was SOE Privatization Prepared? Devaluating Assets for a Cheap Sell

Asset valuation is the first step in SOE privatization. "When carrying out *gaizhi*, firms must go through the procedures of asset valuation, the demarcation of ownership rights and the verification of assets…Valuation has to be perceived as fair if it is to be accepted by all the parties concerned."[21] However, in China there was no formal supervision of the valuation process. "The accounting firms are usually selected by the *gaizhi* firms themselves, and may be influenced by both

[20] Wang Hui, "*Gaizhi yu Zhongguo Gongren Jieji de Lishi Mingyun: Jiangsu Tongyu Jituan Gaizhi Diaocha* (*Gaizhi* and the Historical Fate of the Chinese Working Class: An Investigation of the *Gaizhi at the Tongyu Group in Jiangsu Province*)," Haikou, China, *Tianya* (The Remotest Corner), No.1, 2006.

[21] Ross Garnaut, et al. *China's Ownership Transformation: Process, Outcomes, Prospects*, 67-68.

the *gaizhi* firms and local government to give favorable evaluations… [T]he accounting firms often had little to no experience with standard methods for valuing business assets;"[22] and a proportion of the accounting firms do not act professionally and often provide favorable asset appraisal for local governments and *gaizhi* firms.[23] Thus, it was a common practice that local government officials and SOE managers manipulated the SOE asset evaluation for their personal interests: "discounts are often given by local governments to compensate the buyer for assuming more social obligations or to speed up the *gaizhi* process."[24]

Among the 130 cases this author collected, 26 cases involved inappropriate asset valuation, occurring both in the coastal and inland provinces,[25] which suggested that in the more developed coastal provinces privatization practices were not necessarily better regulated by local governments. In the 26 cases the author found that, in order to sell SOEs for a cheap price to managers or outside investors, managers of twelve SOEs purposely instructed accounting firms to underestimate the assets of their enterprises; in fourteen cases local governments decided to undervalue SOE assets by deducting a large amount from book value so SOE managers could buy the enterprises with a big discount. Garnaut et al. found from their eleven-city survey in 2001 that 38 percent of valuers

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[22] Susan Lu, and David Dranore, "Profiting from *Gaizhi*: Management Buyouts during China's Privatization," *Working Paper Series*, December 22, 2007 (http://ssrn.com/abstract=1348277).

[23] Ross Garnaut, et al. *China's Ownership Transformation: Process, Outcomes, Prospects*, 68.

[24] Ibid.

[25] In coastal areas, one case was found in Guangdong Province, one in Guangxi Autonomous Region, three cases were found in Jiangsu Province, two were in Zhejiang Province, two in Shandong Province and one in Beijing municipality; in inland provinces, four cases were found in Hubei Province, two in Sichuan Province, one in Chongqing municipality, three in Shanxi Province, two in Henan Province, two in Jilin Province, one in Hunan Province, one in Heilongjiang Province. Other case materials that mentioned it did not provide details or focus on the problem.

were chosen by *gaizhi* firms, 33 percent by local governments, and the remaining 29 percent jointly by local governments and firms; it was common for buyers to receive state assets at a discounted price, but most surveyed firms did not want to report whether they had received a discount in *gaizhi*, and, among the firms which reported discounts given by local governments, the discount rate ranged from very low to 37 percent in different cities.[26]

When SOE managers directly manipulated the asset appraisal of their enterprises, they often acted unscrupulously, because rarely did local governments intervene. Workers cccasionally exposed these activities to the media, and the reporters from Beijing did investigations. That is how many of the details of such cases were revealed. For example, the Jialing Chemical Plant in Chongqing Municipality was praised in 1997 as the first full employee shareholding company among the large- and medium sized SOEs in China. Before the enterprise was privatized, the CEO and his wife registered private companies and had the SOE entered into contracts with them for the purchase of raw materials and sale of products. When the SOE bought raw materials from its CEO's private companies at high prices, and sold products to them at low prices, SOE profits were siphoned off by the private companies, and huge debts were accumulating at the SOE. The practice went for years. Under the instructions of the CEO, an accounting firm helped the CEO under-evaluate the net assets of the SOE by appraising its debts as high as 136 million yuan, 91 percent of its total assets. The appraisal made it possible for the CEO to arrange a full EMBO (employee and management buyout)[27] in June 1997. In the EMBO all employees of the

[26] Ross Garnaut, et al. *China's Ownership Transformation: Process, Outcomes, Prospects*, 72-75..

[27] In the last years of the 1990s in China, when employee buyout (EBO) was arranged, managers were also

SOE invested 3.6 million, of which the CEO and his wife put in 950 thousand (27 percent of the total employees' investment) but obtained 35 percent of the shares. In 1998, this EMBO *gaizhi* was promoted in China as a model to be replicated nationwide; but in 2004 when workers of the company organized protests against the corrupt CEO, the dark side of the privatization story was exposed in the media and the CEO was investigated (though he was soon released, whereas the worker protesters were arrested).[28]

Similarly, in January 1998, the managers of Changchun Semiconductor Factory in Jilin Province took the company private at a price of 60 million yuan; seven years later, the manager was detained for corruption, and an investigation found that the factory's assets were undervalued with tacit approval by a local government official. The net value of the enterprise in 1998 was actually 420 million yuan.[29] In Zhejiang province, the Haizheng Pharmaceutical Group reported at the end of 2003 that its net assets were 675 million yuan; but, seven months later when the SOE was privatized by insiders, its net assets through appraisal suddenly shrank to 119 million. When a reporter tried to investigate the valuation process and asked a manager of the company several times what accounting firm did the asset valuation, the manager refused to reveal the

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perceived as employees, because, according to the official ideology, both managers and workers were state employees and the masters of the enterprise.

[28] Fang Xiangming, Zhang Jie, and Yao Yujun, "*Chongqing Jialing Huagongchang Chumai Shilu* (How was the Chongqing Jialing Chemical Plant Sold)," Wuhan, China, *Juece yu Xinxi* (Decision Making and Information), No.4, 1998, 13-14; Yuan Ling, and Wang Rong, "*Shoujia Gaizhi Guoqi Guquan Biangeng Heidong* (The First *Gaizhi* SOE: The Loophole in Its Ownership Change)," *Xin Jing Bao* (The New Beijing Daily), May 24, 2004.

[29] Wang Lei, "*Changchun Bandaoti 4.2 Yi Guozi Liushi, Muhou Heishou Xiekuan Zhengfa* (The State Assets in 420 Million of Changchun Semiconductor Factory was Gone, and the Black Hand behind Disappeared)," Beijing, China, *Caijing Shibao* (the Finance and Economy Times), Nov. 20, 2004.

name.[30] In the Guangxi Autonomous Region, the Guilin Ferroalloy Works was privatized in the spring of 2002. At the end of 2001, the appraised assets of the factory were 230 million; but in April 2002 the result of the asset valuation by an accounting firm for privatization was only 120 million. When reporters of China's official Central TV Station (CCTV) investigated the case, they found that the undervalued assets were not approved by the local government; still, the managers of the factory bought the enterprise at the unapproved price.[31] Similar practices were also found at the Chengdu Printing Factory of Sichuan Province in 2000,[32] the Yunyang Crank Axel Factory of Hubei Province in 2002,[33] the Taicang Winery Factory of Jiangsu Province in 2003,[34] the Xinlian Electric Equipment Company of Jiangsu Province in 2003,[35] the Beijing Heliotechnics in Beijing municipality in 2004,[36] the Tiangong Special Engineering Co. of Hubei Province in 2004,[37] the

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[30] Zou Guangxiang, "*Haizheng Yaoye de MBO Lujing* (The MBO Path at the Haizheng Pharmaceutical Group)," Beijing, China, *Jingji Guancha Bao* (Economic Observation News), Aug. 29, 2004.

[31] Fa Zhan, and Ning Ke, "*Ji Ge Yi Zichan bei Jianmai, Guangxi yi Daxing Guoqi Suoshui Neimu bei Jie* (Assets in 230 Million were Cheaply Sold at a Price of 33.5 Million, the Inside Story at a Large SOE in Guangxi was Revealed)," Beijing, China, *Zhong Xin Wang* (The China Newsnet), Oct. 27, 2003 (news.xinhuanet.com/newscenter/2003-10/27).

[32] "*Chengdu Guan Qi Goujie, Mei Yin Chang 2,800 Wan Guozi bei Tan Zhan* (28 Million Assets of Chengdu Printing Factory were Grabbed)," New York, NY, *Dajiyuan Shibao* (Epoch Times), Oct. 26, 2005.

[33] Yang Min, "*Xianluo zai Xin Jiu Chanye Buju Zhijian* (Fell into the Trap of the Disappearing Industries)," Guangzhou, China, *Nanfeng Chuang* (The Window for the Wind from South), May 16, 2006, 32.

[34] Fan Lixiang, "*Laopai Guoqi bei 'Taokong,' Taicang Yi Yuan Guozi Mimi Zhengfa* (A Hundred Million of State Assets Secretly Disappeared from Taicang Winery Factory)," Beijing, China, *Zhongguo Jingying Bao* (China Management News), Aug. 18, 2003.

[35] Shao Hao, "*Xinlian Dianzi IPO Cunyi, Quxian Huoqu Guoyou Zichan* (The IPO of Xinlian Electric was Questionable, as Managers Acquired SOE Assets)," Jinan, China, *Jingji Daobao* (Economic Guidance), Dec.17, 2010.

[36] The Workers and Staff of the Beijing Heliotechnics, "*Yi Qi You Guoqi Gaizhi Yinfa de Xuanan* (A Pendant Case of SOE *Gaizhi*)," Beijing, China, *Dajun Guancha* (Dajun Observation), Aug. 4, 2006 (http://www.dajunzk.com/guoqianli.htm).

[37] Dai Jingsong, and Wei Mengjina, "*Wuhan Tiangong 'Ziben Yunzuo': Ji Duo Anliu Juan Kong Guoyou Qiye*

Ha'erbin First Tool Factory in Heilongjiang Province in 2005,[38] and the Kaiyuan Engineering of Henan Province in 2006,[39] to name just some instances about which reports were readily available.

A lot of local governments actively participated in SOE privatization decisions, by undervaluing SOE assets, to satisfy purchasers like private businessmen, SOE managers, and sometimes employees. For instance, at the Jialing Chemical Plant in Chongqing Municipality, when the CEO of the factory applied to the local government for privatization of the enterprise that had 150 million assets, the 688 employees of the factory could only invest 450 thousand for an employee buyout. In order to implement the privatization project, officials of the local government deducted 136 million in debts (a quite large portion of the debts was questionable, as explained above), seven million in intangible assets, 750 thousand as employee settlement allowance, and took 2.3 million off as a discount for cash investment; after the deductions the purchase price matched the amount of the employees said they could afford to invest.[40]

(The Capital Operation of Wuhan Tiangong: SOE was Emptied," Beijing, China, *Jingji Cankao Bao* (Economic Information Daily), Aug. 1, 2007.

[38] Yang Ming, "*Waizi Qing Qu Jinghua, Zai Zao Ha Yi Gong Ji Wu Keneng* (Foreign Investors Took the Best Part of an SOE, and Ha'erbin First Machinery Tools Factory Could No Longer be Restructured)," Beijing, China, *Zhongguo Gongye Bao* (The China Industrial News), Dec. 19, 2005.

[39] "*Kongshou Gou de Qianwan Zichan, Yige Pochan Guoqi Laozong de Shangye Yunzuo* (Bought Millions SOE Assets but Paid Nothing: The Business Operation of the CEO of a Bankrupted SOE)," Beijing, China, *Zhongguo Qingnian Bao* (The Chinese Youth Daily), Jan. 17, 2007.

[40] Fang Xiangming, Zhang Jie, and Yao Yujun, "*Chongqing Jialing Huagongchang Chumai Shilu* (How was the Jialing Chemical Plant in Chongqing Sold)," *Juece yu Xinxi* (Decision Making and Information), No.4, 1998, 13-14; Yuan Ling, and Wang Rong, "*Shoujia Gaizhi Guoqi Guquan Biangeng Heidong* (The First *Gaizhi* SOE: The Loophole in Its Ownership Change."

In another case, from 1997 to 1998 the Lin'an city government of Zhejiang Province wanted the state owned Lin'an Silk Spinning Factory to be taken over by a small private company; in order to satisfy the purchaser, the local government ordered Lin'an Accounting firm to undervalua the assets of the factory by revising the appraisal result of the SOE assets; the report was obediently amended twice during the year, and the total value of the assets changed from sixteen million yuan to five million, then to a negative value.[41] In Yuncheng city of Shanxi Province, two officials from the city government undervalued the assets of the Yuncheng Coking Gas Factory, and manipulated the auction of the factory in 2003; after helping a private company buy it for 64 million, the two officials took their one million yuan fee from the new owner. Two reporters investigated the matter and wrote an internal report to the top leaders of the central government. Instructed by the central government, the local government finally arrested the two officials, and the SOE was once again put to auction. In the second auction, the factory was sold for 230 million.[42] Also in Shanxi Province, the Qinshui County government officials, including the secretary of the communist party of the county and the head of a township, valued 520 million yuan in assets from several state-owned coal mines at only 127 million—for sale to a

[41] "*Zhejiang Linan Sichou Zongchang Gaizhi Neimu Diaocha* (An Inside Story of the *Gaizhi* at Lin'an Silk Spinning Factory of Zhejiang province)," Sept. 28, 2007 (http://blog.sina.com.cn/s/blog_50dd45af01008jo0.html).

[42] "*Yuncheng Shi Liang Guoyou Qiye Gaizhi Tai Lipu, 2.3 Yi Yuan Guozi 6,410 Wan Yuan Jiu Mai le* (The *Gaizhi* of Two SOEs in Yuncheng City was Too Strange: 230 Million of State Assets were Sold for 64 Millions)," Beijing, *Guangming Ribao (Guangming Daily)*, Feb. 24, 2004; "*1.6 Yi Guozi Xian Xie Liushi, Yuncheng Liang Ming Guanyuan Luoma* (160 Million State Assets were Almost Peculated, and Two Officials in Yuncheng City Stepped Down)," Taiyuan, China, *Shanxi Wanbao* (Shanxi Evening News), July 26, 2004.

private businessman.[43] The case was reported by China's official Xinhua News Agency in an internal report, and in 2003 Premier Wen Jiabao instructed that the case be investigated and the corrupt officials punished.[44] However, byl the end of 2009, nothing had been done in Shanxi Province against the corrupt officials.[45]

In 2004, when the Changge Power Plant in Henan province was privatized into the hands of the management team of the factory, the net assets of the plant, roughly 32 million yuan, were appraised at fifteen million because the local Xuchang city government gave the buyers a discount of fifteen million (ten million as a reward to the managers who decided to buy the factory, and five million as a discount for cash purchase).[46] In Shandong Province, the *gaizhi* of the Zhangyu Wine Group was directly operated by the Yantai city government in 2004; the board of directors of the company never held a meeting to discuss it. The city government decided that 45 percent of the assets of the SOE—503 million yuan— would be sold to a trust company

[43] "*Shanxi Qinshui 39 Ming Dangyuan Shangshu Jie 800 Yi Guozi Liushi* (39 Communist Party Members Appealed for the Disappearance of 80 Billion State Assets)," Beijing, China, *Huanjing yu Shenghuo* (Environment and Life), No.7, Dec. 4, 2009.

[44] "*Wang Tie Pu Shanxi Qinshui Shubai Yi Guoyou Zichan Liushi* (The Case about the Embezzled Billions of SOE Assets was Exposed)," Shijiazhuang, China, *Yanzhao Dushi Wang* (Yanzhao Metropolitan Newsnet), Sept. 7, 2009 (news.yzdsb.com.cn/system/2009/07/23/010039018).

[45] Li Bao, "*Zhongguo Jizhe Cu Zhongyang Diaocha Qian Yi Guoyou Zichan Bei Qintun* (Chinese Journalists Asked the Chinese Central Government to Investigate the Case of Embezzling Billions of SOE Assets)," Washington, DC, *Voice of America*, Sept. 7, 2009.

[46] Wang Jinfu, and Cheng Honggen, "*Henan Yi Dianchang Gaizhi Anxiang Caozuo: 1,500 Wan Mai Xia 1.2 Yi Qiye* (The *Gaizhi* of a Power Plant in Henan Province was Operated in Black Box: An SOE with 120 Million Assets was Sold at 15 Million)," *Xinhua News Net*, July 4, 2004 (http://unn.people.com.cn/GB/14748/2616584.html). This case was also mentioned by Garnaut, et al. in their book *China's Ownership Transformation: Process, Outcomes, Prospects*, 78.

owned by managers at the discounted price of 388 million yuan.[47] In 2005 when the Changzhi Steel Group in Shanxi Province was privatized, the Changzhi city government approved that 500 million of the 1.3 billion assets of the company be recorded as debt to the government, so the assets for the privatization deal were reduced to 780 million to meet the offered price of the purchaser.[48] Such manipulations were also found in the privatization process of the Guoxing Electronics of Guangdong Province in 2002,[49] the Yichang Water Company of Hubei Province in 2002,[50] and in that of the Zhongshan Group in Jiangsu Province in 2002,[51] the Hejiang Electric Co. in Luzhou city of Sichuan Province in 2003,[52] the Liangshan Paint Factory in Liangshan County of Shandong Province in 2004,[53] the Banxi Antimony Ore Mine in Taojiang County of Hunan

[47] He Yuxin, "*Shui Kongzhi le Zhangyu Gaizhi?* (Who Controlled the *Gaizhi* of the Zhangyu Wine Group)," *Caijing* (the Finance and Economy Magazine), No.6, Mar. 21, 2005, 77-78.

[48] "*Chang Gang Gaizhi* (The *Gaizhi* of Changzhi Steel Factory)," Beijing, China, *ZhengQuan Shichang Zhoukan* (The Stock Market Weekly), No.23, June 24, 2006.

[49] Tiantai Research, "*Guan Kui Guoxing Guangdian: MBO Qi Neng Bawang Yinshanggong?*（Exploring the Guoxing Electronics: How Could MBO be Done Like this?)" May 26, 2010 (http://finance.qq.com/a/20100526/005098.htm).

[50] Workers of Yichang Water Company, "*Guan Shang Goujie, Zhengfu bei Diya, Shu Shi Yi Guoyou Zichan bei Tun Shi, Chuang Xia Gujin Qiguan* (Officials Cooperated with Businessmen, Billions of State Assets were Engulfed)," June 16, 2004 (bbs.shuigongye.com/showtopic-38494).

[51] Yang Guang, "*Nanjing Zhongshan Jituan Gaizhi bei Zhi Ju'e Guoyou Zichan Liushi, Shu Yi Guoyou Zichan Bian Wei 4% Guquan* (The *Gaizhi* of Zhongshan Group in Nanjing City was Accused, as Millions of SOE Assets Shrank to Four Percent)," Changsha, China, *Xin Xiang Bao* (The New Xiang News), Mar. 5, 2009.

[52] "*Hejiang Dianli San Yi Duo Guoyou Zichan Jian Mai Jin Si Qian Wan, Fufu Lianshou, Zaojiu Xianwei Shuji Yi Wan Shenjia* (Hejiang Electric with More than 300 Million Assets was Sold Cheaply at 40 Million, and the Couple of the Party Secretary of the County Got Enriched)," Apr. 9, 2011, *Zhongguo Xiangcun Dushi Wang* (China's Newsnet for Villages and Metropolitan Areas) (www.21vip.com.cn/html/news/zggc/2011-04-09/58690).

[53] Wang Hai, "*Guoqi Baoli Gaizhi: Zichan Liu Geren, 'Heidong' gei Guojia* (The *Gaizhi* in Violence at an SOE and Asset Stripping)," Beijing, China, *Shichang Bao* (The Market News), Jan. 6, 2004.

Province in 2005,[54] and that of the Tonghua Steel Factory of Jilin Province in 2005.[55]

The author even found a case in which the Zaoyang branch of the state-owned Construction Bank cooperated with the local administration and court, and took the opportunity of the debt-equity swap plan mentioned in last chapter to undervalue the assets of 29 SOEs; then sell the non-performing loans of the enterprises to an asset management company (AMC). By releasing SOEs from debt, branch officials received 7 million yuan from the SOEs, of which 5 million was embezzled. The operations took place in Zaoyang city of Hubei Province in 2000. This particular branch made a series of fictitious bankruptcy documents for the SOEs, while the local court provided false orders executing bankruptcy proceedings, and local the government issued official documents to approve the fictitious bankruptcies. In 2004, when the office of the State Audit Bureau discovered the problem, some locally reported "bankrupted" SOEs were still operating normally.[56]

Ultimately, after the privatization of small and medium size SOEs was almost done, Li Yizhong, the Deputy Director of the newly established State Assets Supervision and Administration Commission (SASAC), expressed in 2003 with "a heavy heart": "In some places SOEs were cheaply valuated and sold off. The phenomenon appeared to be popular, with insiders

[54] Feng Zhiwei, Deng Yibo, and Tang Mingbo, "A Large Antimony Ore Mine in Yiyang was Cheaply Sold by Local Government, 2.7 Billion Assets Sold at 50 Million," *Shichang Bao* (The Market News), Dec. 17, 2007.
[55] Zhou Zhenhua, and Zhang Lu, "*Tong Gang Beiju* (The Tragedy at Tonghua Steel)," Beijing, China, *Zhongguo Xinwen Zhoukan* (The China Newsweek), Aug. 5, 2009.
[56] "*San Qian Duo Wan Yuan Guoyou Zichan Cai Mai le 60 Wan Yuan* (30 Million in State Assets Sold for 600 Thousand)," Beijing, China, *Jingji Cankao Bao* (Economic Information Daily), Oct. 16, 2006.

in collusion with outsiders to make the deals and cause losses of state assets."[57]

3. Insider Privatization in China

3.1 Management Buyout (MBO)

A management buyout (MBO) is a practice that emerged in the West from the 1970s, allowing managers of a company to purchase controlling shares of the company from existing shareholders. In most cases, MBOs occur when managers convince private investors that a firm is undervalued and the managers can unlock value if given control. The term management buyout was introduced into China in the late 1990s, and since then the term has been used to define various forms of managers' privatizations. In the West, an MBO refers to transactions between managers and private investors in a company. But in most MBOs in China, managers used the approach to privatize SOEs into their own hands, through obtaining certain shares not from outside shareholders, nor directly from the principal of the state assets (in most situation, the local government), but from the agents in charge of SOE assets management, viz. the SOE managers themselves. Often, local governments tacitly approved such insider transactions. The key difference between the operations as practiced in the West and China is that in the former the buyers in MBOs

[57] Xie Heng, "*Shi Wan Yi Guoyou Zichan Chongzu de Caifu Jihui* (The Opportunities in Reorganizing 10 Trillion State Assets)," Beijing, China, *San Lian Shenghuo Zhoukan* (The Life Weekly), No.50, Dec. 15, 2003, 31.

are not sellers, but in China, very often, the buyers and sellers of MBOs are actually the same person: SOE managers. In such circumstances moral hazard obviously becomes a big problem.

MBO practices in China can be divided into two stages: the period before and after March 2003. From 1997 to early 2003, when the privatization of small SOEs was not yet completed, the central government did not have any policy or law to regulate MBOs,[58] and local governments provided ad hoc MBO policies. For instance, in the Shanghai municipality the government of Huangpu District decided in 1999 that the percentage of managers' shares in MBO or EMBO (employee-management buyout) would be determined by the government based on the financial situation of each SOE: when SOEs were financially healthy, manager's shares should not exceed three to ten times of the average shares held by employees; when SOEs were in bad shape managers could hold no more than 49 percent of the shares of their enterprises and might borrow bank loans to buy the shares.[59] In the same city, the policy was different under the Minhang District government: managers were encouraged to hold at least 20 percent of the shares of their enterprises, and in 2002 the managers of twelve larger enterprises held on average 46 percent of the shares of their enterprises, while the highest percentage was 65 percent.[60]

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[58] Wang Zihui, "*MBO de Zuida Yinhuan: Wufa Huibi de Guoyou Zichan Liushi Wenti* (The Largest Hidden Problem in MBO: The Losses of State Assets that Can not be Evaded)," Beijing, China, *Zhongguo Jingji Shibao* (China Economic Times), June 25, 2003.

[59] The Office of Economic Reform in Huangpu District Government, "*Huangpu Qu Qiye Gaige de Tujing* (The Paths of Enterprise Reform in Huangpu District)," Shanghai, China, *Shanghai Gaige* (Reform in Shanghai), No.10, 1999, 37.

[60] The Office of Economic Reform in Minghang District Government of Shanghai Municopality, "*Shanghai Shi Minhang Qu Gongyou Qiye Chanquan Zhidu Gaige Qude Zhongda Tupo* (The Reform of Public Properties in Enterprises in Minhang District of Shanghai Municipality Has Made Great Progresses)," *Shanghai Gaige* (Reform in Shanghai), No.8, 2002, 9.

MBOs were not carried out simply as an approach to *gaizhi* in SOEs; it was also adopted by some CEOs of the listed state-shareholding companies. At the end of 2002, among 1,224 listed LLSCs,[61] about one hundred companies had already tried an MBO, but only nine provided the information about the transaction in their annual reports.[62] Actually, from 1997 to 2003, not only did MBO policies vary across the country, but local government supervision over MBO practices also differed among cities and provinces. For example, the supervision in Shanghai municipality was much more rigorous than in many provinces. When the supervision was absent or insufficient, SOE managers could manipulate the privatization and engage in unchecked asset stripping.

In the second period, from 2003 to 2005 the Chinese central government moved back and forth with hesitation, before finally reopening the door for MBOs. In March 2003, China's Ministry of Finance proposed a pause in MBO practices.[63] This suggestion was not a formal order but it cooled down the MBO heat temporarily.[64] In November 2003, the central government issued a document titled "The Opinions to Regulate *Gaizhi* in SOEs," and recognized MBO as an acceptable method for *gaizhi*, but emphasized that SOE managers were not allowed to borrow funds from their enterprises or borrow loans from banks by using their enterprises as guaranty. On Feb. 1, 2004, in a document titled as "The Temporary Regulation

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[61] Lin Jian, "*2002 Nian Shangshi Gongsi A Gu Shoufa Chouzi 462.16 Yi Yuan* (The Listed Companies Collected 46 Billion through IPO of A Share in 2002)," Beijing, China, *Renmin Ribao Haiwai Ban* (People's Daily, Overseas Version), Jan. 25, 2003, 5.

[62] Li Hongbing, "*Caizhengbu Jianyi Zanting MBO* (The Ministry of Finance Proposed Temporary Stop of MBO)," Guangzhou, China, *Ershiyi Shiji Jingji Baodao* (Economic Report for the 21st Century), Mar. 26, 2003.

[63] Ibid.

[64] Liu Meng, "*MBO Chuang Fu: Neiburen Caokong de Youxi* (Enriching through MBO: The Game Played by Insiders," Beijing, China, *Xin Caifu Zazhi* (The New Wealth Magazine), No.9, 2004.

about Transaction of SOE Assets," the central government requested that such transactions should use a lump-sum payment.[65]

In the second period, from 2003 to 2005 the Chinese central government moved back and forth with hesitation; then finally reopened the door for MBO. In March 2003, China's Ministry of Finance proposed a pause of MBO practices.[66] This suggestion was not a formal order but it cooled down the MBO heat in China's privatization.[67] In November 2003, the central government issued a document entitled "The Opinions to Regulate *Gaizhi* in SOEs," and recognized MBO as an acceptable method for *gaizhi*, but emphasized that SOE managers were not allowed to borrow funds from their enterprises or obtain loans from banks by using their enterprises as guarantee to carry out MBO. On February 1, 2004, in a document entitled "The Temporary Regulation about Transactions in SOE Assets," the central government requested that such transactions should use a lump-sum payment.[68] However, in many cities the regulations were ignored by local governments and SOE managers.

From 2004 to 2005, in order to prevent SOE managers from privatizing a huge amount of large SOEs' assets into their hands,[69] the SASAC did some investigations of MBO cases,[70] and

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[65] Yu Zhuhan, "*Wo Guo Guoyou Qiye MBO Wenti Yanjiu* (Research about MBO in China's SOEs)," Master's thesis, School of Management, Harbin Engineering University, Harbin, China, Mar. 2006, 33-36 (http://cdmd.cnki.com.cn/Article/CDMD-10217-2006132797.htm).

[66] Ibid.

[67] Liu Meng, "*MBO Chuang Fu: Neiburen Caokong de Youxi* (Enriching through MBO: The Game Played by Insiders," Beijing, China, *Xin Caifu Zazhi* (The New Wealth Magazine), No.9, 2004.

[68] Yu Zhuhan, "*Wo Guo Guoyou Qiye MBO Wenti Yanjiu* (Research about MBO in China's SOEs)."

[69] Wang Xiaojie, "*Cong Jiuming Daocao dao Zhongshizhidi de MBO Zouxiang Hefang* (Where is MBO Moving: From a Key Method of *Gaizhi* to the Target of Criticism)," Beijing, China, *Zhongguo Gongye Bao* (China Industrial News), Dec. 23, 2004.

several CEOs of the privatized large companies, who once awarded by governments as stars of privatization, were put in jail for stripping state assets.[71] Research from SASAC in August 2004 found a lot of problems in SOE *gaizhi* and transactions in SOE assets: SOE managers purposely increased the costs and debts of their enterprises, thus reducing profits before the deals, and SOE managers buying stakes in their enterprises then instructing accounting firms to undervalue enterprise assets.[72] Nevertheless, MBOs were not really stopped in China in 2004 and 2005. The SASAC simply became more cautious, but still approved several MBO cases for large SOEs from July to August 2004.[73] China's state-owned banks were very interested in making money through MBO deals, as they received commissions for brokering them. Banks even designed a number of new financial instruments to make it easier for SOE managers to carry out MBOs.[74]

On April 14, 2005, the SASAC and the Ministry of Finance jointly issued a regulation titled as "The Temporary Regulation of Transfer of SOE Assets to Managers." According to the policy, MBOs of listed LLSCs was prohibited, and managers of large SOEs were not allowed to use trust companies to carry out MBOs; nevertheless, the regulation left a lot of loopholes and

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[70] Zhao Gang, "*Guoziwei Che Cha Guoyou Zichan Liushi, MBO bei Lieru Jiancha Zhongdian* (the State Assets Supervision and Administration Commission (SASAC) Investigating Stripping of SOE Assets, Focusing on MBO," Beijing, China, *Zhongguo Jingying Bao* (China Management News), Sept. 24, 2004.

[71] Yuan Weidong, "*Da Zhengdang: Mingxing de Luoma yu Chuju* (The Big Shock: Stars Falling Down and Out)," Guangzhou, China, *Nan Feng Chuang* (The Window for the Wind from South), Feb.1, 2005, 18-21.

[72] "*Guoziwei Yu Zao 'Wanmei' MBO* (The SASAC would Like to Have a 'Perfect' MBO)," Beijing, China, *Zhongguo Jingji Zhoukan* (The China Economic Weekly), No.16, Apr. 20, 2005.

[73] Liu Meng, "*MBO Chuang Fu: Neiburen Caokong de Youxi* (Enriching through MBO: The Game Played by Insiders."

[74] Wang Zihui, "*MBO de Zuida Yinhuan: Wufa Huibi de Guoyou Zichan Liushi Wenti* (The Largest Hidden Problem in MBO: The Losses of State Assets that Can not be Evaded," Beijing, China, *Zhongguo Jingji Shibao* (China Economic Times), June 25, 2003.

unresolved issues.[75] Despite this effort, restrictions were relaxed in December 2005, when SASAC issued another document in which SOE managers were allowed to hold shares of their enterprises through investment, but were banned from being involved in major proceedings like drafting *gaizhi* plans and fixing prices of SOE assets.[76]

MBOs in China were one of several channels for asset stripping; a lot of managers manipulated the operation of SOEs, taking them from profit making to loss making, in order to put pressure on local governments to agree to the sell-offs; the managers would then arrange the purchase of the assets.[77] Local governments were very active in promoting MBOs,[78] and some bought into the idea that the best path of SOE reform was to let managers take dominant shares in their enterprises.[79]

In most cases, an MBO would need significant amount of capital. Though the author did find one case where managers of a medium-sized SOE spent only 1,200 USD, a nominal price,

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[75] "*Toushi MBO: Guoziwei Jiang Jiakuai Tuidong Guoyou Chanquan Youxu Liudong* (Focusing on MBO: The SASAC will Regulate the Transactions in SOE Assets," Beijing, China, *Xinlang Wang* (Sinanewsnet), Apr. 20, 2005 (http://news.sina.com.cn/o/2005-04-20/16245704162s.shtml); Yu Zhuhan, "*Wo Guo Guoyou Qiye MBO Wenti Yanjiu* (Research about MBO in China's SOEs)," 35, 36-38.

[76] Ge Qing, "*Guoziwei Chu XinGui: Guoyou Daxing Qiye Guanliceng Chigu Jiejing* (Restrictions to Managers' Shareholding in Large SOEs Removed)," Guangzhou, China, *Nanfang Zhoumo* (The Southern Weekend)," Jan. 19, 2006; Xinhua News Agency, "Management Buyout (MBO) Permitted in Major China SOEs," Beijing, China, *People's Daily (English Wensite)*, Jan. 23, 2006.

[77] Liu Meng, "*MBO Chuang Fu: Neiburen Caokong de Youxi* (Enriching through MBO: The Game Played by Insiders)."

[78] Xie Heng, "*Shi Wan Yi Guoyou Zichan Chongzu de Caifu Jihui* (The Opportunities in Reorganizing 10 Trillion State Assets)," 31.

[79] Reporter of Xinhua News Agency, "'*Xin Baiwan Fuweng' Zhengdang Dajiang Nanbei* (The 'New Millionaires' Have Shocked China)," Hangzhou, China, *Zhejiang Gongren Ribao* (Zhejiang Workers' Daily), Aug.7, 2002.

to buy out their enterprise (the net assets were valued at negative eight million USD),[80] Chinese SOE managers could usually not afford to buy the enterprises with their own money, as managers in the West might do. On average, an SOE manager in China earned no more than $300 per month in the mid 1990s, and even much less from the 1950s to 1980s. Their personal wealth (including privatized apartments) per household was usually no more than $10,000. They were clearly unable to simply buy out enterprises that held millions or billions of dollars in assets.

Nevertheless, in January 2006, according to a SASAC report, about half of the restructured SOEs were privatized through MBOs.[81] The observation is supported by a 2006 nationwide survey done by Guo, Gan and Xu. The survey found that 47 percent of the interviewed privatized enterprises in China could be identified as MBOs;[82] but, interestingly, the survey organizers reported that, "due to controversies about MBOs, firms underreport that they are MBOs… only 8.6 percent of the sample categorized themselves as MBOs."[83] Obviously,

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[80] The Assets Transaction Center of Shandong Province, "*Yantai Gongcheng Jixie Chang Paimai Gonggao* (The Auction Notice of Yantai Construction Machinery Factory), Project No. SZZR06038," Jinan, China, Aug. 10, 2006 (http://www.sdcqjy.com/column.action?exid=SZZR06038).

[81] Wen Sibao, "*Yunnan Guoqi Gaizhi Cuisheng Fubai Jituan, Dang Kan Han You Paohong* (Corruption Cadres were Found in SOE Gaizhi of Yunan Province, and the Media of the Communist Party Criticized of them)," Hong Kong, China, *Yazhou Shibao* (Asia Times), Jan. 8, 2006.

[82] Gan Jie, "Privatization in China: Experiences and Lessons," in James R. Barth, John A. Tatom, and Glenn Yago, eds. *China's Emerging Financial Markets: Challenges and Opportunities*, Berlin, Germany, and New York, NY, Springer, The Milken Institute Series on Financial Innovation and Economic Growth 8, 2008, 584. The sample size is 717.

[83] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," Seoul Journal of Economics, Vol.21, No.2, 2008, 319, footnote 3. The survey was conducted in early 2006 through telephone interviews done by a survey company that had close relationship with China's State Statistics Bureau, and named by the author as GGX Survey (G, G, X are the first letter of the last name of the three authors). The authors did not provide the organization name that financially supported the survey. Their random sample was drawn from the official database of China's all industrial firms with sales of 5 million yuan or more (the data

when the managers wanted to conceal their MBO operations, they refuse to admit it. The authors also found that, the average that each MBO manager paid was 7.2 million yuan; three-quarters of them paid 100 percent of MBO payments by cash, and one-quarter paid one-third of the cost in down-payments and expected to pay the rest from future profits of the firms.[84] The controversies regarding MBOs in China actually focus on a simple question: how did the SOE managers carry out the deal without the requisite personal funds to buy the shares in their enterprises?[85] Guo, Gan and Xu did not answer the question. According to Yu, in manufacturers, about 70 percent of SOEs chose the MBO route, particularly in the pharmaceuticals, electronics and machine building industries; geographically, more MBOs took place in coastal areas, especially in Guangdong Province, Shanghai Municipality, and Jiangsu Province; in terms of the approaches employed in MBOs, more than 50 percent of managers used a shell company to buy out SOEs, twenty percent personally bought their SOEs, and twenty percent used another investor or a trust company; in most cases the sources of funds were not explained, and very often were much larger than what managers could personally pay—it was thus certain that SOE managers usually had to borrow funds to complete the buyout.[86]

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were provided by China's State Statistics Bureau), and includes 3,065 firms (of which 898 were privatized firms). In their survey, if managers held more than 50 percent of shares of their enterprises, the privatization of the firm was defined as MBO.

[84] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," 9.

[85] Wang Xiaojie, "*Cong Jiuming Daocao dao Zhongshizhidi de MBO Zouxiang Hefang* (Where is MBO Moving: From A Key Method of *Gaizhi* to the Target of Criticism)."

[86] Yu Zhuhan, "*Wo Guo Guoyou Qiye MBO Wenti Yanjiu* (Research about MBO in China's SOEs)," 28-30.

From where, and how, did SOE managers borrow funds for the buyouts? The author collected 41 MBO cases in 20 provinces, municipalities and autonomous regions,[87] and found that, often with the help of local governments, SOE managers borrowed money from individuals, other enterprises, or banks, to buy their enterprises, then paid them back with the funds from the enterprises; in other words, in these manager privatizations, the managers did not really invest their personal money in the buyout, and the privatization was a low-cost, if not zero-cost, game, enriching SOE managers.

Actually, according to China's bank regulations, individuals are not allowed to borrow money from banks to buy shares or stocks.[88] If a CEO of an SOE borrowed loans from a bank with the guaranty of the SOE, he should not spend the money of the SOE for personal use, e.g. to buy an apartment for his family, or buy out the SOE where he worked. Analyzing the 41 cases materials, the author found that a lot of Chinese SOE managers were able to obtain loans from banks to carry out MBO, and bank regulations and laws were ignored by local governments and bank officials.

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[87] The 41 cases were found in following 20 provinces, municipalities and autonomous regions: Anhui Povince, 1; Beijing Municipality, 1; Chongqing Municipality, 2; Gansu Province, 1; Guangdong Province, 2; Guangxi Autonomous Region, 1; Heilongjiang Province, 1; Henan Province, 5; Hubei Province, 4; Hunan Province, 2; Jiangsu Province, 3; Jilin Province, 1; Neimenggu Autonomous Regions, 2; Shandong Province 6; Shanxi Province, 1; Sichuan Province, 4; Tianjin Municipality, 1; Xinjiang Autonomous Region, 1; Yunnan Province, 1; Zhejiang Province 1.

[88] From 1979 to 2008, China's regulations on bank loans did not allow banks to lend money to individuals for buying stocks or shares. Only after December 2008 when the Chinese government issued a new regulation, banks were allowed to lend money to activities for mergers and acquisitions. See "*Jiangsu Sanyou Gaoguan Weigui Dongyong Xindai Zijin MBO* (MBO Senior Managers of the Sanyou LLSC in Jiangsu Province Illegally Used Bank Loans for MBO)," Shanghai, China, *Shanghai Zhengquan Bao* (The Shanghai Security News), Mar. 31, 2010.

For example, in Xinjiang Autonomous Region, a local government sold the Bayinguoleng Agricultural Machinery Company to its CEO. The CEO personally did not have money to pay, so he borrowed one and half million from a state-owned bank on Jan. 23, 1998, using the SOE as a guaranty. He paid a check of 1.5 million yuan to the local government on Jan. 25, and thus became the owner of the company. Actually, on Jan. 24, before the privatization was done, he wrote checks of 1.5 million from the account of the company payable to the bank. So the privatization did not cost the CEO a cent; he even did not pay any interest for the one-day borrowing. Later, disputes occurred in the company between the CEO and workers and staffs. After investigating the case the local government said: "This approach was not created by us, and has been used in other cities to promote reform. The government believes that we should borrow and learn successful experiences and practices from other cities and have a correct attitude towards the new approaches in the reform."[89]

In May 1998 in Yuanmou County of Yunnan Province, the county government approved the privatization of the Yuanmou Cement Factory; in the privatization the CEO of the enterprise was selected as the only eligible buyer for the sale of the factory at a price of about seven million yuan. The CEO personally borrowed one and half million yuan, and, under the instruction of the government, another SOE lent him five and half million, so he was able to buy out the factory. After several days, the CEO returned the five and half million yuan from the account of the

[89] Wang Nan, and Zhang Xuebiao, "*Wu Aimin Zhuang Gao Ba Zhou Guozi Ju* (Wu Anmin Sued the Bayinguoleng Administration of State Assets)," Beijing, China, *Zhongguo Jingji Shibao* (China Economic Times), Oct. 7, 1999.

privatized firm.[90] In other words, he obtained five and half million yuan of assets within days.

In Daye city of Hubei Province, when the Jing Wine Factory was privatized in 1998, the takeover bid by the factory's CEO was backed up by the local government that lent him all the cash needed to close the deal, and pressured workers to sell him their shares. "'I didn't even have to spend my own money,' the CEO said, grinning as he explained how he came to own what is now a thriving wine and beverage manufacturer with $35 million in annual sales."[91]

Similar practices were also found at the Tongqing Company in Pengshan County of Sichuan Province in 1994,[92] the Boda Company in Kaifeng city of Henan Province in 1994,[93] the Jialing Chemical Plant in Chongqing Municipality in 1997,[94] the Changjiang Second Hydraulic Factory in Luzhou city of Sichuan Province in 1999,[95] the Tongda Company and the Xiangjiang Paint

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[90] "*Yuanmou Shuini Chang 'Siyou' Ji* (The Story of Privatization of Yuanmou Cement Factory)," Beijing, China, *Huasheng Bao* (Asia Today), Jan. 18, 1999.

[91] Philip P. Pan, "Workers in China Fail as Owners of Factories, Managers and Investors are Taking Over," Washington, DC, *Washington Post*, Dec. 4, 2002, Page A01.

[92] Xu Xiang, "*Sichuan Pengshan Tongqing Gongsi Liu Taiqing Nuoyong Qian Wan Gongkuan Neimu* (The Inside Story about How Liu Taiqing of the Tongqing Company in Pengshan County of Sichuan Province Embezzled Millions of Funds)," Chengdu, China, *Sichuan Newsnet*, Oct. 27, 2006 (http://www.51zhengyi.net/shownews.asp?NewsID=1969).

[93] Zhou Bin, "*Kaifeng Boda Gongsi Yuan Dongshizhang Liyong Qiye Gaizhi Fanzui Bei Pan Wu Nian* (The Chairman of the Board of Directors of the Boda Company in Kaifeng City was Sentenced for Seven Years for Crimes in *Gaizhi*)," Zhengzhou, China, *Henan Newsnet*, Dec. 31, 2005 (http://news.163.com/05/1231/12/26A6FME10001122E.html).

[94] Workers and Staff of the Jialing Chemical Plant, "*Chongqing Jialing Huagong Chang 'Gaizhi' Beijing ji Neimu* (The Background and Insider Story of the *Gaizhi* at the Jialing Chemical Plant in Chongqing Municipality)," Apr. 16, 2005 (http://www.xinmiao.com.hk/0004/0100-0139S.htm).

[95] Fang Yuan, "*Luzhou Gongren Dao Shizhengfu Kangyi Gaizhi Liyi Bei Boduo* (Workers in Luzhou City Protested at the City Government for the Consequences of *Gaizhi*)," Washington, DC, Radio Free Asia, Nov. 10, 2009.

Company in Changsha city of Hunan Province in 1999,[96] the Haizheng Pharmaceutical Group in Zhejiang Province in 2003,[97] the Beijing Heliotechnics in 2004,[98] the Sanyou LLSC of Jiangsu Province in 2004,[99] the Kaiyuan Engineering of Henan Province in 2006,[100] and the Liaoyuan Electronics Company in Xinxiang City of Henan Province in 2007.[101] These cases have a common feature: SOE managers bought out their SOEs with borrowed funds, and the sources of the funds were questionable. On the other hand, in the MBO of the Yutong Bus Manufacturer of Henan Province in 2001,[102] the Tianjin Watch Factory of Tianjin Munifipality in 2002,[103] the Conch Group

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[96] Fang Dafeng, "*Changsha: Hui Bie Guoqi* (Changsha: Good Bye to SOEs)," *Caijing* (the Finance and Economy Magazine), No.9, Sept. 5, 2000.

[97] Zou Guangxiang, "*Haizheng Yaoye de MBO Lujing* (The MBO Path at the Haizheng Pharmaceutical Group)."

[98] The Workers and Staff of the Beijing Heliotechnics, "An SOE Privatization Case," Beijing, China, *Dajun Observation*, Aug. 4, 2006 (http://www.dajunzk.com/guoqianli.htm).

[99] "*Jiangsu Sanyou Gaoguan Weigui Dongyong Xindai Zijin MBO* (MBO Senior Managers of the Sanyou LLSC in Jiangsu Province Illegally Used Bank Loans for MBO)," Shanghai, China, *Shanghai Zhengquan Bao* (The Shanghai Security News), Mar. 31, 2010.

[100] "*Kongshou Goude Qianwan Zichan, Yige Pochan Guoqi Laozong de Shangye Yunzuo* (Bought Millions SOE Assets but Paid Nothing: The Business Operation of the CEO of a Bankrupted SOE)," *Zhongguo Qingnian Bao* (Chinese Youth Daily), Jan. 17, 2007.

[101] "*Liaoyuan Dianzi Gongsi Gongren de Laixin* (A Letter from the Workers of Liaoyuan Electronics)," Oct. 30. 2008 (http://news.163.com/05/1231/12/26A6FME10001122E.html); "*Henan Jungong Qiye Chongzu, Yuangong Fuli Zao Boduo* (Workers were Exploited when a Military Industrial Enterprise in Henan Province Restructured)," Mar. 8, 2011, Radio Free Asia (Cantonese Branch).

[102] Xin Linchi, "*Shou Li MBO Liangnian Xuanan Diaocha, Yutong Keche Guozi Shifou Liushi* (An Investigation of the First MBO in China: Any Asset Stripping in the Yutong Bus Manufacture Case?)" *Jingji Guancha Bao* (The Economic Observation News), Jan. 28, 2004.

[103] Tian Wenlu, "*Tianjin Shoubiao Chang de Zhuanzhi Yintong* (The Pains of the *Gaizhi* at Tianjin Watch Factory)," Beijing, China, *Jizhe Guancha* (The Reporters' Observation), Apr. 2007 (www.kankan.cn/superlibtary/freearticle.asp?aid=27192).

of Anhui Province in 2002,[104] the Shandong Construction Engineering Plant of Shandong Province in 2003,[105] and of the Neicheng Pharmaceutical Factory of Shanxi Province in 2004,[106] the sources of MBO funds were questioned by some researchers or reporters, but the managers who completed the MBO declined to clarify from where they obtained the funds to buy out their enterprises.

MBOs in China might be under the cover of another company which could be called a shell or proxy company. A lot of Chinese SOE managers or their family members set up private companies with little private investment or with bank loans; then use such companies to purchase their SOEs at a cheap price. This approach had two advantages for the managers. Firstly, workers would not know who was behind the proxy company, and thus harbor less grievances towards managers who privatized the asset—into their own hands. Secondly, managers could easily borrow bank loans for the buyout through the proxy company using their SOE as a guaranty, an approach that got around the regulations prohibiting SOE managers from borrowing bank loans to buy shares with the company as guaranty.

A typical case in Guangxi Autonomous Region was revealed by reporters from CCTV in 2003: the SOE managers of Guilin Ferroalloy Works registered the Kangmilao private company; then claimed that the latter would pay 34 million in debt for the former company. With this

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[104] Zhang Honggang, "*Guanliceng Shougou (MBO) Dianxing Anli Yanjiu* (Research about Cases of Management Buy Outs)," Master's thesis, Dept. of Business Administration, The Southeast University, Nanjing, China, Jan. 2005, 33-35 (http://cdmd.cnki.com.cn/Article/CDMD-10286-2007065026.htm).

[105] Gong Xiangde, and Long Xiao, "*Binggou Shan Gong, Caterpillar Zhenghe Jihua Mai Chu Diyi Bu* (The Merger and Acquisition of Shandong Construction Engineering: The First Step of Caterpillar's Plan)," Beijing, China, *Zhongguo Gongye Bao* (The China Industrial News), Nov. 7, 2005.

[106] Liu Wei, "*Da Gudong Gaizhi, Qi Gaoguan Jianjie Konggu Yabao Yaoye* (Large Shareholder *Gaizhi*, Seven Senior Managers Indirectly Controlled the Yabao Phamaceutical," *Ershiyi Shiji Jingji Baodao* (The 21st Century Economic Report), Oct. 27, 2004.

promise the managers sold the former, which had 120 million net assets (a deliberate undervaluation) to the latter at the price of zero in 2002. The case was reported to the Anti-Corruption Bureau of the Guilin city government. When the reporters asked the Bureau about the results of official investigation of the case, officials privately said that they actually stopped the investigation, because otherwise they might have lost their jobs.[107] At the Xilin Iron and Steel Group in Yichun city of Heilongjiang Province, 33 managers of the SOE registered a private company with 70 million yuan borrowed from their SOE, then used the private company to privatize the SOE in 2006, obtaining 30 percent of the shares of the privatized enterprise. Interestingly, even though such an operation was obviously against SASAC regulations in 2005, the provincial bureau of SASAC still approved it.[108]

Similar practices were also found in the privatization of the Xinlian Electronics of Jiangsu Province in 1999,[109] the Linyi Construction Equipment of Shandong Province in 2003,[110] the Tiangong Special Engineering Company of Hubei Province in 2004,[111] the Neimenggu Scientific

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[107] Fa Zhan, and Ning Ke, "*Ji Ge Yi Zichan bei Jianmai, Guangxi yi Daxing Guoqi Suoshui Neimu bei Jie* (Assets of 230 Million were Cheaply Sold at a Price of 33.5 Million, the Inside Story at a Large SOE in Guangxi was Revealed)."

[108] Zhao Weimin, and Long Hao, "*Xi Gang Gaizhi Mituan* (the *Gaizhi* Puzzle at the Xilin Steel Group)," *Zhongguo Jingji Shibao* (China Economic Times), Feb. 22, 2010.

[109] "*Xinlian Dianzi IPO Cunyi: 'Quxian' Huoqu Guoyou Zichan, Gaizhi Cun Xiaci* (The Questionable IPO at the Xinlian Electronics: Obtaining SOE Assets 'Indirectly,' Problems Exist in the *Gaizhi* of the Enterprise)," Hong Kong, China, *Jingji Daobao* (The Economic Guidance), Jan. 8, 2011.

[110] Wang Haiyan, and Lu Peng, "*Shandong Lin Gong MBO Chedi Diaocha* (A Thorough Investigation of the MBO of Linyi Construction Equipment)," Beijing, China, *Shangye* (Commerce), Apr. 10, 2006.

[111] Dai Jingsong, and Wei Mengjina, "*Wuhan Tiangong 'Ziben Yunzuo': Ji Duo Anliu Juan Kong Guoyou Qiye* (The Capital Operation of the Tiangong Company in Wuhan City: SOE was Emptied," *Jingji Cankao Bao* (Economic Information Daily), Aug. 1, 2007.

Instruments Company of Neimenggu Autonomous Region in 2005,[112] the Taian Crane Machine Manufacturing of Shandong Province in 2005,[113] and that of the Guoxing Electronics of Guangdong Province in 2007.[114]

In some cases, SOE managers personally decided to invest SOE funds in a private business; then they registered a new joint private company with the private business partner; the SOE managers thus became owners in the joint private company without a personal investment. For example, in Gansu Province, the CEO of Liancheng Aluminum Manufacturer used 36 million yuan from his SOE to buy land through a businessman for potential real estate development; then the two parties established a private company. During the process, the CEO personally took bribes of 3 million yuan from the businessman, as the personal investment of the CEO in the private company.[115]

When arranging MBO of small SOEs, managers could temporarily borrow several millions from state-owned banks, then pay back with the funds of the enterprises after manager's privatization was done. The privatization of medium- and large-sized SOEs would need hundreds of millions, and SOE managers may encounter difficulty to obtain such huge amount of loans. Since the beginning of the 21st century, sophisticated approaches to finance managers'

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[112] Li Zhongfeng, "*Neimenggu Yi Guoyou Qiye Zao Jianmai, 317 Wan Jing Zichan Jin Mai 39 Wan* (An SOE was Cheaply Sold in Inner Mongolia, 3.17 Net Assets Sold at 390 Hundred)," Beijing, China, *Shichang bao* (The Market Daily), Oct. 29, 2007.

[113] "*Yan Gong, Tai Qi Gaizhi Miwu* (The *Gaizhi* of Taian Crane Machines in the Fog)," *Zhongguo Jingji Shibao* (China Economic Times), June 13, 2007.

[114] Tiantai Research, "*Guan Kui Guoxing Guangdian: MBO Qi Neng Bawang Yinshanggong?*（Exploring the Guoxing Electronics: How Could an MBO be Done Like this?)"

[115] Yang Wei, "*Zhiming de Hezuo* (The Fatal Cooperation)," *Nanfang Zhoumo* (The Southern Weekend), Oct. 5, 2000.

privatization of large SOEs have been developed in China. One of the new approaches for SOE managers was to establish a trust and investment company, or through an existing trust company, to borrow money from individual investors or financial institutions in order to buy an SOE, then use the money of the privatized enterprise to pay back to the investors. Such operations were sometimes arranged by local governments.

In Shandong province, the managers of a listed large SOE which had 1.25 billion assets, the Zhangyu Wine Group, decided in Oct. 2004 to carry out an Employee Management Buyout (EMBO) privatization, but the board of directors of the company never held a meeting to discuss the issue. The plan was approved by local government, Yantai city government. In the privatization process, 45 percent of the shares of the company were sold to insiders at a price of 388 million, of which 18 percentages sold to 14 senior managers, 10 percentages to 150 middle-level managers, and 17 percentages to 2000 workers and staff. To buy the shares, workers and staff had to pay cash in full amount, whereas middle-level managers paid half of the value of their shares by cash, and the 14 senior managers who bought shares valued as 154 million only paid 10 percent in cash. To pay the rest of the amount, the senior and middle level managers collectively borrowed 174 millions to buy their shares from a trust and investment company, with no any guaranty but their managerial status. A worker of the company told a reporter that the privatization was arranged for the managers. After the privatization, the CEO of the Zhangyu Wine Group individually obtained 3.24 percent of the total shares of the company with a purchase price of 28 million. He said in an interview that, personally, he would never be

able to pay back the amount he borrowed for buying the shares.[116] After the MBO, the manager-owners arranged very high dividend distribution (the dividend rate was more than 50 percent per year) from the profit of the company to themselves.[117] Thus they were able to pay back the 174 million they borrowed with the large amount of dividend income.[118] The privatization practice was once questioned by media in China, but the managers of the company responded that all the deals were reasonable and legal, and the local government kept quiet. The MBO of the Suzhou Chemical Factory of Jiangsu Province in 2003 were completed by borrowing 125 million through a trust company;[119] and the MBO of the Wuhan Organic Chemical Company was so done as well.[120]

In China, the above cases were called the MBO through direct purchasing. In such operations the managers personally used SOE assets as guaranty to borrow huge amount of money to privatize the enterprise into their hands. The legality of such a method in China was questionable, but the managers who used the method were often protected by local governments from legal investigations. In order to avoid legal problems, there also appeared a more

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[116] He Yuxin, "*Shui Kongzhi le Zhangyu Gaizhi?* (Who Controlled the *Gaizhi* of the Zhangyu Wine Group)," 77-79.

[117] Huang Weihua, Liu Xiuchun, and Qiu Yizheng, "*MBO Shangshi Gongsi Gao Xianjin Fenhong Xingwei Fenxi* (An Analysis of the High Dividend Distribution Behavior of the Listed MBO Companies)," Beijing, China, *Caiwu yu Kuaiji, Licai Ban* (*Finance and Accounting, the Wealth Management Version*), No.3, 2010.

[118] "*Zhangyu MBO Anli* (The MBO Case of the Zhangyu Wine)," Oct. 7, 2010 (http://wenku.baidu.com/view/f5eac129647d27284b735165.html).

[119] Chen Rui, "*Jieli Xintuo Wancheng MBO, Daxing Guoqi Chedi Minying* (MBO was Completed through a Trust Company: A Large SOE was Thoroughly Privatized," Nanjing, China, *Jiangsu Jingji Bao* (Jiangsu Economic News), May 20, 2003.

[120] Zhang Honggang, "*Guanliceng Shougou (MBO) Dianxing Anli Yanjiu* (Research about Cases of Management Buy Outs)," Master's thesis, Jan. 2005, 24-26.

complicated MBO method through indirect purchasing. The MBO through indirect purchasing was so operated: SOE managers borrowed certain amount of money to register a private company owned by them; then they used their new private company to borrow funds from other companies, or from the public through a trust company, to finance the managers' privatization; after the privatization was done, the managers used the profit, revenue or assets of the privatized enterprise to pay back the borrowed funds. Some economists in China perceived such financial operation as a financial instrument innovation for manager's privatization; and some called it an implicit MBO.[121]

For instance, in Sichuan Province, the managers of the Quanxing Spirits Group arranged an MBO plan to privatize their enterprise. On Sept. 24, 2002, the managerial group of the company signed an agreement with local government, the Finance Bureau of Chengdu city, to buy the SOE which had 609 million of net assets, but at that time the managers did not pay any cent to the government. Upon the agreement, the managers claimed that they became owners of the company, and the SOE was nominally privatized; at least, the local government so recognized it. On Nov. 2002, eighteen senior managers of the company borrowed 58 million from unknown sources and registered the Yingsheng Investment Company, which announced that it held two thirds of total shares of the privatized Quanxing Wine Company, which was valued as 413 million. Next, the managers used their ownership of the company as guaranty, arranged an agreement on Jan. 15, 2003 with a trust and investment company, which issued a

[121] "*Zhangyu MBO Anli* (The MBO Case of the Zhangyu Wine)."

trusted financial product to institutional and individual investors and obtained 270 million. Then the managers used the 270 million to pay their due payments in the privatization project on Jan. 29, 2003. In the following three years they paid back the 270 million with interest to the trust and investment company. This MBO case was introduced in China as a successful example.[122] According to an analysis about financial situation of a subsidiary company of the Quanxing Group, from 2004 to 2008 the net profit of the subsidiary company was 764 million, of which 633 million (83 percent of the profit) were distributed as dividends to its new private owners (67 percent of the ownership was held by the managers). With such high dividend income, the managers were able to pay back the borrowed funds to the investors.[123]

Also in Sichuan Province, the managers of the Jiannanchun Spirits Group, an SOE with 929 million of net assets, decided to conduct an MBO in 2003, without the approval of its employee owners who held 17 percent of shares of the company.[124] Twenty managers of the Jiannanchun Group registered the Tongsheng Investment Company on Sept. 15, 2003, which total registered capital was 20 millions. On Sept. 30, 70 percent of the shares of the Jiannanchun Group (646 million) were transferred to the Tongsheng Investment, and nine percent of the

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[122] Leng Hongchuan, "*Guoyou Qiye MBO zhi Lu: Quanxing Jituan he Jiannanchun Jituan Shishi MBO Fenxi* (The Path of MBO for SOEs: An Analysis of the MBO Cases of Quanxing Group and Jiannanchun Group)," Nov. 6, 2010 (http://wenku.baidu.com/view/f1fcfd60ddccda38376bafe5.html).

[123] Huang Weihua, Liu Xiuchun, and Qiu Yizheng, "*MBO Shangshi Gongsi Gao Xianjin Fenhong Xingwei Fenxi* (An Analysis of the High Dividend Distribution Behavior of the Listed MBO Companies)."

[124] "*Jiannanchun Youxing Zichan Suohui Jiu ge Yi, MBO Luoding, Xilie Pinpai Xuankong: Jiannanchun Guo Gai Si Shenmi Guocheng* (The Assets of the Jiannanchun Group Shrank to 900 Millions and MBO was Done: the Mysterious Privatization of the Jiannanchun Group," *Zhongan Zaixian* (The Zhongan Online), Jan. 8, 2004 (http://finance.anhuinews.com/system/2004/01/18/000546076.shtml).

shares were transferred to the Blue Sword Company. On Jan. 6, 2004, the Finance Dept. of Sichuan provincial government approved the transaction. The payment of the transaction was so arranged: the Tongsheng Investment borrowed 300 million from the Blue Sword Company and pay the amount to the state owner, and the managers immediately obtained 70 percent of ownership of the Jiannanchun Group; then, in the next four years the managers used the dividends they received and the revenues through selling part of the assets of the Jiannanchun Group to pay the rest of the amount to the state owner.[125] This method was also used by the Yili Dairy Group in Neimenggu Autonomous Region in 2003,[126] the Haizheng Pharmaceutical in Zhejiang Province in 2004,[127] and the Twin Star Company in Shandong Province in 2006.[128]

In order to encourage SOE managers to privatize their enterprises through MBO, some local governments offered discount on transaction prices of SOE assets, as "reward" to the managers. For example, in Guangdong Province, when the provincial government transferred the assets of the Huaqiang Group to its managers in 2003, the appraised net assets of the SOE in amount of 539 millions were discounted by the government to 185 millions;[129] in Shandong

[125] Leng Hongchuan, "*Guoyou Qiye MBO zhi Lu: Quanxing Jituan he Jiannanchun Jituan Shishi MBO Fenxi* (The Path of MBO for SOEs: An Analysis of the MBO Cases of Quanxing Group and Jiannanchun Group)," Nov. 6, 2010.

[126] Zhang Fan, and Su Dandan, "*Yili MBO Lu Zouxiang Zhongdian* (The MBO of the Yili Dairy Went to Its End)," Beijing, *Caijing* (the Finance and Economy Magazine), No.26, Dec. 26, 2005.

[127] Zou Guangxiang, "*Haizheng Yaoye de MBO Lujing* (The MBO Path at the Haizheng Pharmaceutical Group)."

[128] Long Hao, "*Qingdao Shuangxing de Tuoxie zhi Tong* (The Pains of Twin Star in Qingdao City)," *Zhongguo Jingji Shibao* (China Economic Times), Nov. 21, 2007.

[129] Qin Yongzhao, "*Guoqi Zhigong Jiekai Caichan Fenpei de Heimu* (The Insider Story of a Plot in the Distribution of SOE Assets at the Huaqiang Group)," Beijing, China, *Dajun Guancha* (Dajun Observation), Nov. 14, 2005 (www.dajunzk.com/caichanfp).

province, the Yantai city government offered the managers of the Zhangyu Wine Group 115 million as discount and reward for the MBO of the SOE in 2004;[130] in Henan Province the Changge city government in 2004 allowed the managers of the Changge Power Plant to deduct fifteen million from the transaction price of the MBO of the SOE as reward and discount;[131] in Hubei Province, the Huangshi city government offered the managers of the Huangshi Industrial and Mine Group 66 percent of the shares of the company (twelve million) as a reward for the MBO of the company in 2005;[132] in Jilin province, based on the "Regulation about Share Reward to Managers of *Gaizhi* SOEs" issued by the provincial government in 2007, the government offered the managers of the Tonghua Steel Factory shares in value of 100 million as reward for privatization in 2009. [133]

Another hidden or informal approach for MBO is worth noticing. Many industrial administrative offices in governments at different levels were renamed as state shareholding companies since the late 1990s. The governmental "mother companies" still controlled industrial SOEs until the SOEs were privatized. Often, when SOEs under the "mother companies" were privatized the state might still hold a part of the ownership of the enterprises; then the "mother

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[130] He Yuxin, "*Shui Kongzhi le Zhangyu Gaizhi?* (Who Controlled the *Gaizhi* of the Zhangyu Wine Group)," 78.

[131] Wang Jinfu, and Cheng Honggen, "*Henan Yi Dianchang Gaizhi Anxiang Caozuo: 1,500 Wan Mai Xia 1.2 Yi Qiye* (The *Gaizhi* of a Power Plant in Henan Province was Operated in Black Box: An SOE with 120 Million Assets was Sold at 15 Million)."

[132] "*Guoqi Gaige Buneng Cheng Naoju* (SOE Reform should not Become a Farce)," *Renmin Ribao* (The People's Daily), Mar.22, 2005.

[133] "*Jianlong Chongzu Tonggang Jituan Zai Diaocha* (The Reinvestigation of the Takeover of Tonghua Steel Co. by the Jianlong Group," *Xin Jing Bao* (The New Beijing Daily), Aug. 14, 2009.

companies" would send some board members to the boards of the partially privatized enterprises. A hidden MBO could take place when the board members from the "mother company" worked together with the CEO of a privatized firm, the CEO could obtain a full control over the partially privatized firms with little personal investment. For instance, the Chongqing Meter and Instrument Factory in Chongqing Municipality with net assets in 34 million was privatized in 1998, while its "mother company" held 34 percent of shares of the privatized company (the Naide Industrial LLSC), employees held 36 percent, and managerial staff held 30 percent (of which eight percentage was assigned to the legal representative of the firm, i.e., the CEO, and two percentage to the two board members from the "mother company").[134] In the ownership structure the managers did not occupy a dominant portion; however, the CEO of the Naide Company was also the deputy CEO of its "mother company;" therefore, he was able to "represent" the 34 percent of the state ownership with the support of the other two board members from the "mother company," and was elected as the chairman of the board of directors.[135] In 2004, when the CEO no longer occupied the position of the deputy CEO of its "mother company;" he forced the employee shareholders to give up their shares and personally

[134] "*Chongqing Naide Gongye Gongsi de Chanquan Zhidu Gaige Jiqi Chengxiao* (The Property Rights Reform at the Chongqing Naide Industrial Company and Its Effects," Chongqing, China, *Juece Daokan* (The Decision Making Guidance Magazine), No.5, 2001, 24.

[135] "*Shizai Zuoren, Renzhen Zuoshi: Fang 1980 Ji Xiaoyou Lin Chaoyang* (An Interview to Our 1980 Class Mr. Lin Chaoyang)," Chongqing, China, *The Website of the Chongqing Technology and Business University* (http://60.ctbu.edu.cn/index.php?action-viewnews-itemid-622), visited on 5/16/2012.

obtained the 34 percent of employee shares without paying any cent.[136] In this way, the earlier informal MBO became a formal MBO.

In Western societies, asymmetric information possessed by managers may lead to the principal-agent problem and moral hazard in MBO process; and corporate valuation in insider trading is often subject to considerable ambiguity, as it can be heavily influenced by asymmetric or inside information. In China, more problems emerged in its MBOs. A Chinese scholar points out that in China's MBOs three problems are often questioned: whether the valuation of SOE assets were properly done, were the financial resources used by managers to buy the assets problematic, and if the MBOs were operated with transparency and fairness.[137] From the MBO cases introduced above, readers could easily find that the problems were quite apparent. First of all, SOE managers were all appointed by governments, but not selected through market mechanism. After MBO the managerial *nomenklatura* suddenly became millionaires, if not billionaires, through questionable procedures. Whether did such transactions of state assets challenge the principle of social justice remains a controversial issue in China. Second, most MBO practices were silently operated in black box, and huge amount of state assets were sold by SOE managers to themselves with cheap price. Third, some SOE managers simply used the funds of their enterprises or bank loans based on the guaranty of their enterprise assets to buy the firms; some hired financial institutions to raise funds from the public for managers' privatization; and some paid

[136] The Workers of Chongqing Meter and Instrument Factory and the No. 3403 Military Factory, "*Yige Zai Jiuye Dianxing de Heimu* (The Inside Story of Lin's Company)," Dec. 20, 2004 (www.chinasoe.com.cn/review/debate/2011-08-22/1479).

[137] Liu Meng, "*MBO Chuang Fu: Neiburen Caokong de Youxi* (Enriching through MBO: A Game Manipulated by Insiders)."

themselves very high salaries, bonuses and dividends after privatization, then used the money to pay their debts for buying their SOEs.[138]

Some Chinese economists defend the practices by suggesting that, if SOEs were making losses, property rights of the enterprises should be given to managers for saving the enterprises from sinking; and, if SOEs were in good conditions, the managers ought to receive a large portion of shares as incentive.[139] At the other side, counter argument emphasizes social justice in MBO process. A metaphor often mentioned is that MBO in China has become a pattern that a housekeeper altered himself to a house owner.[140] As the central government once again approved MBO at the end of 2005, and the propaganda machine of the regime prohibited further discussion about the issue, the debate was gradually silenced.

MBO was once described in China's media as the last grand banquet for SOE managers.[141] Garnaut et al. point out that "[t]he ongoing privatization, especially MBOs, has resulted in the loss of a large amount of state assets to the benefit of a small number of private individuals and SOE managers. It is clear that *gaizhi* has been a messy process often associated with asset stripping. It is difficult-perhaps impossible-to quantify the extent of this type of abuse."[142] When analyzed the 41 MBO cases exposed in China's media, the author noticed that in 32 cases the problems emerged had

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[138] Ibid.

[139] "*Zhang Weiying Huiying Lang Xianping: Shandai wei Shehui Zuochu Gongxian de Ren* (A Response from Zhang to Lang: Kindly Treat Managers Who Made Contributions: An Interview to Zhang Weiying)," *Jingji Guancha Bao* (Economic Observation News), Aug. 28, 2004.

[140] *"Shi Shui Zai Hemou 'Boxue' Guoyou Zichan* (Who is 'Exploiting' State Assets: An Interview to Lang Xianping)," Aug. 13, 2004 (http://www.globalview.cn/ReadNews.asp?NewsID=1778).

[141] Xie Heng, "*Shi Wan Yi Guoyou Zichan Chongzu de Caifu Jihui* (The Opportunities in Reorganizing 10 Trillion State Assets)," 28.

[142] Ross Garnaut, et al. *China's Ownership Transformation: Process, Outcomes, Prospects*, 49.

never been investigated by local governments even though in some enterprises workers wrote petitions to the governments to report the corruption of their managers, four cases were investigated but no formal charge was filed, and only in five cases charges against corrupt SOE managers were filed.

3.2 Employees Shareholding

Employee shareholding had been experimented since early 1990s in China. Employee ownership might have some advantages: when both managers and employees were owners, the insider privatization provided both parties greater incentive to improve performance as they might share the benefits of the improvement.[143] The experiment in China was often called the shareholding cooperative system with an emphasis on employee's equal rights and collective occupation of the assets of enterprise.[144] Employee shareholding could bring about some changes in management-employee relations. In some firms, employee shareholders elected and monitored their managers;[145] however, in other firms, managers were still at the dominant position while the board of directors was either under the control of managers or was not established, and employee

[143] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," in Robert W. McGee, ed. *Corporate Governance in Transition Economies*, Springer, New York, 2008, 225.

[144] Li Chuanxin, "*Dangqian Gufen Hezuo Zhi Qiye Gaige Zhong Cunzai de Wenti he Duice* (The Problems and Solutions in Current Reform of the Shareholding Cooperative System)," *Shanghai Gaige* (Reform in Shanghai), No.3, 1998, 20; Zhang Daijing, "*Gufen Hezuo Zhi Qiye yu Zhigong Zhurenweng Diwei* (The Shareholding Cooperative System and the Position of Workers as Masters)," *Shanghai Gaige* (Reform in Shanghai), No.7, 1998, 35.

[145] Zhang Daijing, "*Gufen Hezuo Zhi Qiye yu Zhigong Zhurenweng Diwei* (The Shareholding Cooperative System and the Position of Workers as Masters)," 36.

shareholders could hardly oversee their managers.[146]

In small industrial SOEs, employee shareholding could be used for EBO (employee buyout), and the enterprises were thus transformed to LLSCs; but in large SOEs, the investment of employee shareholders was too small to take over and the state remained to be the dominant owner.[147] For instance, at the Shanghai Second Iron and Steel Factory, 95 percent of employees bought shares of their enterprise in 1995; their total investment was 44 millions, only equal to eight percent of the total capital of the factory and the enterprise was still categorized as an SOE.[148] In Shanghai, the largest industrial city with the best industrial administrative capacity in China, among 2,272 industrial SOEs of the city, only eight carefully selected industrial SOEs adopted the shareholding cooperative system in 1995. The experiment in Shanghai reached some successes, as the total profit of the eight firms after the implementation of employee shareholding was immediately increased by two thirds.[149] As of April 1994, there were 9,069 LLSCs (including non-industrial LLSCs) in China and 21 percent of the shares of the companies were held by employees.[150]

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[146] Li Chuanxin, "*Dangqian Gufen Hezuo Zhi Qiye Gaige Zhong Cunzai de Wenti he Duice* (The Problems and Solutions in Current Reform of the Shareholding Cooperative System)," 20; Ju Lixin, "*Zhigong Chigu: You Gufen Hezuo Zhi Dao Gongsi Hua Gaizhi* (From Shareholding Cooperative to Corporatization)," *Shanghai Gaige* (Reform in Shanghai), No.6, 2001, 7-8.

[147] Ju Lixin, "*Zhigong Chigu: You Gufen Hezuo Zhi Dao Gongsi Hua Gaizhi* (From Shareholding Cooperative to Corporatization)," 6.

[148] Li Nanshan, "*'Liang Gang' Jianli Zhigong Chigu Hui de Tansuo* (Exploration in Employee Shareholding at the Second Iron and Steel Factory)," *Shanghai Gaige* (Reform in Shanghai), No.4, 1996, 32.

[149] The Office of Economic Reform in Shanghai Municipality Government, "*Shanghai Guoyou Qiye Gaige Jinzhan Zongshu* (An Introduction about the Progresses of SOE Reform in Shanghai)," *Shanghai Gaige* (Reform in Shanghai), No.11, 1996, 18.

[150] Ju Jinwen, "*Yuangong Chigu Jihua yu Guoyou Qiye Chanquan Gaige* (Employee Shareholding and the Property Rights Reform in SOEs)," Beijing, China, the Research Center for Development under the State Council, *Guanli Shijie* (Management World), No.6, 2000, 86.

After the summer of 1997 the central government began to encourage the nationwide implementation of employee shareholding as an important approach for *gaizhi*, particularly for small and medium SOEs.[151] The policy perceived manager shareholding as a part of employee shareholding, because in the discourse of state socialism both managers and workers were SOE employees. As of 2001, in many SOEs managers' and employees' shareholding had been adopted.[152] Guo et al found in their 2006 survey that, among employee shareholders, each employee on average paid 33 thousand yuan (4,075 USD); 96 percent of them bought shares with cash.[153]

However, unlike in Russia, there was no any law or nationwide standardized program in China to instruct the employee shareholding practices;[154] and about 30 provincial governments carried out various policies,[155] not only different across regions, even within a province disagreements existed between the office for economic reform, the office of state assets administration and labor union.[156] Some scholars even depicted employee shareholding in China as

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[151] Zang Chuanzhi, Lin Yu, and Liu Juan, "*Ji, Lu, Gan Chengshi Gufen Hezuo Zhi Diaocha* (An Investigation of the Cooperative Shareholding System in Hebei, Shandong and Jiangxi Province," *Jingji Cankao Bao* (Economic Information Daily), Oct. 28, Oct. 29, Oct. 30, 1997.

[152] Gao Shangquan (former deputy director of the State Commission for Economic Reform), "*Guanyu Woguo Zhigong Chigu Zhi de Ruogan Wenti Tantao* (A Discussion about Several Issues in China's Employee Shareholding System)," *Shanghai Gaige* (Reform in Shanghai), No.9, 2001, 5-6.

[153] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," 9-10.

[154] *Ibid*, pp.6-7.

[155] Ju Jinwen, "*Yuangong Chigu Jihua yu Guoyou Qiye Chanquan Gaige* (Employee Shareholding and the Property Rights Reform in SOEs)," 88; Zheng Shao, and Fu Erji, "*Zhigong Chigu Zhidu Yanjiu Zonghe Shuping: Beijing, Xianzhuang, Mudi, Wenti, he Jianyi* (A Summary of the Researches about Employee Shareholding: Background, Current Situation, Purposes, Problems and Proposals)," *Shanghai Gaize* (Reform in Shanghai), No.6, 2001, 21.

[156] Wang Jianping, and Fang Baoguo, "*Guifan Tuijin Zhigong Neibu Chigu Zhidu: Shanghai Fayuan, Gaoxiao, Zhengfu, Qiye, Gonghui Lianhe Zhuanti Yantao Zongshu* (Regulating and Promoting the Institutions of Employee Shareholding: A Discussion among Participants from Shanghai's Supreme Court, Universities,

"full of loopholes."[157] In a discussion in Shanghai in 2001, Chinese scholars pointed out that the three original goals in promoting employee shareholding, i.e. letting employees share profits, establishing an incentive mechanism for employees so they could more care about the performance of their enterprises, and cultivating the consciousness as masters of enterprises among employee shareholders, were not reached for three main reasons. The first was the poor regulation. The second was that employee shareholders' rights were not legally protected. And the third reason was that in a lot of enterprises employee shareholding became a forced action by managers.[158]

Indeed, many SOE employees did not want to invest money from their pockets to the enterprises they worked for, and often did not have enough personal savings to do so, as their wages were kept very low for decades by the state.[159] But a lot of SOE managers forced workers to buy employee shares in exchange for keeping their jobs.[160] If workers declined to do so, some managers would threaten them with cutting wage or laying off, in an excuse that "employee shareholding is a reform policy, if you do not buy the shares you are opposed to the reform thus should be punished."[161] In 640 sampled enterprises where managers adopted employee

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Government Offices, Enterprises, and Labor Unions)," *Shanghai Gaize* (Reform in Shanghai), No.9, 2001, 47-48.

[157] Ibid. p.48.

[158] Ibid. pp.47-51.

[159] Zheng Shao, and Fu Erji, "*Zhigong Chigu Zhidu Yanjiu Zonghe Shuping: Beijing, Xianzhuang, Mudi, Wenti, he Jianyi* (A Summary of the Researches about Employee Shareholding: Background, Current Situation, Purposes, Problems and Proposals)," 23.

[160] Ju Jinwen, "*Yuangong Chigu Jihua yu Guoyou Qiye Chanquan Gaige* (Employee Shareholding and the Property Rights Reform in SOEs)," 88; Zheng Shao, and Fu Erji, "*Zhigong Chigu Zhidu Yanjiu Zonghe Shuping: Beijing, Xianzhuang, Mudi, Wenti, he Jianyi* (A Summary of the Researches about Employee Shareholding: Background, Current Situation, Purposes, Problems and Proposals)," 22.

[161] Qin Hui, "*Bu Rugu Zhe Kou Gongzi?* (Cut Wage or Be a Shareholder?)" *Nanfang Zhoumo* (The Southern

shareholding, Chinese scholars found that 63 percent of the enterprises forced their employees to buy shares of their own factory with various methods (see Table 8-3).

Table 8-3 Methods to Force Employees to Buy Shares

Punishment Methods when Employees Did not Want to Buy Shares	%
Jobs were kept only after shares were bought	44
Those did not buy shares were moved to positions with low wages	22
Wages and benefits were cut	19
No longer received wages	9
Dismissal or firing	6
Total	100

Source: Ju Jinwen, "*Yuangong Chigu Jihua yu Guoyou Qiye Chanquan Gaige* (Employee Shareholding and the Property Rights Reform in SOEs)," Beijing, China, *Guanli Shijie* (Management World), No.6, 2000, 87. Ju cited the survey results from a survey report of the China Social Survey Institute, but the details of the survey were not introduced in his essay.

In some SOEs the compensation funds paid to the enterprises by governments to buy off workers' permanent employment status was detained by managers, and employees were instead given shares of their enterprises,[162] and such an approach was approved by some local governments.[163]

Employee shareholding in China may also serve as a supplement for MBO. For example, at the Zhangyu Wine Group, when managers obtained dominant shares of their company,

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Weekend), Mar. 17, 2000.

[162] Ross Garnaut, et al. *China's Ownership Transformation: Process, Outcomes, Prospects*, 49.

[163] The Administration Office of State Assets of Shanghai City, "*Guanyu Jinyibu Tuijin Guoyou Ziben cong Xiao Qiye zhong Tuichu Gongzuo de Ruogan Yijian* (Several Policies for Promoting Privatization of Small SOEs)," June 22, 2000 (www.1128.org/html/zcfg/zxqy/2004/07/doc15437).

employees were encouraged to buy small amount of shares, thus the MBO in the company could be perceived as a part of insider privatization and encountered little resistance from workers.[164]

From the point of view of ownership determination, the employee shareholding in China could be perceived as a kind of privatization. But, the employee ownership in China often does not allow the employee shareholders to exercise their owners' rights. Managers of employee shareholding companies and local governments in China often disregarded the rights of employee shareholders; thus employee shareholders in many enterprises simply became nominal owners, and could hardly speak and act as real owners of their enterprises. Their managers often did not report to shareholders, nor were institutions of overseeing managers by shareholders really established.[165] The properties of employee shareholders might even be peculated, but the employee shareholders found no way to defend their own rights, as local governments often stood on the side of managers or that of the purchaser of employee shareholding companies.

In order to observe various practices of employee shareholding in China, the author collected nineteen cases from eleven provinces, municipalities and autonomous regions, and found that in six cases no disputes between managers and employee shareholders regarding the rights of employee ownership were reported,[166] but in thirteen cases such disputes were observed. The author identified

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[164] He Yuxin, "*Shui Kongzhi le Zhangyu Gaizhi?* (Who Controlled the *Gaizhi* of the Zhangyu Wine Group)," 77-79.

[165] Qin Hui, "*Bu Rugu Zhe Kou Gongzi?* (Cut Wage or Be a Shareholder?)"

[166] The six cases include the employee shareholding at the Shanghai Second Iron and Steel Factory (Li Nanshan, "*'Liang Gang' Jianli Zhigong Chigu Hui de Tansuo* (Exploration in Employee Shareholding at the Second Iron and Steel Factory)," 32), the Zhangyu Wine Group (He Yuxin, "*Shui Kongzhi le Zhangyu Gaizhi?* (Who Controlled the *Gaizhi* of the Zhangyu Wine Group)," 77-79) and the Julong Textille Company in Shandong province (Zhang Jun, et al, "*Weifang Shi Guoyou Qiye Diaoyan Baogao* (An Investigation of SOE Reform in

three methods used by managers to peculate the properties of employee shareholders.

Among the thirteen cases, seven refer to a method of transferring employee's ownership into another private company without permits of the employee shareholders. It was used in the sale of the Tongyu Textile Group in Yangzhou city of Jiangsu Province. This shareholding company was registered in 1999 with 59 million assets, of which 29 percent (eleve million) were cash investment of employee shareholders under the custody of the official labor union of the company. The members of the employee shareholders' committee of the company were not elected by employee shareholders, but appointed by managers. In 2003, the city government decided to sell the company to a questionable private company at a cheap price. In summer of 2003, under the pressure of the local government, the employee shareholders' committee of the company held a meeting to approve the sale. When the meeting was under the surveillance of more than ten plain-cloth policemen and three police cars parked outside of the meeting room, the attendants were requested to vote not by ballots but by raising hands. Under such circumstances the sale was approved; but workers of the factory involved in protests that had lasted for more than one year.[167]

Similar operation was found in Kaifeng city of Henan Province, where the Zhongzhou Mechanical Factory was restructured in 2000 and employee shareholders held 83 percent of

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Weifang City)," *Shanghai Gaige* (Reform in Shanghai), No.12, 2000, 47), and the other three cases in the power supply industry (the Jinyuan Company in Guizhou Province, the Lu Energy Company in Shandong Province and the Yinglite Company in Ningxia Autonomous Region) will be discussed later in this section.

[167] Wang Hui, "*Gaizhi yu Zhongguo Gongren Jieji de Lishi Mingyun: Jiangsu Tongyu Jituan Gaizhi Diaocha* (*Gaizhi* and the Historical Fate of the Chinese Working Class: An Investigation of the *Gaizhi at the Tongyu Group in Jiangsu Province*)."

shares. The factory was poorly managed for several years and in 2005 was sold to another company without compensation to employee investors. When the new owner refused to pay wages to workers, which was against the terms listed in the transaction contract, the workers of the factory wanted to cancel the transaction, but their request was rejected by local government.[168]

The author also found the same practices at the Linzhou Iron and Steel Company of Henan Province in 2004,[169] the Jialing Chemical Plant of Chongqing Municipality in 2004,[170] and in three companies of Sichuan province, the Hejiang Electric Company in Luzhou city in 2003,[171] the Guangda Pharmaceutical Company in Pengzhou city in 2005,[172] and the Twin Horse Cement Factory in Mianyang city in 2007.[173]

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[168] Liang Peng, and Gu Lilin, "*Kaifeng Yangban Guoqi 'Gai' Xiang Bailuo, 1,800 Zhigong Zouxiang Hefang?* (A Model SOE in Kaifeng City was 'Transformed' into Failure, Where could 1,800 Employees Go?)" *Jingji Cankao Bao* (Economic Information News), Apr. 17, 2004.

[169] Chen Yifang, "*Lin Gang Shijian Qianqian Houhou* (The Background and Consequences of the Event at Linzhou Iron and Steel)," Shanghai, China, *Xinmin Zhoukan* (Xinmin Weekly), Aug. 31, 2009.

[170] Yuan Ling, and Wang Rong, "'*Shoujia Gaizhi Guoqi Guquan Biangeng Heidong* (The First *Gaizhi* SOE: The Loophole in Its Ownership Changes);" the Workers and Staff of the Jialing Chemical Plant, "*Chongqing Jialing Huagong Chang 'Gaizhi' Beijing ji Neimu* (The Background and Inside Story of the '*Gaizhi'* at the Jialing Chemical Plant in Chongqing Municipality)," Apr. 16, 2005.

[171] "*Hejiang Dianli San Yi Duo Guoyou Zichan Jian Mai Jin Si Qian Wan, Fufu Lianshou, Zaojiu Xianwei Shuji Yi Wan Shenjia* (Hejiang Electric with More than 300 Million in Assets was Sold Cheaply at 40 Million, and the Party Secretary of the County and His Wife Got Rich)," Apr. 9, 2011.

[172] "*Sichuan Guangda Zhiyao Youxian Gongsi Baofa Gongren Bagong, Bagong Canyuzhe Jiashu bei Zhuisha* (Strikes at the Guangda Pharmaceutical in Sichuan Province, and the lives of Spouses of Some Protesters were Threatened)," Durham, NC, China Free Press, *Boxun Xinwen Wang* (Boxun Newsnet), Sept. 1, 2005 (http://boxun.com/news/gb/china/2005/09/200509010324.shtml).

[173] Lin Cong, "*Zai Guanliao he Ziben zhihou: Sichuan Shuangma Gongren Kangzheng Shijian Shuping* (Behind Bureaucrats and Capital: An Analysis of Workers' Protest at the Twin Horse Factory in Sichuan Province)," Aug. 5, 2007 (http://www.xinmiao.com.hk/0004/0100-0168S.htm).

Another method of peculating the properties of employee shareholders was forcibly transferring the employee's ownership into the hands of managers. For instance, in the Jing Wine factory in Daye city of Hubei province, seven hundred employees of the factory were asked that everyone invested six hundred USD to their enterprise in 1997 when they made about five hundred USD a year and had to borrow from friends or relatives to buy the employee shares. A year later, local government decided to back the takeover bid of the CEO of the factory, pressuring workers to sell him their shares and lending the CEO all the cash needed to close the deal. The party officials of the city held long meetings at the factory, telling workers that selling to the CEO was the only way the factory would survive. In a meeting the officials refused to break for lunch until every worker agreed to the deal. The local state banks lent the CEO the money he needed, and he paid every worker the face value of their shares plus ten percent.[174]

In Shanxi Province, the managers of the Ruibao Iron and Steel Group used similar method. This company was an employee shareholding company, as 70 percent of shares were held by about ten thousand of employees who organized a shareholding fund as a legal entity in 2003; however, in 2004 the managers of the company transferred the employee ownership to an official labor union of the company, which was controlled by the managers, without approval of the employee shareholders, and the official labor union was registered as new owner but paid nothing for the transaction.[175] Also, in the Wuzhou Shock Damper Factory of Jiangxi Province, the CEO of the factory played the similar game. 80 percent of 14 million assets of the company were

[174] Philip P. Pan, "Workers in China Fail as Owners of Factories, Managers and Investors are Taking Over."
[175] "*Chang Gang Gaizhi* (The *Gaizhi* in Changzhi Iron and Steel Group)," *Zhengquan Shichang Zhoukan* (The Security Market Weekly), No.23, June 24, 2006.

owned by employees collectively and 20 percent by employees individually. In order to privately obtain the employee collective ownership, the CEO forced employee shareholders to give up their individual ownership by paying them certain amount of compensation, then the restructured shareholding company was re-registered under the name of the CEO, his wife, and some unidentifiable persons.[176] In 2000, the managers of the Luohe First Paper Mill took back the shares of some employee shareholders after the company was listed on stock market, and gave the shares to their relatives and local officials. 73 employee shareholders of the company filed litigations against the action of the managers, but the local court refused to conduct the trail.[177] In 2004 at the Naide Industrial LLSC in Chongqing Municipality, the CEO of the company even forced employee shareholders to give their shares to the CEO for free.[178]

The case of the Shuangfeng Textile Factory located in Dafeng county of Jiansu province was the application of the third method, applying bankruptcy of the employee shareholding company without notifying employee shareholders, then reregistered a new private company under manager's name to occupy the assets of the employee shareholding company. Four thousand workers of the factory were forced to buy shares of the enterprise in 1996. Many workers invested large portions of their life savings, about five to six hundred USD per worker

[176] Li Xinde, and Li Ming, "*Jiangxi: 6,501 Wan Yuan Zhigong Guquan bei Lueduo Neimu* (The Inside Story about How 65 Million Property Rights of Employees' Shares were Confiscated," Beijing, China, *Zhongguo Xingzheng Jiandu Wang* (The China Website for Monitoring Administrations), Apr. 5, 2008 (http://www.zgxzjd.cn/article/show.asp?id=139).

[177] Shi Po, "*Bei Yiwang yu Bei Sunhai Zhe* (The Forgotten and Damaged People)," China, *Nanfeng Chuang* (The Window for the Wind from South), March 1 -15, 2002, 29-30.

[178] The Workers of Chongqing Meter and Instrument Factory and the No. 3403 Military Factory, "*Yige Zai Jiuye Dianxing de Heimu* (The Inside Story of Lin's Company)."

on average, or more than a year's salary each. When was interviewed a worker said: "Some people invested willingly. Others did not think it was a good idea. But in the end, we all handed over the money… If we did not give them the money, we would lose our jobs." The workers of the factory were promised high annual dividends and new rights as shareholders; but over the next five years, they received only one dividend payment and were never invited to shareholders' meetings. In November 2001, suddenly, the managers announced that the factory was transferred to their hands through a "fake bankruptcy," in which corrupt managers hid factory's assets, declared bankruptcy and then purchased the firm at a reduced price with questionable funds. Without getting any compensation for their investment, the workers felt that they became victims, thus attended protests.[179]

In China, because the central government did not set up rules of employee shareholding for different areas and industries, another problem in terms of employee shareholding in the monopolized public energy supply industry appeared, as such employee owned companies expanded quickly by utilizing its monopoly advantages and provided a great potential of profit for their employee owners; particularly, once the companies were approved for listing on stock market, their stock prices could increase rapidly and the employee stockholders may make large amount of money by selling their shares bought at a low price for insiders. The central government realized in 2003 that the employee shareholding of the companies could become a way of privately benefiting from the valuable assets of the monopolized industries. It thus stepped in to intervene by ordering

[179] Philip P. Pan, "High Tide of Labor Unrest in China: Striking Workers Risk Arrest to Protest Pay Cuts, Corruption", Washington, DC, *The Washington Post*, Jan. 21, 2002, p.A01.

that all employee shareholders must sell their shares back to the companies.[180] In the cases the author collected, three employee shareholding companies in the power supply industry had to suspend their practices of employee shareholding.

In Guizhou province, the Jinyuan Company was established in 2000 when more than 20,000 employees of electricity supply companies in the province invested 120 million and established the employee shareholding company. The company utilized its insider relations in the state monopolized power supply industry of the province, obtained eleven new power plant projects with the financial support of local branches of state banks, and at the end of 2003 its total assts increased to fifteen billion.[181] In 2005 28,762 managers and workers in the industry controlled 97 percent of the shares of the company.[182] From 2006 to 2008, the company completed power supply projects with investment of 21 billion. In Mar. 2008, the central government issued a document and requested that all employee shareholders in power supply industry must sell out their shares within a year. On Sept. 1, 2008, the CEO of the Jinyuan Group was detained by an investigation group of the central government for "embezzling SOE assets."[183]

In Shandong province, the Lu Energy Group was established in 1995 as a small company to develop services for the power supply industry of the province, with only five employees. In 1998,

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[180] Luo Wensheng, Wang Xiaolin, and Li Qiyan, "*'Jinyuan Diguo' Qiang Zhendang* (The Strong Shock to the 'Jinyuan Kingdom')," *Caijing* (the Finance and Economy Magazine), No.19, Sept. 15, 2008, 122-124.

[181] Tang Zheng, "*Dianli 'Jinyuan Diguo' Diaocha* (The Investigation of the Electric 'Jinyuan Kingdom')," *Caijing* (the Finance and Economy Magazine), No.17, Sept. 6, 2004.

[182] Li Qiyan, "*Dianli Zhigong Chigu Guifan Chutai Shimo* (Behind the Issued Regulation about Employee Shareholding in Power Supply Industry)," *Caijing* (the Finance and Economy Magazine), No.7, Mar. 31, 2008, 105.

[183] Luo Wensheng, Wang Xiaolin, and Li Qiyan, "*'Jinyuan Diguo' Qiang Zhendang* (The Strong Shock to the 'Jinyuan Kingdom')."

the company absorbed employees' investment, and the shares held by employees increased to 26 percent, while the provincial power supply SOEs held 57 percent of its 2.6 billion assets. At the end of 2002, through collecting investment from employees of the industry of the province, the company became a full employee shareholding company which controlled 36 billion state-owned assets of the industry. Under the pressure of the central government, from 2006 to 2008, the employee shareholders involuntarily sold out all their shares back to the company.[184]

The Yinglite Company in Ningxia Autonomous Region was another case of employee shareholding in power supply industry. It was originally a small collectively owned company; in 2000 the company was restructured to a full employee shareholding company, while each employee of the industry in the Region was forced to invest several thousand yuan, and the employee shares were under the custody of the official labor unions of the industry. In 2002, arranged by the local government, the Yinglite Company took over a part of the state-owned power plant and the Minzu Industrial Group, a manufacturing company that produced chemical products. By providing cheap electricity to the chemical company, the Yinglite Company gained a good profit from the chemical company, and became the top ten enterprises in the Region within years. In 2003, encouraged by managers, the employee shareholders of the company increased their investment voluntarily. From 2003 to 2004, the dividend rate for the employee

[184] Li Qiyan, and Wang Xiaobin, "*Shui de Lu Neng* (Who's Lu Energy)," *Caijing* (the Finance and Economy Magazine), *Finance and Economy,* No.1, Jan. 8, 2007.

shareholders was as high as 12 percent.[185] After 2008, the employee shareholders were also requested to sell out their shares to the company.

A hot debate about the employee shareholding in the power supply industry and whether it should be suspended lasted from 2003 to 2008 in China. An official of the central government said that the employee shareholding companies in the industry benefited from their close relations with the provincial power supply administrations, and could have exclusive advantages from project approval, project financing to power plant construction, thus was able to expand so quickly.[186] Moreover, the employee shares of the companies were usually under the control of managers or labor union officials, whereas employee shareholders could hardly exercise their rights as owners; sometimes, "the employee shareholding was simply an instrument to cover actual managers' privatization."[187]

Finally, in 2008 the SASAC issued a regulation, "The Suggestions for Regulating Employee Shareholding and Investment in SOEs." According to it, employees of small- and medium-sized SOEs could voluntarily restructure their enterprises through employee shareholding, but managers of the enterprises are prohibited from organizing employee investment; and large SOEs can not sell

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[185] Shi Dong, "*Shili Pai Yingteli de Fazhan Guiji* (The Development of Yinglite: How could a Small Company Save a High Energy Consumption Large Company)," *Caijing* (the Finance and Economy Magazine), No. 17, Sept. 6, 2004.

[186] Wang Xiaobing, and Shi Dong, "*Jingti Dianli Longduan Quan Bianxiang Siyou Hua: Dianli Xitong Zhigong Chigu shi Dianli Gaige zhong de Yige Lujing Shiwu* (Being Alerted by the Privatization of the Monopolized Power of Electricity Supply: Employee Shareholding Is the Wrong Path for the Reform of Power Supply", *Caijing* (the Finance and Economy Magazine), No.17, Sept. 6, 2004.

[187] Li Qiyan, "*Zhigong Chigu Xingui Bimian 'Zuihuai Siyou Hua'* (The New Regulation about Employee Shareholding Avoids the 'Worst Privatization')," *Caijing* (the Finance and Economy Magazine), No.13, June 23, 2008.

its shares to employees.[188] Since the regulation was issued, new practices of employee shareholding were rarely reported in China. Actually, the privatization of most small- and medium-sized SOEs had already been done in China years ago, so the items in the regulation regarding the employee shareholding in the small- and medium-sized SOEs are simply a belated action. If it had been issued ten years ago, a lot of problems in China's employee shareholding would have been avoided.

4. Privatization by Outsiders

Besides insider's privatization (MBO and employee shareholding), SOEs in China were also privatized by outsiders. Western economists have long believed that outsider's privatization is better than insider's privatization. There were two possible groups of outside private purchasers in China's SOE privatization: domestic individuals or private companies, and foreign investors including the businessmen from Hong Kong and Taiwan. Foreign direct investment (FDI) has contributed a great deal to China's economic development during the past three decades. In existing literature about China's privatization, the roles of foreign and domestic investors have rarely been explored. In this section the author will analyze three different outside investors: foreign investors, domestic private purchasers of SOEs, and individual buyers of the stocks of listed SOEs.

[188] Ibid.

4.1 The Role of FDI: The More FDI, the Greater is Its Privatization Effect?

Foreign direct investment (FDI) has contributed a great deal to China's economic development during the past three decades. China's official statistics show that from 1979 to 2008 the total amount of FDI in China was 853 billion USD.[189] Many outside observers may think that the huge amount of FDI inflow would largely help China's privatization; but, rarely have they tried to identify the privatization effects of different FDI projects in China. In China foreign investors in industrial fields may have two basic options, greenfield investment[190] or merger and acquisition (M&A); and the results of the two investment approaches could either be a joint-venture with Chinese partner or a firm wholly owned by foreign investors. So there could be four different FDI projects and their privatization effects are different (see Table 8-4). Greenfield investment aiming at establishing a wholly foreign-owned new company has nothing to do with privatization; joint-venture projects with SOEs through greenfield investment or M&A could partially privatize the SOEs; and acquiring an SOE and transferring it to a wholly foreign-owned enterprise would fully privatize the SOE. In previous literature about privatization in China, the privatization effects of different FDI projects have never been discussed or analyzed. Without a clarification in terms of the issue, the privatization effects of FDI in China might be exaggerated.

[189] China's State Statistics Bureau, *Zhongguo Tongji Nianjian 2009* (China Statistical Yearbook 2009), Beijing, China, China Statistical Publishing House, 2009, 745.

[190] Greenfield investment is a form of FDI where a parent company starts a new venture in a foreign country by constructing new operational facilities from the ground up.

Table 8-4 Privatization Effect of FDI

Privatization Effect		Investment Approach	
		Greenfield Investment	Merger & Acquisition
Ownership Structure	Joint-venture	Partial Privatization	Partial Privatization
	Wholly Foreign-owned	No Privatization Effect	Full Privatization

Greenfield investment is attractive to foreign investors who would like to avoid inheriting legacy issues and historical liabilities of M&A, whereas for those who are interested in China's domestic market M&A could bring about established sales and distribution networks.[191] M&A is usually applied to larger SOEs, because Chinese private industrial enterprises were usually quite new and small, with only little advantages in technology, human capital and sales networking; thus, foreign investors would more likely look for SOEs as their targets. From the point of view of China's development, greenfield investment projects could create new production capacity and employment opportunities, thus are helpful for economic growth. M&A through equity injection or buyout would input financial resources and technology to China's existing enterprises, but, probably, at the cost of laying off some employees or shutting down some workshops. Therefore, M&A might encounter labor protests, whereas greenfield investment is usually welcomed without resistance if no pollution issues incurred.

[191] Renu Prasad, "China FDI: A Two-way Street?" Australia, *Australian Legal Business*, June 30, 2009 .

Before China initiated its nationwide privatization, acquiring an SOE was politically and ideologically more controversial than developing a joint-venture;[192] therefore, 79 percent of foreign related enterprises in China were joint-ventures in 1995. After 1997, it seemed to be reasonable to assume that foreign investors would be more active than before in acquiring industrial SOEs, as the *gaizhi* policy and China's responses to the requests of WTO removed a lot of institutional barriers for foreign investors. However, the survey data of Garnaut et al. showed that the percentage of the shares of *gaizhi* firms owned by foreign companies declined from ten in 1995 to three in 2001.[193]

What kind of role did foreign investors really play in China's privatization? In order to find out an answer to the question, one has to identify the four different FDI projects in China. However, statistics of the four types of FDI are not available in China. When publishes statistics yearbooks, China's State Bureau of Statistics does not identify the investment approaches of FDI, but provided the data of ownership structure of foreign-related industrial enterprises (joint-venture and wholly foreign-owned) for several years. Analyzed the data, the author found that, after the nationwide privatization started in 1997, the percentage of joint-venture projects in FDI dropped significantly from 61 in 1999 to 21 in 2008, and joint-venture industrial enterprises decreased from 39,350 in 1995 to 30,279 in 2008, while the new FDI for joint-venture projects maintained a level of sixteen to nineteen billion USD each year from 2006 to 2008 (see Table 8-5).

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[192] Ma Shu-yun, "Foreign Participation in China's Privatization," London, UK, *Communist Economies and Economic Transformation*, Vol.8, No.4, 1996, 539.

[193] Ross Garnaut, et al. *China's Ownership Transformation: Process, Outcomes, Prospects*, 117-118.

Table 8-5 FDI and Foreign Related Industrial Enterprises in China

FDI and Foreign Related Enterprises	1995	1997	1999	2002	2006	2007	2008
Total FDI (Million USD)	37,521	45,257	40,319	52,743	63,021	74,768	92,395
of which: for Manufacturing	N.A.	28,120	22,603	36,800		40,865	49,895
of which: from Industrialized Societies and Other Countries	16,782	21,086	20,105	25,145	24,933	22,130	25,124
from Hong Kong	20,185	21,551	16,363	17,861	20,233	27,703	41,036
from Small Territories/Islands	554	2,620	3,851	9,737	17,855	24,935	26,235
FDI for Joint-Venture Enterprises (Million USD)			24,482	20,322	16,318	17,012	19,221
FDI for Wholly Foreign-Owned Firms (Million USD)			15,837	32,422	46,703	57,756	73,174
Total Foreign Related Industrial Enterprises	49,559	42,881			60,872	67,456	77,847
Number of Equity and Contractual Joint Ventures	39,350	31,580			26,604	28,622	30,279
Investment from Hong Kong and Taiwan	22,424	16,750			11,849	12,600	12,701
Investment of Other Countries	16,926	14,830			14,755	16,022	17,578
Number of Wholly Foreign-owned Enterprises	10,209	11,301			34,268	38,834	47,568
Owned by Hong Kong and Taiwanese Companies	6,945	6,270			17,332	19,349	22,877
Owned by Companies Based in Other Places	3,264	5,031			16,936	19,485	24,691

Source: The State Statistics Bureau of China, *Zhongguo Tongji Nianjian 1996* (China Statistical Yearbook 1996), 424, 598-599; *Zhongguo Tongji Nianjian 1998* (China Statistical Yearbook 1998), 456, 639-641, 646; *Zhongguo Tongji Nianjian 2000* (China Statistical Yearbook 2000), 604-608, 610; *Zhongguo Tongji Nianjian 2003* (China Statistical Yearbook 2003), 671-674; *Zhongguo Tongji Nianjian 2007* (China Statistical Yearbook 2007), CD Version; *Zhongguo Tongji Nianjian 2008* (China Statistical Yearbook 2008), 485, 730-733; *Zhongguo Tongji Nianjian 2009* (China Statistical Yearbook 2009), 487, 745-749. Beijing, China, China Statistical Publishing House, 1996, 1998, 2000, 2003, 2007, 2008 and 2009. When official data were not available, cells in the table are empty.

Note: Foreign owned LLSCs are included in the wholly foreign-owned enterprises. The fifth row from the top shows the FDI from the following small territories and islands, the British Virgin Islands, Cayman Islands, Samoa, Mauritius, Barbados, Macao, Bermuda, Bahamas, Brunei, and Marshall Islands.

Compared the numbers of the joint-venture enterprises established by Western companies and that by the companies based in Hong Kong and Taiwan, the author found that the former increased from 16,926 in 1995 to 17,578 in 2008, a slight growth of 50 per year, but the latter decreased from 22,424 in 1995 to 12,701 in 2008, down by 43 percent. On the other hand, the wholly foreign-owned enterprises rapidly increased from 10,209 in 1995 to 47,568 in 2008 (see Table 8-5). Obviously, after privatization was push forward in 1997, rather than establishing more and more joint-venture enterprises, foreign investors input more capital to their existing joint-venture projects and established many new wholly foreign-owned enterprises in China.

In global figure, from 1996 to 2005 about 70 percent of FDI was cross-border M&A, and greenfield investment accounted for 30 percent only.[194] However, in China the portion of M&A in FDI had never been more than seven percent during the period from 1996 to 2003; it rose to fourteen percent in 2005 but fell to three percent again in 2010 (see Table 8-6).. The increase of the cross-border M&A investment from 2004 to 2008 was mainly the results of some large cross-border M&A activities in China's finance sector by the banks of industrialized countries;[195]

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[194] Li Yong, "*Kuaguo Binggou Zai Hua Tedian ji Woguo de Yingdui Celue* (The Features of the Cross-Boarder M&A in China and the Strategies of Our Country)," Wuhan, China, *Hubei Jingji Xueyuan Xuebao, Renwen Shehui Kexue Ban* (The Journal of Hubei Institute of Economics, the Humanity and Social Science Version), Vol.4, No.6, 2007, 57.

[195] In 2004 and 2005, the M&A FDI in China involved about 10 billion USD. See Economist Intelligence Unit of *The Economist*, "The Great Buyout: M&A in China," Whitepaper of the Economist Intelligence Unit, London, UK, May 2006, p.6 (http://www.eiu.com/site_info.asp?info_name=eiu_The_great_buy_out_MnA_in_China). From 2001 to 2008, there were about 39 cases of M&A in China's finance sector, and 23 cases occurred during the period from 2005 to 2007, see Chen Deqiang, "Inspect on China's Banking Industry Reform in the Past Decade: From the Perspectives of Foreign Strategic Investors," Beijing, China, *Dangdai Jinrongjia* (Financier Today), May 14, 2009.

and the amount of the cross-border M&A in China's industrial enterprises remained quite small from 1996 to 2010.

Table 8-6 M&A in FDI

Year	FDI in China (Billion in USD)	of which: M&A (Billion in USD)	%
1996	41.7	1.9	4
1997	45.3	1.9	4
1998	45.5	0.8	2
1999	40.3	2.4	6
2000	40.7	2.2	6
2001	46.9	2.3	5
2002	52.7	2.1	4
2003	53.5	3.8	7
2004	60.6	6.8	11
2005	60.4	8.3	14
2008	92.4	13.0	14
2010	105.7	3.2	3

Source: The percentages from 1996 to 2005 were cited from Li Yong, "*Kuaguo Binggou Zai Hua Tedian ji Woguo de Yingdui Celue* (The Features of the Cross-Boarder M&A in China and the Strategies of Our Country)," Wuhan, China, *Hubei Jingji Xueyuan Xuebao, Renwen Shehui Kexue Ban* (The Journal of Hubei Institute of Economics, the Humanity and Social Science Version), Vol.4, No.6, 2007, 57; the percentage for 2008 was cited from Zhang Jinqing, and Wu Youhong, "*Waizi Binggou dui Woguo Jingji Anquan de Qianzai Weixie Fenxi* (The Analysis of Potential Threats of Foreign M&A to China's Economic Security)," Shanghai, China, *Fudan Xuebao* (The Academic Journal of Fudan University), No.2, 2010; and the data for 2010 was cited from the official 2010 statistics bulletin posted by China's State Statistics Bureau on Feb. 28, 2011 (www.stats.gov.cn/tjgb/ndtjgb/qgndtjgb/t20110228_402705692), and a news report, "*Shangwubu La Qi Waizi Binggou 'Jingjie Xian'* (The Commerce Ministry Began to Regulate M&A)," Apr. 13, 2011 (http://www.cnpre.com/search/news/index.php?modules=show&id=26341).

Why was more than 90 percent of FDI in China greenfield investment, and why more and more foreign investors aimed at establishing wholly foreign-owned companies? If one analyzes

from which countries China's FDI come, he might find some clues to answer the two questions. The amount of FDI from industrialized societies to China was relatively stable between 21 to 25 billions per year from 1997 to 2008; the most striking portion of the increasing FDI from 2002 to 2008 was from Hong Kong and Macau, and nine small territories and islands, i.e. the British Virgin Islands, Cayman Islands, Samoan, Mauritius, Barbados, Bermuda, Bahamas, Brunei, and Marshall Islands. In 2008 the amount from the nine small territories and islands was even larger than that from all industrial countries (see Table 8-5). The unique FDI from the small territories and islands was related to the activities of the round-tripping FDI; it had caused the attention of Chinese government and scholars.[196] The round-tripping FDI is actually a part of China's capital flight;[197] it has got around China's regulations and gone abroad, then returned under the name of foreign companies registered at Hong Kong, the offshore financial and business centers such as the British Virgin Islands, Cayman Islands and Samoan, and other places where government

[196] Li Xing, "*Yi Zi E Jing You San Cheng 'Jia Waizi'* (In China's FDI Thirty Percent was Phony Foreign Investment)," Beijing, China, *Xinhua Meiri Wenzhai* (The Xinhua Daily Digests), Dec. 9, 2005 (http://www.gmw.cn/01wzb/2005-12/15/content_346240.htm); "*'Jia Waizi' Da Xing Qi Dao, Si Buwei Lianshou 'Waizi Dajia'* (Phony FDI was Too Active, and Four Ministries Began to Restrain it)," *Zhongguo Jingying Bao* (China's Management News) *(Zhongguo Jingying bao)*, June 10, 2006; Jiang Ziye, "*Jia Waizi Yuan He Ji Chu Zhen Waizi* (Why was Real FDI Replaced by Phony FDI)?" Beijing, China, *Zhongguo Jinrong* (Finance in China), No.1, 2010.

[197] Mei Xinyu, "*Zhongguo yu Li An Jinrong Zhongxin Kua Jing Ziben Liudong Wenti Yanjiu* (Research on the Cross-Border Capital Movement Between China and the Off-Shore Financial Centers," a Research Report of the Ministry of Commerce, Beijing, China, Aug. 18, 2004 (http://caitec.mofcom.gov.cn/aarticle/bw/200408/20040800265731.html); Nan Yan, and Wang Yongfu, "*Meiti Jie Zhongguo Qiye Li An Mi Shi, Kaiman Qundao Cheng Bishui Tiantang* (Media Revealed the Secret Off-Shore History of Chinese Enterprises: Cayman Islands Became the Paradise for Tax Evasion," Beijing, China, *Zhongguo Jingji Zhoukan* (China Economic Weekly), No.30, Aug. 1, 2011.

regulations on business are loose.[198] Such activities were often motivated by the needs of corrupt officials and SOE managers for money laundry and by the benefits of tax advantages available for foreign companies in China. It is worth noting that many of the round-tripping capital owners are mainland Chinese, and they know very well that there exist risks if they use the capital to develop joint-venture with SOEs or arrange M&A, because their SOE partners would easily find out the phony FDI and the real identity of the foreign investors, even the sources of their wealth. It is thus understandable why the rapidly increasing round-tripping FDI was often not put into M&A or joint-venture business; instead, these investors more preferred the wholly owned greenfield investment projects which did not need the maintenance of close relations with Chinese business partners in company management.

In order to identify the amounts of the four types of FDI projects, we must know how cross-border M&A investment was divided between joint-venture and wholly foreign-owned projects and how greenfield investment was divided between them. As the total amount of the cross-border M&A investment was quite small, and the percentage of the joint-venture investment for M&A does not much affect the percentages of the two types of greenfield investment projects, the author might estimate the figures of the greenfield projects by assuming that the cross-border M&A investment was equally divided between joint-venture projects and wholly foreign-owned projects. The estimated results are quite interesting: in 1999, about 38 percent of China's total FDI was wholly foreign-owned greenfield investment projects that had

[198] Geng Xiao, "Round-Tripping Foreign Direct Investment in the People's Republic of China: Scale, Causes and Implications," Hong Kong, China, *The Asian Development Bank Institute Discussion Paper*, No.7, June 2004.

no privatization effects, and the percentage increased to 60 in 2002 and 72 in 2008 (see Table 8-7).

After China started its nationwide privatization in 1997, many foreign investors put a large portion of FDI into greenfield investment projects wholly owned by foreign companies, and did not play any role in the privatization of industrial SOEs. In other words, when the round-tripping FDI was dramatically expanded after 1997, the privatization effects of rapidly increasing FDI actually kept reducing in China. Since the cross-border M&A investment for wholly acquiring industrial SOEs was so small, one may conclude that, when industrial SOEs were taken over by outsiders of the enterprises, the purchasers were more likely domestic companies or individuals, rather than foreign investors.

In contrast to other transition countries, FDI inflow to China has been large enough. If the 853 billion USD of FDI from 1979 to 2008 was divided by 80 thousand of the privatized industrial SOEs, in average there seems to be 10 million USD available for each SOE. However, the actual privatization effect of FDI in China has not been as large as the total amount of FDI suggests. In 1999, about 62 percent of FDI had partial privatization effects in China (most cases were joint-venture investment, whereas the cross-border M&A investment for full privatization of SOEs was very small); but in 2008, only 28 percent of FDI had such effects. China has made various efforts to absorb foreign investment as much as possible, but FDI did not contribute much for the nationwide privatization of industrial SOEs; in other words, domestic individuals or companies have been the main force to implement the privatization.

Table 8-7 Estimated Composition of FDI in China

Four FDI Projects	1999	2002	2008
Total FDI (Billion USD)	40	53	92
of which:			
Cross-border M&A Investment for Joint-Venture	0.5	0.55	6.5
Cross-border M&A Investment for Wholly Foreign-Owned Firms	0.5	0.55	6.5
Greenfield Investment for Joint-Ventures	24	20	13
Greenfield Investment for Wholly Foreign-Owned Firms	15	32	67
Percentage of the FDI that Had No Privatization Effects (the Greenfield Investment for Wholly Foreign-owned Firms in Total FDI, %)	38	60	72
Percentage of the FDI that Had Partial or Full Privatization Effects (%)	62	40	28

Source: The numbers in the table were calculated with the data in Table 8-5 and 8-6 and with an assumption that M&A investment was half put into join-venture projects and half to wholly-owned foreign enterprises.

4.2 Cases of Cross-Border M&A

One of the reasons why the cross-border M&A investment was so small is that most small and medium sized SOEs in China were poorly equipped, thus were not attractive to Western large M&A investors. China's large industrial SOEs could be objective of foreign M&A, but there had been a lot of barriers for foreign investors. Probably, only during the period from 1997 to 2006 when the cross-border M&A were not regulated by the Chinese central government, were foreign large investors able to find opportunities for the M&A of large SOEs in China. The author analyzed 22 cases of industrial SOEs that were partially or fully privatized by foreign investors through cross-border M&A.[199] Among them, fifteen were large SOEs and seven were small or medium

[199] The cases were collected from Anhui Province, Heilongjiang Province, Henan Province, Guangxi Autonomous Region, Jiangsu Province, Liaoning Province, Ningxia Autonomous Region, Shandong Province,

size SOEs; thirteen of the large SOEs were machine building enterprises. From the fifteen case materials the author came to understand better how foreign M&A of large industrial SOEs were carried out in China.[200]

In the fifteen cases of large SOEs, three were fully taken over by foreign investors (two by an American private equity company and one by a Singapore manufacturing company) in 2005 and 2006, and twelve large SOEs were transformed into joint venture companies with foreign investors. Of the twelve joint venture companies, two were established in 1994 and 1995, before China's nationwide privatization was pushed forward, and the other ten were all established from 1997 to 2007. Among the foreign partners of the twelve joint venture companies, nine were manufacturing companies from Germany, the U.S., France, Great Britain, Japan and Sweden, and some of them were well known in the world, and three were non-industrial companies. Actually, during the period from 1997 to 2006, many foreign companies went to China to look for large industrial SOEs as business partners, because, when foreign investors developed their business in China's industrial fields, joint venture project, particularly with China's large industrial SOEs, was the most common practice they preferred.

In China, most large industrial SOEs were directly controlled by ministries of the central government under the planned economy, a feature of the Soviet version of industrial

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and Shanghai Municipality.

[200] The fifteen enterprises were the Changzhou Transformer Manufactory, the Dalian Motor Manufacturing Plant, the Dalian Second Motor Manufacturing Plant, the Harbin No.1 Tool Manufacturing Corporation, the Jiamusi Combine Manufacturing Corporation, the Jiamusi Mining Machinery, the Jinxi Chemical Machinery, the Jixi Mining Machinery, the Northwest Bearing Manufactory, the Shandong Rizhao SSYMB Pulp and Paper, the Shanghai Tire and Rubber, the Shenyang Rock Drill Manufactory Plant, the Wuxi Weifu High-Tech Co., the Xuzhou Construction Machinery Group, and the Yulin General Diesel Engine Plant.

management. In the era of planned economy, often, each enterprise was established to produce a particular product, and was responsible to provide a quite large portion of the product for nationwide consumers. Because the large industrial SOEs were usually capital intensive with unique technologies and equipments, the marketization of China's economy from the 1980s to 1990s did not improve the market structure of their products, and newly established small- and medium-sized private industrial firms could hardly compete with the giants. It was exactly the dominance of the large industrial SOEs in domestic market that attracted foreign investors, and in most situations when foreign investors looked for business partners among the large industrial SOEs, their main purpose was to occupy China's domestic market as large as possible through sharing the sales network of their SOE partners of joint venture firms. In early 1990s, the control of most large industrial SOEs by industrial ministries of the central government was released to local governments. Therefore, when foreign investors went to China to seek for cooperation with the large industrial SOEs after 1997, they had to deal with local governments which controlled the enterprises through appointing CEOs of the SOEs, but were bothered by the increasing losses made by the large SOEs.

From the fifteen privatization cases of the large industrial SOEs, the author found that, from 1997 to 2005, the central government did not issued any rule to regulate the M&A of large industrial SOEs, and local governments played a very important role in such activities, even more important than that of SOE managers. Because the SOEs were quite large and, often, more than a billion assets would be privatized, CEOs of the SOEs had to get approval of local governments before and during their negotiations with foreign investors. Managers and workers

of the large industrial SOEs and local governments usually expressed different concerns during the negotiations with foreign investors, while managers worried about the survival of their enterprises and were in urgent need of foreign capital and technologies, workers mainly cared about their jobs, and local governments had great enthusiasm to welcome foreign investors and might easily compromise with foreign companies as successes in absorbing foreign investment and progresses in SOE *gaizhi* were two main indicators in evaluating the performance of majors and governors. If local governments had strong interest in M&A by foreign investor, very often, workers' voice was eventually silenced, and managers had to listen to the instructions of local officials regarding the terms of joint venture projects, even though the managers did not really agree.

For instance, the Harbin city government of Heilongjiang Province requested that, in order to develop real estates at the center of the city, most large industrial SOEs located in the center should be removed to suburb. For that purpose, the city government encouraged an American company, the Gleason Corporation, to develop a joint venture project with the Harbin First Tool Manufacturing Corporation, by providing favorable conditions to Gleason, such as only the best workshops of the factory would be put into the joint-venture company and Gleason was allowed to control 70 percent of shares with an investment of 8.7 million USD, although managers and workers of the enterprise disagreed.[201] In Huludao city of Liaoning Province, when the Siemens Corporation of Germany wanted to take over the turbo machinery branch of the Jinxi Chemical

[201] Yang Ming, "*Waizi Qing Qu Jinghua, Zai Zao Ha Yi Gong Ji Wu Keneng* (Foreign Investors Took the Best Part of an SOE, and Ha'erbin First Machinery Tools Factory Could No Longer be Restructured)," *Zhongguo Gongye Bao* (The China Industrial News), Dec. 19, 2005.

Machinery, the most competitive part of the SOE in China's market, managers and workers of the enterprise resisted the project; but the city government was interested in inviting a worldwide well-known foreign industrial corporation to the city, as an evidence of achievements in attracting FDI. As a result, the local government dominated the negotiation with Siemens, and asked the CEO of the enterprise to sign the joint-venture agreement which let Siemens control 70 percent of shares of the joint-venture company.[202] In the two cases, the real decision maker in the projects was actually not the CEO of SOEs but local officials.

During the 1980s and 1990s China's FDI policy was to "exchange for foreign technologies with domestic market shares."[203] The policy encouraged Chinese industrial enterprises to request their foreign partners to transfer technologies if the foreign investors wanted to access to China's market. Not only did the Chinese partners of the joint-venture companies benefit from foreign technology transfers, other Chinese enterprises might also share the transferred technologies, as intellectual property rights were not really protected in China. However, after China joined WTO in November 2001, the policy was gradually shaken because WTO regulated that pressure to foreign companies for technology transfer should be removed. For foreign investors, joint-venture projects might be the most convenient way to establish their business in China; but, they would benefit more and feel safer about their technologies if they could hold dominant

[202] Jia Cundou, "*Jinxi Hua Ji Nian Yu Nian Zaishu, Ximenzi Yizhao Zhaiguo* (The Jinxi Chemical Machinery Planted the Tree for Twenty Years, but Siemens Took the Fruits)," *Zhongguo Gongye Bao* (China Industrial News), Sept. 19, 2005.

[203] Chen Man, and Yue Jianyong, "*Yi Shichang Huan Jishu? Zhongguo Xiyin Waizi Celue Fenxi* (Exchanging Technology for Market Share? An Analysis of China's Strategy in Absorbing FDI)," Princeton, NJ, *Dangdai Zhongguo Yanjiu* (Modern China Studies), No.4, 2002, 93-100.

shares in their joint-venture companies in China. Therefore, many of them have finally taken over their joint-venture firms by increasing their shares steadily. For example, in twelve M&A cases of large industrial SOEs, four joint-venture projects were transformed by foreign investors into fully foreign-owned companies within several years[204] (one joint-venture company was taken over by an SOE company[205]).

But, from 2005 to 2006, controversies regarding foreign M&A emerged in China, when technocrats at the central administration and some reporters raised the question if foreign M&A of large industrial SOEs would threaten China's economic security. Their argument was that a lot of foreign M&A targeted the strategically important SOEs in China's critical industrial sectors, and foreign control over the enterprises would weaken China's economic independence. The M&A case of the Xuzhou Construction Machinery Group led the controversy to the highest point and the negotiation between the SOE and the Carlyle Group, an American personal equity investment company, had lasted two years. After many people participated in a debate about the case in media and on the internet, in July of 2006 China's Commerce Ministry called all related parties of the case to Beijing for inquiries. Three weeks later, the Chinese government issued a new rule to regulate foreign M&A in China. The Carlyle Group finally got its deal in March 2007, but obtained less shares (decreased from the previously planned 85 percent to 45 percent in the final

[204] The four enterprises were the Dalian Motor Manufacturing Plant fully taken over by the Western Electric of Singapore, the Dalian Second Motor Manufacturing Plant fully taken over by the Brook Crompton Motor Group of the Great Britain, the Jiamusi Combine Manufacturing Corporation fully taken over by the John Deere of the United States, and the Northwest Bearing Manufactory fully taken over by Siemens.

[205] The joint-venture company of Changzhou Transformer and the Toshiba Corporation of Japan was established in 1995 and was taken over by China's state-owned Western Electricity Group in 2006.

draft of their contract) at a higher price than that in the earlier contract.[206] Since then, foreign M&A of large industrial SOEs has seemingly become less active in China, and its privatization effects in *gaizhi* of large SOEs has remained small. For example, in 2006 a large Germany bearing company, the Schaeffler Group, tried to fully take over the Luoyang Berearing Plant, a large bearing production enterprise located in Henan Province, with an investment more than 200 million USD.[207] After the regulation about foreign M&A was issued, an investigation group from the State Council was sent to the SOE, and finally the negotiation with the Schaeffler Group was ceased.[208]

Most cross-border M&A cases in China referred to medium- and small-sized SOEs. In such cases, particularly those done by the businessmen from Taiwan or other countries, the author found that the identity of some foreign investors were questionable, and in some cases the real purpose of foreign M&A activities was not to restructure the SOEs for long-term industrial production, but for profiting through selling the land, equipment and inventory of the SOEs. For instance, in 2005 the International Industries Corporation registered by a Chinese American in the U.S. took over a medium sized SOE, the Wuhan Machine Tool Plant of Hubei Province; later, the identity of the foreign company and the acquisition process were found questionable.[209]

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[206] Ma Tao, "*Kailei Shougou Xu Gong An Xiemu, Duidai Waizi Zouxiang Lixing* (The M&A Case of the Xuzhou Construction Machinery by the Carlyle Group was Done, the Attitudes towards Foreign Investment Became Rational)," *Nanfang Zhoumo* (The Southern Weekend), Mar. 22, 2007.

[207] Yang Hao, "*Zhongguo Zhou Xie Ji Shangshu Fandui, Zu Waizi 11 Yi Gou Luo Zhou* (The China's Bearing Association Urgently Sent a Report to the Central Government to Oppose the Foreign M&A of the Luoyang Breaing," *Zhongguo Gongye Bao* (The China Industrial News), July 6, 2006.

[208] Ji Yafei, "*Luo Zhou Jituan Binggou yu Chongzu Wenti Yanjiu* (A Study on the M&A of the Luoyang Bearing Group)," MBA Thesis, Dept of MBA, Chengdu University of Electronics Science and Technology, Chengdu, China, June 2009.

[209] Zhang Xiangdong, "*Wuhan Jichuang Chang Xiju Xing Gaizhi Zaoyu Kuajing Diaocha* (The Cross-Border

In Luohe city of Henan Province, a Taiwanese businessman, Xiao Wande, took over three SOEs. The Luohe Pharmaceutical Factory, one of the 500 largest pharmaceutical enterprises in China, was sold by local government to him. The factory had 100 million yuan sales and ten million profit per year. Xiao took over the debt of the factory in amount of 53 million in exchange of the whole assets of the factory. The deal was made without letting the managers and workers of the factory known. After Xiao became the new owner, he paid only 400 thousand to the factory; then, with the help of local officials, he borrowed huge amount of loans on behalf of the firm from the local branches of state banks, and spent part of the loans to pay a small portion of the due debts, but put at least 27 million yuan into his pocket. The reason why local officials were so supportive and helpful to Xiao was that every time when the local banks lent to Xiao, Xiao paid the government and bank officials a portion equal to 20 to 30 percent of the approved loan as a bribe. In fact, Xiao did not really invest much to obtain the assets of the factory; instead, he used the loans to pay part of the debts, but left the privatized firm more new debts; thus, the factory was actually privatized through a way like a gift giving to him, and from the deal Xiao grabbed at least 50 million yuan. In 1999 the factory encountered serious difficulties and stopped production, and the foreign owner disappeared.

In the same city, Xiao took over in 1996 another SOE, the Luohe Second Knitting Factory, through similar approach. According to the M&A contract he was supposed to pay 48 million yuan debt within three years in exchange of the ownership of the enterprise. Xiao paid only 300

Investigation of the *Gaizhi* at the Wuhan Machine Tool Plant," *Jingji Guancha Bao* (Economic Observation News), Oct. 21, 2007.

thousand, but obtained the control of the enterprise. After became the new owner, he sold out seven machines, more than ten trucks and part of the buildings of the firm. Totally he received six million yuan from the sales, all into his pocket. The city government never asked him to pay rest of the debts. Most of workers were dismissed, and Xiao was gone. He also took over the Weishida Shoes Factory in the city, and sold out most of equipment for cash and run away.

After privatization the three SOEs, the Taiwanese businessman had no any interest in managing them; instead, he simply sold the assets of the enterprises as much as possible, and left the firms as empty shells. Ultimately, the first enterprise was given to another businessman by the city government; the third firm was finally closed; and at the second firm, after workers kept appealing, the enterprises was taken back by the city government thus retransformed into an SOE, though it had only empty buildings left.[210]

It must be mentioned that joint-venture projects would leave a lot of unsolved issues for local governments. When foreign investors acquired a part of assets of small- and medium sized SOEs for joint-venture projects, these SOEs often could hardly survive upon the remaining assets or equipments. A lot of foreign investors financed a transfer of ownership of exiting assets of the poorly managed SOEs, and their Chinese SOE collaborators often became corporate "shells," obtaining income from dividend payoffs proportionate to their ownership shares but did not participating operation and management of the joint-venture enterprises.[211]

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[210] Shi Po, "*'Cheng Mai Guang' Mai Chu Eguo Leilei* ('Cheng All Sell-off' Involved Pernicious Consequences)," *Nanfeng Chuang* (The Window for Wind from South), March 1 -15, 2002, 21-23.

[211] Huang Yasheng, *Selling China: Foreign Direct Investment during the Reform Era*, 253.

4.3 The Practices of Domestic Purchasers of SOEs

China had initiated economic liberalization in the late 1970s, about 20 years earlier than the start of the nationwide privatization. Could the rapidly growing private companies in China greatly help implementation of SOEs' privatization? Domestic private companies are operated in industrial and non-industrial sectors, and those in the latter sectors were not the best purchasers as they did not have experiences in industrial management. In 1997, there were 99 thousand of industrial SOEs and 34 thousand of private industrial enterprises, and the average employees of the former was 404 and that of the latter was 100.[212] The figures suggest that the total number of the industrial SOEs in 1997 was about three times of that of the private industrial enterprises, and the average employee of the former was four times of that of the latter. Obviously, it is impossible in China to find sufficient domestic private industrial companies to take over the industrial SOEs, given that the physical, financial and human capital of the private industrial enterprises were much smaller than that of the SOEs. Moreover, many SOEs were loss makers and were of little attractions to private industrial businessmen. As the number and size of private industrial firms were much smaller than that of SOEs in China, the domestic outside buyers might often not be private industrial companies; instead, they could be individuals who did not own and operate industrial firms before they stepped into the takeover process, and their interest in the privatization might not be restructuring the privatized

[212] In Table 13-1 of *China Statistical Yearbook 1998*, "Number of Industrial Enterprises and Gross Industrial Output Value by Ownership," an item "Enterprises of Other Types of Ownership" covers the number of foreign funded enterprises and that of domestic private enterprises, and its total amount is 77 thousand. After deducted the number of foreign funded enterprises (43 thousand) from the 77 thousand, the author got the number of private industrial enterprises, 34 thousand, and calculated the average employees of the private industrial enterprises in 1997. See *China Statistical Yearbook 1998*, compiled by China's State Bureau of Statistics, Beijing, China, China Statistical Publishing House, 1998, 142, 431, 432 and 444.

SOEs, but something else such as selling the land of SOEs for cash.

Privatization policies in China varied among provinces and cities. Some local governments, for example, the municipality government of Shanghai, were cautious and expressed their concerns with the rights of workers, thus more emphasized employee shareholding rather than selling off SOEs to outsiders. In Shanghai, the total number of publicly owned small enterprises (including non-industrial enterprises) in 1999 was 100 thousand; after the municipality government implemented the policy of "letting small go within three years" declared by the central government in 1997, the number in 2001 was only reduced to 99 thousand, one thousand less than in 1999. In the investment to the small enterprises in 2001, the portion from individual investors was only 15 percent and that from foreign investors was 21 percent; at the end of 2001, 70 percent of the capital of the small publicly owned enterprises in Shanghai was still in the hand of the state.[213] But, a lot of local governments were more reckless and had promoted selling-off policies. A typical case was found in Luohe city of Henan Province. The city government and the party secretary of the city, Cheng Sanchang, were well known in China for their brave "All Selling-off" policy of privatizing industrial SOEs. Cheng told a reporter that he opposed to the privatization approach through employee shareholding and insisted on selling SOEs off to private companies that were capable to buy and manage the firms to be privatized. His idea was once considered by the provincial and central government great ambitions to make a break through for SOE reform, and

[213] *Shanghai Xiao Qiye Fazhan Yanjiu Ketizu* (The Research Group about the Development of Small Enterprises in Shanghai), "*Shanghai Xiao Qiye Gaige he Fazhan Qingkuang Fenxi* (An Analysis of the Reform and Development of Small Enterprises in Shanghai)," *Shanghai Gaige* (Reform in Shanghai), No.7, 2002, 12-15.

he earned a reputation as the pioneer of SOE reform in China. About 90 percent of SOEs in the city were sold off, and he personally arranged selling 27 SOEs from 1996 to 1999.[214] Through the transactions Cheng accepted bribes from private businessmen and accumulated 12 million USD. Later the corrupt official fled China and has lived in a four-flour luxury house bought at Auckland of New Zealand since 2001.[215]

Garnaut, et al. pointed out: "In many cases of *gaizhi*, the local government is unable to cash in on the sale of state assets. Many SOEs already have negative net assets at the time of *gaizhi*. Many owe wages, social security payments, taxes, or health insurance premiums. These debts have to be settled before a firm is privatized."[216] It was reported in China that SOE managers often encountered six problems in *gaizhi* process. First, SOE assets could hardly be cashed to pay due debts; second, the managers could hardly find sufficient funds to pay unemployment subsidies and pensions; third, workers' medical expenditures could not be reimbursed; fourth, employees' investments to their enterprises could not be paid back; fifth, the laid-off workers could hardly get sufficient compensation; and sixth, workers' angry against managers for losing jobs and cut social security payments could hardly be calmed down.[217]

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[214] Shi Po, "*'Cheng Mai Guang' Mai Chu Eguo Leilei* ('Cheng All Sell-off' Involved Pernicious Consequences)," *Nanfeng Chuang* (The Window for Wind from South), March 1 -15, 2002, 21-23.

[215] Wei Hongqian, Wang Wentao, and Tan Qing, "*Sanren Shuji Xiangji Luoma, Luohe Zhentong* (The Pains of Luohe City: Three Successors as Party Secretary of the City were Accused of Corruption)," Beijing, China, *Fazhi Fangyuan* (The Rule of Law and Beyond), July 21, 2008. According to the report, in 2007 Cheng Sanchang began to write the inside story how he colluded with private businessmen when at the position of party secretary. But the author has not found the book.

[216] Ross Garnaut, et al. *China's Ownership Transformation: Process, Outcomes, Prospects*, 33-34.

[217] "*Qiye Gaige de Liu Da Kunnan Wenti* (Six Large Difficult Problems for Enterprise Reform)," *Zhongguo Gaige Bao* (China Reform News), May 7, 1997.

Therefore, for many SOE managers, their main concern in *gaizhi* was not to restructure enterprises, but simply a money issue, i.e. from where to get funds to pay the social security expenditures to their workers; thus, enterprise institution building through privatization was left aside. Many SOE managers were eager to find domestic purchasers of their enterprises, whom might bring urgently needed cash for the managers; on the other hand, in order to collect funds for the social security expenses, the SOE managers had no hesitation in selling equipment and other properties such as land or factory building. Consequently, in many SOEs privatization became a property cashing process for social security payments, and the productive capacity of the enterprises were so deteriorated and many SOEs were simply destroyed during privatization. It is no doubt that the policy of the central government to remove its fiscal obligations to the shoulders of SOE managers and workers was partly responsible for the negative consequences of the privatization in China.

What kind of role did the domestic purchasers play in the privatization of industrial SOEs? Existing literature on privatization in China usually focuses on the results of asset transactions, i.e. how many SOEs were privatized, but rarely analyzes social aspects of privatization process and answers the questions such as who the domestic purchasers were, how did they arrange asset transactions and for what purposes, and how did workers of the privatized enterprises responded to their activities. In order to understand their practices, the author collected 31 cases from 16 provinces and municipalities.[218] The 31 cases were analyzed from four dimensions: the identity of

[218] Among the 31 cases, one was collected from Anhui Province, two from Chongqing Municipality, two from Guangxi Autonomous Region, one from Hebei Province, one from Heilongjiang Province, three from Henan

the domestic purchasers, the transaction processes, their real purposes, and workers' responses to the privatizations.

In terms of the identity of private purchasers of SOEs, only in five cases the purchasers were private industrial enterprises; in fourteen cases the purchasers were non-industrial private companies or individuals; in nine cases purchasers' eligibility was questionable; and in three cases the real purchasers of SOEs were local officials or their family members. The last pattern was found in the following cases. The Hejiang Electric Plant in Luzhou city of Sichuan Province was sold to a private company whose real owner was the wife of the communist party secretary of the city in 2003;[219] in the same year, in Zaoyang city of Hubei Province, 36 SOEs were sold as a package to a deputy director of the local branch of the state-owned Construction Bank at 70 thousand USD, about two thousand USD per SOE in average;[220] and in Wuhu city of Anhui Province, ten million USD non-performing loans of seventeen enterprises were sold at a price of 600 thousand USD in 2005 to a small private company registered for the deal, owned by the Vice Chairman of the People's Congress (the parliament) of Wuhu County and managed by his younger brother.[221]

Province, two from Hubei Province, one from Hunan Province, three from Jiangsu Province, one from Jiangxi Province, two from Jilin Province, one from Qinhai Province, two from Shandong Province, three from Shanxi Province, four from Sichuan Province, and two from Zhejiang Province.

[219] "*Hejiang Dianli San Yi Duo Guoyou Zichan Jian Mai Jin Si Qian Wan, Fufu Lianshou, Zaojiu Xianwei Shuji Yi Wan Shenjia* (Hejiang Electric with More than 300 Million Assets was Sold Cheaply at 40 Million, and the Couple of the Party Secretary of the County Got Enriched)," Apr. 9, 2011.

[220] "*San Qian Duo Wan Yuan Guoyou Zichan Cai Mai le 60 Wan Yuan* (30 Million State Assets Sold at 600 Thousands)," *Jingji Cankao Bao* (Economic Information Daily), Oct. 16, 2006.

[221] Ge Rujiang, "*Anhui Wuhu 8000 Duo Wan Guoyou Zichan bei 550 Wan Jian Mai* (80 Million SOE Assets in Wuhu County of Anhui Province were Cheaply Sold at 5.5 Million)," *Jingji Cankao Bao* (Economic

Regarding the questionable eligibility of the purchasers, the author found identity fraud in several cases. For instance, in the Hainan Tibetan Autonomous Region of Qinhai Province, a businessman from Hainan Province presented a fake business registration of a non-existing private company and successfully obtained 80 percent of shares of the Qinhai Third Pharmaceutical Factory in 1999.[222] In Nanjing city of Jiangsu Province, the representative of the private Tianan Group of Zhejiang Province prepared a fake official stamp to make a fake official document about the investment input of the company; then obtained the control of a large SOE, the Nanjing Zhongshan Group, in 2003.[223] Also in Nanjing city, a former city government official registered a company at the British Virgin Islands,[224] then, as a "foreign investor," he successfully bought two SOEs, the Nanjing Instrument Factory and the Nanjing Machine Building Factory, in 2006 and 2007 by removing the two SOEs to suburb of the city and selling their land located in the center of the city, thus became a millionaire.[225] In Baoding city of Hebei province, the CEO of a large SOE, the Yi Textile Group, cheated the city government and the workers of the enterprise in 2004 that a Hong Kong based well-known investment group with

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Information Daily), Feb. 12, 2007.

[222] Ma Yingshan, "*Weizao Gongshang Zhizhao, Xu Tou Konggu Zijin, Pian Zhan Guoyou Zichan Fa Burong* (With Fake Business Registration, Obtained Control over an SOE by False Investment)," *Renmin Ribao* (The People's Daily), Nov. 10, 1999.

[223] Yang Guang, "*Nanjing Zhongshan Jituan Gaizhi bei Zhi Ju'e Guoyou Zichan Liushi, Shu Yi Guoyou Zichan Bian Wei 4% Guquan* (The *Gaizhi* of Zhongshan Group in Nanjing City was Accused, as Millions of SOE Assets Shrank to Four Percent)," *Xin Xiang Bao* (The New Xiang News), Mar. 5, 2009.

[224] In China, many businessmen and corrupt officials registered companies at the off-shore business centers through domestic agents; thus they became "foreign investors" without any personal foreign identity.

[225] "*Shougou Men: Pochan Laoban San Nian Cheng Yiwan Fuhao* (The SOE Sales: A Bankrupt Businessman Enriched with One Hundred Million Wealth within Three Years)," Dec. 23, 2010 (http://blog.cntv.cn/13778878-1484888.html).

strong financial capability would purchase the SOE, but actually the real purchaser was a shell company registered at the British Virgin Islands by her graduate schoolmate in an institute in Shanghai. The SOE was then privatized into the hands of the CEO and her friends, but the shell company did not invest any cent.[226] In 2003 the Yichang city government decided to sell the Yichang Water Company to a shell company registered in Beijing with very cheap price; when workers of the enterprise questioned the eligibility of the purchaser, the government sent police cars with siren on to threaten the workers.[227] In Guangxi Autonomous Region, after the Nanning Gourmet Powder Factory was sold to a company registered at Shenzhen of Guangdong Province in 2005, some workers of the factory found the identity of the purchaser suspicious and went to Shenzhen city and investigated the background of the purchaser. Finally they found that the purchaser was a shell company owned by several individuals with a fake document about its qualification.[228] In Shandong Province, the previously mentioned employee shareholding company, the Lu Energy, was secretly sold to two private companies that were unknown to the public at a price of 3.7 billion yuan in May 2006. After the transaction was done, the identity of the purchasers was questioned in media and the transaction was accused as an SOE asset stripping. In Feburary 2008 the SASAC decided to have the Lu Energy renationalized from the

[226] Wang Fangjie, "*Ling Chengben Man Tian Da Pian* (A Big Fraud Case at Zero Cost)," *Zhengquan Shichang Zhoukan* (The Stock Market Weekly), Dec. 13, 2010.

[227] Workers of the Yichang Water Company, "*Shu Shi Yi Guoyou Zichan bei Tunshi* (The Billions Asset Stripping at the Yichang Water Company)," Beijing, China, the Website of Water Industry, June 16, 2004 (http://bbs.shuigongye.com/showtopic-38494.html).

[228] Luo Wensheng, "*'Hehua Weijing' Tudi Zhengduo Zhan* (The Fight for the Land of 'the Lotus Gourmet Powder')," *Caijing* (The Finance and Economy Magazine), No.21, Oct. 15, 2007, 120-123.

private companies with a price of 8.3 billion yuan.[229] The cases of questionable eligibility implied that, on the one hand, there were some unqualified purchasers participating in the privatization of industrial SOEs; and, on the other hand, a lot of transactions of privatization might not be properly or legally processed.

Analyzed the transaction process of the 31 privatization cases, the author noticed that in six cases local governments ordered SOE managers to transfer the enterprises to designated private purchasers, in four cases the purchasers obtained control over the SOEs before they paid off the due amount for the takeover, in four cases fraud purchase was observed, in eleven cases the paid amount for SOE asset transaction was unclear, and only in six cases the transactions were done without problems.

As local governments actively participated in the decision making of SOE privatization, sometimes government officials directly decided to whom an SOE was sold and at what price, and ignored if SOE managers and workers agreed or not. In such forced privatizations by government officials, often, the arrangements made by the officials in the privatization schemes were questionable. For instance, in Yuncheng city of Shanxi Province, several government officials helped a private purchaser to obtain a state-owned mine at a very low price in 2003, and took bribe from him.[230] In Liangshan county of Shandong Province, officials of the county government

[229] Qiao Xiaohui, "*Shandong Dianli 83 Yi Shouhui Lu Neng Jituan* (The Shandong Power Group Bought Back the Lu Energy at 8.3 Billion)," *Caijing* (The Finance and Economy Magazine), No.5, Mar. 3, 2008; Li Qiyan, "*Lu Neng Chai Shou Qi Mu* (The Separation and Sell of the Lu Energy)," *Caijing* (The Finance and Economy Magazine), No.24, Nov. 24, 2008.

[230] "*Yuncheng Shi Liang Guoyou Qiye Gaizhi Tai Lipu, 2.3 Yi Yuan Guozi 6,410 Wan Yuan Jiu Mai le* (The *Gaizhi* of Two SOEs in Yuncheng City was Too Strange: 230 Million of State Assets were Sold at 64

decided in 2003 to give the Liangshan Paint Factory to a private company at zero cost, while a lot of assets of the factory, including its land, were excluded from the appraisal of the transaction price. When former managers and workers of the factory questioned the deal, the private owner was protected by local officials, and a judge of the local court showed a fake official document as a "legal" evidence of the transaction.[231]

Sometimes, the forced privatization would trigger off large scale labor protests or demonstrations. In Chongqing Municipality, the No.3403 Military Factory was sold to a privatized enterprise by the city government in 2004; the protest of workers in the No. 3403 Factory lasted 13 days but was finally suppressed by 1,200 police.[232] In 2009 at the Linzhou Steel Plant of Henan Province, the privatization scheme and its purchaser were arranged by local government without transparency. Finally, workers of the enterprise organized protest and a government official who was responsible for arranging the privatization was detained by workers in the plant for three days.[233] Similar but worse situation occurred at the Tonghua Iron and Steel Plant of Jilin Province, where a private steel company directly negotiated with the provincial government and made deals, without letting the managers and workers of the enterprise know. The SOE was privatized in Dec. 2005 by

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Millions)," *Guangming Ribao (Guangming Daily)*, Feb. 24, 2004; "*1.6 Yi Guozi Xian Xie Liushi, Yuncheng Liang Ming Guanyuan Luoma* (160 Million State Assets were Almost Peculated, and Two Officials in Yuncheng City Stepped Down)," *Shanxi Wanbao* (Shanxi Evening News), July 26, 2004.

[231] Wang Hai, "*Guoqi Baoli Gaizhi: Zichan Liu Geren, 'Heidong' gei Guojia* (The *Gaizhi* in Violence at an SOE and Asset Stripping)," *Shichang Bao* (The Market News), Jan. 6, 2004.

[232] Workers of the No.3403 Factory, "*Guoqi Siyou Hua Zhong Jiang Jifa Geming: Zhi Zhonggong Shiliu Jie Si Zhong Quanhui de Gongkaixin* (Privatization would Trigger off a Revolution: A Petition to the Headquarter of the Chinese Communist Party)," Sept.17, 2004 (www.xinmiao.com.hk/0004/0100-0124S).

[233] Chen Yifang, "*Lin Gang Shijian Qianqian Houhou* (The Background and Consequences of the Event at the Linzhou Iron and Steel)," Shanghai, China, *Xinmin Zhoukan* (Xinmin Weekly), Aug. 31, 2009.

the private company. In March 2009, the private company decided to withdraw from the Tonghua Steel, because a tension between managers and worker kept increasing and the firm made a large amount of losses after the privatization. But, the Tonghua Steel began to make profit right after the private company withdrew. Attracted by the profit, the private company changed mind again and negotiated with the provincial government officials for a second time takeover. On July 22, 2009 the provincial government proclaimed that the Tonghua Steel would be re-privatized by the same private company within two days. Workers of the firm got angry about the decision. They did not fight against the provincial government; instead, they surrounded the CEO from the private company and beat him to death. After the tragedy occurred, the provincial government immediately compromised by issuing a document in which the government promised that the enterprise would never be privatized again.[234]

When SOE privatization was manipulated by managers, they might cooperate with outside purchasers and cover up some inappropriate transactions. For instance, SOE managers might transfer the control of an SOE to an outside purchaser before the latter paid off the amount to buy the SOE; in other words, the purchaser could offer an empty investment promise or pay only a small portion of the investment amount written in the transaction contract, but gained actual control over the SOE and was able to use the resources of the SOE to complete the transaction. Thus, the privatization would become a fully or partly free deal. In the case of the Qinhai Third Pharmaceutical Factory mentioned earlier, managers of the SOE allowed the outside purchaser to control the firm when the purchaser paid only 1.5 million yuan, about one third of the amount he

[234] Wang Jianjun, "*Tong Gang Beiju de Luoji* (The Logic behind the Tragedy at the Tonghua Steel)."

ought to pay for the privatization; ultimately, the purchaser borrowed 3 million yuan collateral loans from state banks on the assets of the enterprise, then took the money away.[235] At the end of 2005, a private company formerly took over an SOE, the Changzhi Steel Plant in Shanxi Province. But, a questionable arrangement was made by the managers of the SOE: before the asset transaction took place: six months earlier the managers of the SOE notified their customers that payments for products of the SOE were all paid to the private company who was not yet the owner of the SOE. In this way, the private company was able to collect huge amount of funds and used the sales revenue of the Changzhi Steel to buy the SOE.[236] Also in Shanxi Province, in the case of the Qinshui Mine, the private purchaser was allowed to pay the transaction of privatizing the SOE through three payments within a year, but to gain control over the enterprise right after the first payment. So the purchaser used the revenue of the mine to pay off the transaction.[237] At the end of 2005, the Xilin Steel Plant in Heilongjiang Province was privatized by a private company; the latter immediately obtained the control over the SOE, but the payment for the asset transaction was paid only a year later. The purchaser controlled the cash flow of the SOE before it really bought it, and used the revenues of the SOE to pay off the transaction.[238] At the Changchun

[235] Ma Yingshan, "*Weizao Gongshang Zhizhao, Xu Tou Konggu Zijin, Pian Zhan Guoyou Zichan Fa Burong* (With a Fake Business Registration, Obtained Control over an SOE by False Investment)." *Renmin Ribao* (The People's Daily), Nov. 10, 1999.

[236] "*Chang Gang Gaizhi* (The *Gaizhi* of the Changzhi Steel Factory)," *ZhengQuan Shichang Zhoukan* (The Stock Market Weekly), No.23, June 24, 2006.

[237] "*Shanxi Qinshui 39 Ming Dangyuan Shangshu Jie 800 Yi Guozi Liushi* (39 Communist Party Members Appealed for the Disappearance of 80 Billion State Assets)," *Huanjing yu Shenghuo* (Environment and Life), No.7, Dec. 4, 2009.

[238] Zhao Weimin, and Long Hao, "*Xi Gang Gaizhi Mituan* (the *Gaizhi* Puzzle at the Xilin Steel Group)," *Zhongguo Jingji Shibao* (China Economic Times), Feb. 22, 2010.

Semiconductor Factory in Jilin Province, a private purchaser input 20 million yuan and obtained 80 percent shares of the factory; but, three days later, the purchaser transferred the 20 million out of the account of the privatized firm but maintained his control as a new owner. Ultimately, he got the SOE but did not really pay any cent.[239]

Obviously, the strategy of "spending your money to buy your home for me" or "obtaining your home without real payment" exposed in the cases could hardly be implemented without tacitly approval of the SOE managers. They might be rewarded for their collaboration with the outside purchasers, but such deals were often hid carefully. Workers of the SOEs might feel suspicious but could not collect sufficient evidences about the under-table deals. Occasionally, workers' protests could cause the attention of local governments, and fraud purchases were revealed after investigations. In Baoding city of Hebei Province at the Yi Textile Factory mentioned earlier, the CEO of the factory, Wang Lijuan, and her outside collaborators were accused for contract fraud and corruption, thus were sentenced for thirteen to twenty years in jail; but, a local newspaper so expressed, "in Baoding city and other places all over China, innumerable figures like Wang Lijuan have not been prosecuted."[240] Besides this case, the author noticed that among the other 30 analyzed cases, the transaction processes of 24 cases were more or less questionable, but only the fraudulent

[239] Wang Lei, "*Changchun Bandaoti 4.2 Yi Guozi Liushi, Muhou Heishou Xiekuan Zhengfa* (The State Assets in 420 Million of the Changchun Semiconductor Factory was Gone, and the Black Hand behind Disappeared)," *Caijing Shibao* (the Finance and Economy Times), Nov. 20, 2004.

[240] "*Yuan Yi Mian Jituan Dongshizhang Wang Lijuan Yi Shen Huo Xing 20 Nian* (The Former Chairman of the Board of Directors of the Yi Textile Group, Wang Lijuan, was Sentenced for Twenty Years in Jail)," Baoding, China, *The Baoding Evening News (Baoding Wanbao)*, Jan. 24, 2011.

purchases in three cases were officially investigated. [241]

The author also analyzed the post-privatization activities of the purchasers. In the 31 cases, only seventeen private purchasers continued industrial production of the privatized SOEs, of them five purchasers were interested in the value of the land of the SOEs and removed the privatized SOEs to suburb and made great profit by selling the land located in cities; and the other fourteen purchasers bought the SOEs for various non-industrial purposes, and the most frequently observed non-industrial purpose was to sell the land of SOEs if the enterprises were located in cities and their land had huge commercial value. For example, a military enterprise, the No.5023 Factory located in Mianyang city of Sichuan Province, was sold to a private company in 2004 at a price of 18 million yuan and the new owner then sold the land of the firm and made a profit of 1 billion yuan.[242] In Yiyang city of Hunan Province, the managers of the Yiyang Bearing Factory sold their enterprise to a private real estate developer in 2007 and their decision caused protests of workers.[243] In Linan city of Zhejiang Province, the Linan Silk Spinning Factory was sold to a small private company in 2007, and the purchaser's purpose was to sell the land for real estate development by changing the local zoning policy, so the industrial

[241] The three cases were the case of the Qinhai Third Pharmaceutical Factory, the Changchun Semiconductor Factory, and that of the Nanjing Zhongshan Group.

[242] Fang Xiao, "*Sichuan 'Wo An' Jundongchang Shu Yi Guozi Jian Mai Siren* (The Case of the Privatization of a Military Enterprise in Sichuan: Hundreds of Millions of State Assets were Sold Cheaply to Private Purchasers)," *Dajiyuan Shibao* (Epoch Times), July 31, 2009.

[243] Lao Chunyan, and Yu An, "*Yiyang Zhoucheng Gongsi Gaizhi Weihe Fanfu Fasheng Chongtu he Qun Fang* (Why Do Labor Conflicts Repeatedly Take Place in the *Gaizhi* Process of the Yiyang Bearing Company)," Sept. 18, 2011 (www.tianya.cn/publicforum/content/no110/1/195147).

properties could be used for commercial purposes.[244] Also, in Luzhou city of Sichuan Province the Changjiang Second Hydraulic Factory was sold to a real estate developer in 1999[245] and in Henan Province the Zhengzhou Ethyl Alcohol Factory in Zhengzhou city was sold to a real estate developer in 1997.[246] When the private purchasers targeted the land or other physical assets of the SOEs, rather than the enterprises themselves, the privatized firms were not really restructured; more likely, the firms, together with their workers, were abandoned by the new private owners.

Since a lot of privatization schemes in the 31 cases benefited SOE managers or private purchasers at the costs of workers, it was very possible that such privatization would lead to labor protests. Analyzed the situation at the workplace in the 31 cases, the author found that in 24 cases workers' protests or demonstrations took place during and after privatization, and some of them were in large scale and will be further discussed in the next chapter.

4.4 Decorated Large SOEs for Listing on Stock Market

Another privatization method is to reorganize SOEs into LLSCs for listing on stock market and have the LLSCs partially privatized through IPO (initial public offering); it could only be applied to qualified LLSCs. Since the Chinese government lacked financial resources to cover the

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[244] "*Zhejiang Lin'an Sichou Zongchang Gaizhi Neimu Diaocha* (An Inside Story of the *Gaizhi* at the Lin'an Silk Spinning Factory of Zhejiang Province)," Sept. 28, 2007 (http://blog.sina.com.cn/s/blog_50dd45af01008jo0.html).

[245] Fang Yuan, "*Luzhou Gongren Dao Shizhengfu Kangyi Gaizhi Liyi Bei Boduo* (Workers in Luzhou City Protested at the City Government for Consequences of *Gaizhi*)," Radio Free Asia, Nov. 10, 2009.

[246] Sun Jibin, "*Fubusi Fuhao Xie Guosheng Beibu Neimu: Huo Qi Jianbing Guoqi* (The Inside Story about a Billionaire Xie Guosheng who was Once Listed on the Forbes but Now Put in Jail: The Troubles Caused by Purchasing SOEs)," Beijing, China, *Fazhi Ribao* (The Rule of Law Daily), Sept. 8, 2007.

huge costs of SOE reform, it encouraged large SOEs to raise funds through stock market from individual stock buyers and from foreign investors as well to decrease the debt-asset ratio of the SOEs; thus, the costs of the SOE reform in the enterprises were partly removed from governments to individual stock buyers. With such a consideration, the government was more interested in raising funds than in improving corporate governance of the listed LLSCs.

Since 1997, incorporatization of large and medium SOEs in China had been considered the core approach to transform them into modern enterprise system. It usually took two steps: organizing enterprise groups[247] and establishing shareholding companies. Many large- and medium-sized SOEs were reregistered as limited liability shareholding corporations (LLSCs). Among them, some were enterprise groups through merging several large or medium SOEs without real changes of the public property ownership structure. A lot of government offices previously in charge of industrial administration simply changed their legal status by registering themselves, with some SOEs under their administration, as state shareholding companies and the largest shareholders of the companies that were previously administrated by the offices. In such corporation groups, the government-enterprise relations between the previous administrative offices (now are "mother company") and the SOEs (now are "son company") remained unchanged, and the incorporatization of the SOEs did not have privatization effect. Very often, the process was arranged by government officials and SOE managers behind closed doors. A survey found that if SOEs were transferred into the hands of the state shareholding companies, in average, the sale price of the transactions would

[247] "*Guowuyuan Jueding Jiakuai Jianli Daxing Qiye Jituan de Shidian* (The State Council Decided to Push Forward Experiments for Establishing Large Enterprise Groups)," Beijing, China, *Jingji Ribao* (Economic Daily), May 17, 1998.

be only 63 percent of book value, whereas the price for a transaction of large SOEs to private companies was about 98 percent of book value.[248]

Only when an SOE was listed on stock market and its ownership structure was diversified through selling SOE shares to the public via IPO and "bringing in outside investors while maintaining majority state ownership,"[249] could partial privatization effect be observed. China's stock market was established in the early 1990s, and the large scale privatization took place after 1997, so the stock market in China could more support the privatization than that of Russia. Many large industrial SOEs have been listed on China's stock market; but, the number of the listed industrial SOEs was not really large enough, in contrast to the huge number of the industrial SOEs to be privatized. As of July 2012, there are about three thousand listed LLSCs[250] (most of them were former SOEs); from 1992 to 2011, the stock market only absorbed 1,329 listed industrial companies,[251] eight percent of all large- and medium sized industrial enterprises of 1992,[252] and of the listed industrial companies 447 were machine building and instrument manufactures, 252 were petrochemical companies, and 188 were metal and non-metal processing companies.[253]

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[248] Liu Xiaoxuan, "*Guoyou Qiye Gaige yu Chongzu* (The Reform and Transformation of SOEs (a speech at Unirule Institute))", May 27, 2005 (http://www.unirule.org.cn/symposium/c287.htm).

[249] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 48.

[250] "*Yuan 'Shijie Yiliu' Chengwei A Gu Touzizhe de Fuyin* (Hope China's Stock Market Becom One of the Best in the World, and the Perspective to be a Good News for the A Share Investors)," *Zhengquan Shichang Zhoukan* (The Stock Market Weekly), No.27, July 8, 2012..

[251] China's Association of Listed Companies, "*Zhongguo Shangshi Gongsi de Fazhan* (The Development of China's Listed Companies)," Beijing, China, the Website of China's Association of Listed Companies, visited on July 7, 2012 (http://www.capco.org.cn/zhuanti/cjz/xi_hylt.html).

[252] China's State Statistics Bureau, *Zhongguo Tongji Nianjian 1993* (China Statistics Yearbook 1993), 417.

[253] China's Association of Listed Companies, "The Development of China's Listed Companies," Beijing, China, the Website of China's Association of Listed Companies, visited on July 7, 2012.

The numbers suggest that privatization of the majority of industrial SOEs could hardly count on IPO. In the stock market the listed former SOEs only released about 35 to 40 percent of their state-owned shares in average, and the proportion of state-owned shares in the capital structure of China's listed companies was maintained between 61 to 64 percent from 1995 to 2004.[254] The listed companies are seemingly unable to release much more state shares in the near future, because such releases would reduce dividend per share and hurt the stock market.

Actually, most listed companies in China did not perform well and and transactions in the stock market were often manipulated by security trading companies and the listed LLSCs. From 1992 to 2005, China's Shanghai Stock Index fluctuated between 300 points and 2,200 points; in 2006 and 2007 the market was bulled from 1,161 points at the beginning of 2006 to 5,979 points in Nov. 2007, a rise of 415 percent; however, the boom was followed by a dramatic fall to 1,821 points at the end of 2008. From 2009 to the end of July 2012, the index remaind at a low level between 2,000 and 2,200 points, although the Chinese government proclaimed that it has kept a high economic growth in the years.[255]

Most individual buyers and sellers in China's stock market were speculators for short-term gains through frequent trading; usually, they were not interested in long-term investment. In such a market environment of stock exchange, whether a listed company had good corporate governance and performance was often not an issue those individual speculators cared about; some companies

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[254] Ma Shu-yun, "China's Privatization: From Gradualism to Shock Therapy?" *Asia Survey*, Vol.48, No.2, 2008, 201.

[255] "*Shang Zheng Zhishu Lishi Jilu* (The Historical Record of the Shanghai Stock Index)," Beijing, China, *Sohu Website*, July, 12, 2012 (http://q.stock.sohu.com/zs/000001/lshq.shtml).

had made losses for years and had never distributed dividends, but individual buyers might still purchase their shares,[256] as long as the companies were identified as rising stars by the stock market analysts who work together with the managers of the companies. In 2008, 70 percent of the Chinese individual stock buyers put half of their assets into the stock market, and 20 percent of them put 30 to 50 percent of their assets; but, at the end of the year, a survey reported that 60 percent of them lost more than 70 percent of their investment in the stock market, 22 percent of them lost 50 to 70 percent of their investment, and seven percent of them lost 30 to 50 percent[257] (see Appendix of this chapter). Therefore, the number of individual traders decreased from 69 million in 2002[258] to 42 million in 2011, and eighteen million of individual stock traders sold out all their stocks in 2011.[259]

Wu, a well-known economist in China, pointed out in 2000 that in many new LLSCs the state was still the dominant shareholder and the rights of minor shareholders were often ignored; on the other hand, as a lot of LLSCs were simply the renamed former industrial management government offices, those directors of the board, who were previous officials, did not really play the role as owners, and some of them even directly involved in instructing management as they were used to

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[256] "*Huaqian Mai 'Zhai'* (Buy 'Debts')," *Jingji Ribao* (Economic Daily), Sept. 12, 1998.

[257] "*Gumin Shengcun Xianzhuang Diaocha: Yu Jiu Cheng Gumin Kuisun, Liu Cheng Kuisun Yu 70%* (A Survey about the Current Status of Individual Stock Investors: More than 90 Percent Lost Money, and 60 Percent Lost More than 70 Percent of Their Total Investment)," *Shanghai Zhengquan Bao* (Shanghai Securiry News), Dec. 29, 2008.

[258] Ma Shu-yun, "China's Privatization: From Gradualism to Shock Therapy?" *Asia Survey*, 205.

[259] "*Jiangsu Gumin Zongshu 666 Wan, Ju Quanguo Disan* (Individual Stock Holders in Jiangsu Province Reached 6.66 Million, the Third Place in China)," Beijing, China, *the Website of People's Daily*, Feb.20, 2012 (http://js.people.com.cn/html/2012/02/20/80954). At the end of 2011, individual stock traders in China maintained 133 million trading accounts; in the account holders 60 million involved in stock trading in 2011 and 30 percent of them sold all their stock.

do before.[260] For many LLSCs, establishing proper corporate governance was not the main task; instead, they were most interested in financial operations for listing on the stock market so they could sell shares to collect easy and quick money from domestic and foreign individual buyers. As Yusuf, Nabeshima and Perkins said, in China, the listing of state-owned enterprises on the stock market and the sale of their shares were not the beginnings of an effort to change the nature of corporate governance; the purpose of the sales was mainly to provide the enterprises with other avenues for raising capital both at home and abroad; this process did not affect corporate governance, because shareholders had no right to select company management or influence the behavior of management in any other way.[261]

Since the late 1990s, "decorating a company for listing" became an issue widely discussed and practiced by CEOs of LLSCs. In China the central government controlled the approval for stock market listing, and it used the power in a manner as in the planned economy: it did not really use standardized requirements to determine whether a company was qualified for listing, instead, the government distributed the quota for listing to provinces and ministries, and let officials of the central government personally decide which company to be listed and how many SOE shares to be sold to the public. In order to get the approval and to have a higher IPO price, CEOs of the state-owned LLSCs spent a lot of resources and used various tactics to "decorate" their companies for listing, e.g. companies were reorganized so that only would the best quality assets appear in the

[260] Wu Jinglian, "*Woguo Da Gongsi Zhili Jiegou Cunzai de Wenti he Gaishan de Tujing* (The Structural Problems of Corporate Governance in China's Large Corporations and the Path for Improvement)," a speech on June 2, 2000, in Wu Jinglian, *Zhuangui Zhongguo* (China in Transition), Chengdu, China, Sichuan People's Press, 2002, 128-138.

[261] Shahid Yusuf, et al. *Under New Ownership: Privatizing China's State-Owned Enterprises*, 72.

balance sheets of the companies to be listed.[262] Often, those companies transformed from large SOEs had better chances to obtain the scarce quota, as the government would like to utilize stock market to raise capital for those strategically important state-owned companies. Some LLSCs even made false accounting records. For instance, at the Dongfang Boiler Manufacture in Zigong city of Sichuan Province, its senior managers changed accounting record to provide false information before the company was listed.[263]

How did LLSCs in China get approval for stock market listing? The operation of the Kangsai Group in Hubei Province was a typical case and was named as "Kangsai phenomenon" by China's official Xinhua News Agency. The term implied that the practices of the Kangsai Group for stock market listing were widely used in the country.[264]

The Kangsai Group was the former Huangshi Garment Factory, under the Kangsai Business Development Inc. Its main products T shirts and dresses were warmly welcomed in market, and in 1990 the minister of China's Textile Industry named its T shirt "the flower of T shirt." Since 1993, Tong, the CEO of the factory, and Zhang, the communist party secretary of the factory, decided to make large amount of quick money by arranging stock market listing. As administrative approval for the listing was a precondition, the managers so did their "public relations": gave 100 thousand of

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[262] Lu Guoyuan, "*Shangshi Gongsi Xianxiang* (The Phenomenon of Stock Market Listing Company in China)," *Shanghai Zhengquan Bao* (Shanghai Security News), Sept. 15, 1998.

[263] Qiu Li, and Mu Zi, "*Dong Guo Tan Wei: Women de Fenxi yu Sikao* (Exploring the Dongdang Boiler Case: Our Analysis and Thinking)," Beijing, China, *Caiwu yu Kuaiji* (Finance and Accounting), No.8, 2000.

[264] Fang Zhengjun, Fu Gang, and Jiang Shiqiang, "*Cong 'Kangsai' Xianxiang Kan Xingzheng ShenpiLoudong* (The Problems of Administrative Approval for Stock Market Listing: The Implication of the 'Kangsai Phenomenon')," *Xinhua News Agency*, Nov. 26, 2000 (http://www.people.com.cn/GB/channel1/11/20001126/327112.html).

shares to critical figures in the central administration for the approval, five to ten thousand of shares to the officials who could influence the approval, and one to two thousand of shares to those who would not influence the approval but might make troubles for the listing process. In December of 1993, Zhang met with a deputy director of the State Commission for Economy and Trade at Beijing, and asked him to support the approval. As an exchange, the wife and daughter of the senior official bought 40 thousand of employee shares of Kangsai at the price of one yuan per share. Before the stock of Kangsai was traded in stock market, Zhang sent another 44 thousand employee shares to the wife with the same price in 1996. Later, family members of the deputy director received 37 thousand of distributed shares as dividends. All together the family members got 121 thousand of the shares from the company, and obtained 1.13 million yuan in cash after the company bought the shares back at a price of ten yuan per share.

In 1996 Tong met with the director of China's Association of Textile Industry (the former Ministry of Textile Industry) and asked her to provide a document for recommending the listing. As an exchange, in March of 1996 the son of the director of the association bought 100 thousands of shares of Kangsai at the price of one yuan. Later the son sold all the shares at market price and made a profit totally in 890 thousand yuan. Besides the mentioned officials at the central administration, local government officials also received the shares. For instance, the communist party secretary of Huangshi city got 50 thousand of the shares and then made a profit in 350 thousand yuan; and the director of Huangshi branch of Construction Bank got a bribe in 500 thousand yuan for providing loans to Kangsai, with the funds the company was able to manipulate stock price of the company for profiting. Also, several other local officials received

such bribes for supporting the listing of Kangsai.

The factory was actually not really qualified for the listing; but, through the operation in "public relations," the managers successfully obtained a permit for the listing, and the Kangsai Group got a quota for issuing 18 million SOE shares on stock market after Aug. 28, 1996. On the first day when the stock was traded at the market, its price went up to eleven yuan. Like many listed companies in China, the corporate governance of Kangsai was in poor status, while the chairman of the board of directors and senior managers were still appointed by local governments, and effective overseeing by shareholders' congress was not available. Under the leadership of the corrupt managers, after Kangsai's stock was traded in the market, its performance declined within years. The market share of its products decreased by 60 percent and the debt rate of the company increased to 70 percent, and the accumulated losses of the company had reached 160 million.[265]

The Kangsai case suggests that, while stock market listing served for quick money making, and unqualified companies were listed, the ideal function of building up a modern enterprise system through SOE restructuring was often left aside in China. Rather than worked hard to improve operation of the enterprises, managers of such companies were concerned with making quick money through speculation on stock market. This is one of the reasons why partial privatization of the listed SOEs did not necessarily improve their performance in China.

[265] Ibid.

In 2002, Jiang, a Deputy Director of the State Commission for Economy and Trade, pointed out six problems found from SOEs' listing process: released false or misleading information from the companies, the board of directors was run poorly, CEOs were appointed by insiders, balance and check by controlling shareholders were absent, minor shareholders were not protected, and some listed companies could hardly survive.[266] Indeed, in China's stock market emerged a unique "three-year phenomenon:" a lot of listed companies showed good performance in the first year when they did IPO and made no profit in the second year, then had losses since the third year and were soon off-listing from the stock market.[267] The "three-year phenomenon" implied that, after SOEs were listed, they simply raised capital from individual stock buyers, but the performance of the listed companies was not improved. In other words, the individual stock buyers simply played a role in putting capital into the state shareholding companies for the state. Therefore, a debate between the government and its defenders and those who stood on the side of ordinary people appeared in China, and the core issue of the debate was who should pay the SOE reform costs, the state or the people.[268]

China's privatization policy for all SOEs was "grasping the large and letting the small go;" and the policy for large SOEs was actually "grasping the profitable ones and letting the loss-makers go." Most large SOEs with better performance were transformed into LLSCs whose dominant

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[266] Zhao Jianhua, "*Jiang Qiangui: Zhongguo Guoyou Qiye Chongzu Shangshi Chuxian Liu Da Wenti* (Jiang Qiangui: Six Big Problems are Found in the SOEs Reorganized for Listing," China News Agency, May 13, 2002 (http://finance.sina.com.cn/t/20020514/206434.html).

[267] Mei Yongcun, "*'San Nian Xianxiang' Zhide Guanzhu* (Pay Attention to the 'Three Year Phenomenon,')," *Jingji Cankao Bao* (Economic Information News), Oct. 18, 1999.

[268] Zhang Yugui, "*Guoqi Gaige de Chengben Gai You Shui Chengdan* (Who Ought to be Responsible to Pay the Costs of the SOE Reform)?" Beijing, China, *Jingji Shikan* (Economic Times Magazine), No.5, 2003.

shareholders are government bodies; at the same time, the companies were listed in stock market so their financial situation could be improved through IPO. In this way, the central and local governments have not only kept the profitable companies under their control,[269] but also were able to collect capital for the companies. However, such strategies already encountered difficulties in recent years when China's stock index kept falling.

5. Why Did Shanghai Want an Incomplete Privatization?

The Function of Shell Company

The privatization in China might be featured as a spontaneous one. The central government has never made privatization an official policy and no national legislation exists to dictate the process; "there are only a few government guidelines, which are far from clear and whose enforcement is highly problematic."[270] During the most important years of the privatization process, the only government office that was responsible for supervising state-owned properties was rescinded; thus the spontaneous privatization became convenient. As the Chinese regime continues to proclaim that it insists on the direction of China's economic reform along the track of socialist system, it has somewhat succeeded in releasing the financial threat of the poorly performing SOEs to its state-owned banking system through the unnamed privatization. However, such a privatization inevitably caused widespread corruption, labor disputes and social protests in the country.

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[269] Liu Xiaoxuan, "The Reform and Transformation of SOEs (a speech at Unirule Institute)", May 27, 2005.

[270] Chen Feng, "Privatization and Its Discontents in Chinese Factories," *China Quarterly*, No. 185, 2006, 45.

In China both SOE managers and workers were categorized as state employees (*guojia zhigong*) until the early 1990s; but, during the privatization process the two parties were treated by the state very differently. Unlike the Russian government which offered both managers and workers options for privatizing their enterprises, the Chinese central government perceived SOE workers as a burden to the state, and gave local governments and SOE managers the power to determine the fate of the workers in privatization. Therefore, when Russian workers were in alliance with their managers against outside investors during privatization process, Chinese SOE workers were targeted as the only party that was responsible to pay the costs caused by the failure of the SOE system. As Chen points out, the "privatization in China has been carried out in opaque ways, with little regard to the principles of fairness and justice… Local authorities and SOE managers are granted considerable discretionary power to decide how factory property is handled; workers, on the other hand, are totally excluded from the process."[271] The above sections of this chapter have described some detailed aspects of trilateral relations between the state, SOE managers and workers during the privatization process, and have revealed how local governments and SOE managers worked together and manipulated the privatization process spontaneously, and why labor protests were triggered off and how local governments suppressed the protests or demonstrations.

However, it would be a mistake to assume that all local governments in China behaved ruthless without mercy. For instance, the government of Shanghai Municipality seemed to be somewhat different with that of many hinterland provinces, and in Shanghai appeared a unique phenomenon since the 1990s, i.e. after *gaizhi* a lot of shell enterprises or companies related to

[271] Ibid.

their privatized mother SOEs have existed in the city, as a result of purposive incomplete privatization. The shell companies usually have no industrial production capacity, but are not shut down because they are responsible to pay social security contributions for their laid-off workers. Some of them have physical assets in hand and might receive revenues upon the assets; and some simply rely upon the funds transferred from government offices or state-owned LLSCs. The shell enterprises or companies have two member groups, the laid-off workers of the mother SOEs and a small group of managerial staff (usually four percent of the laid-off workers). The existence of the shell enterprises or companies is indeed a headache of the city government, but still the government chooses to maintain them.[272]

Why would the privatization of SOEs in Shanghai become purposively incomplete and what kind of role have the shell enterprises or companies played? This is an issue that has not been discussed in existing literature published outside China. In order to understand how an SOE became a shell company after privatization and why there was a need to maintain a shell company for former SOE workers, the author did a case study of the Shanghai Silk Spinning Factory. The case was selected from textile industry of Shanghai municipality. Textile industry in China was one of the loss-making industries, with "gradual decrease in always negative profitability" from 1993 to 1997.[273] The Shanghai Silk Spinning Factory was one of the leading SOEs in China's silk spinning and weaving industry during the period from the 1950s to 1980s. The author traced the changes

[272] Zhu Yaozhong, "*Qian Xi Keti Qiye Zhigong Sixiang Zhuangkuang ji Jiaqiang Gaijin de Duice Cuoshi* (Analysis about the Thought of Workers and Staff at the Empty Shell Enterprises and the Way to Improve Political Work)," Shanghai, China, *Qiye yu Wenhua* (Enterprise and Culture), No.3, 2010, 62.

[273] Carsten Holz, *China's Industrial State-owned Enterprises: Between Profitability and Bankruptcy*, 225.

occurred at the textile SOE and its shell company from the early 1990s to 2010.

The Shanghai Silk Spinning Factory was established by a Japanese company and some Chinese businessmen in 1906. In 1946 it was the largest silk spinning factory in the Far East. In 1950 the enterprise was taken over by the Chinese communist government and became an SOE. In the beginning of the 1990s, the SOE had two main workshops for silk spinning and weaving and twenty nine hundred workers, and more than two thousand pensioners as well. From the late 1980s the enterprise fell into difficulties as its equipments were too old and prices of raw materials became higher and higher. In order to get rid off the difficulties, the factory looked for the help of its prior Japanese owner, the Kanebuchi Spinning Group (it was later reorganized as Kanebo Ltd.) based in Osaka, Japan. In 1993, the Japanese company invested twelve million USD and the SOE input the equipment and building of its silk spinning workshop (equal to 1.3 million USD) as investment, and organized a joint-venture company, the Shanghai *Huazhong* Silk Spinning Company (Shanghai China-Kane Silk Spinning Company). The joint venture company did not performe well, thus the Japanese investor withdrew from the joint-venture years later and its mother company, the Kanebuchi Spinning Group in Osaka, was closed. In 2000 the Shanghai *Huazhong* Silk Spinning Company was taken over by an SOE located in Jiaxing city of Zhejiang Province, and workers of the former joint-venture company were reduced to three hundred. Later the company in Jiaxing fell in bankrupt.

During the 1990s, managers and workers of the Shanghai Silk Spinning Factory struggled for survival. Besides the joint-venture efforts, they also tried outsourcing by establishing new companies in nearby rural areas with support of village or township administrations (two in

suburb of Shanghai city and one in Kunshan county of Jiangsu Province near Shanghai). The SOE input capital and its old equipment into the new companies, and hired cheap rural labor to continue production. Being unable to improve product quality or develop new products, the outsourcing strategy did not succeed and the three new companies were closed within years. From 1993 the SOE began to lay off workers, and as of 1996 more than one thousand workers left the workplace with a minimum compensation (25 USD per month).[274] In November 1999 the Shanghai Municipality Government approved bankruptcy of the Shanghai Silk Spinning Factory and the enterprise was formally shut down in 2002.

However, the SOE was not fully closed and its assets were not all sold out. Before the SOE was shutdown, another company, the Shanghai New Silk Spinning LLC, with only a very small capital in 40 thousand USD, was established in January 1999, which was actually a shell company of the mother SOE. The main task of the Shanghai New Silk Spinning LLC was to take care of the needs of the laid-off workers and pensioners of the SOE. An empted quite new factory building of the SOE was left to the shell company and several former management staff worked there. The factory was located at *Caojiadu*, one of the business centers of Shanghai city, so the shell company was able to lease the space of the building to flower shops and other small businesses such as restaurants, and used revenues to pay employer and employee contributions to the city-run pension system for the laid-off workers, and to reimburse a part of medical expenditures for the laid-off workers and pensioners because until 2009 there was no state sponsored medical insurance available for the people.

[274] According to an interview with a workshop director of the factory, conducted by the author in June 1996.

The shell companies actually played a missing role of the central government. During the era of planned economy, the central government promised that all state employees would receive their pension from their work units, but there was no state-sponsored pension system in China. During the privatization period, Shanghai established the first local pension insurance system in the country, and collected contributions from employers and employees to pay distributions to retirees. However, the millions of laid-off workers were left at a hopeless situation, as the previously promised pension payments to them were denied by the central government in *gaizhi* process, and they might not be eligible to receive pension from the newly established pension system after they reach their retirement age, because they do not have current employers who could make contributions to the new pension system for them and are personally unable to make such contributions after they lost jobs. Consequently, they could only count on their previous work units, the SOEs, while perceive the SOEs as the only "home" and rely upon it financially and psychologically;[275] and the SOEs, even though already bankrupted or privatized, are still obligated to pay the pension contributions for the laid off workers, through the operation of shell companies.

In the case of the Shanghai Silk Spinning Factory, the city government did not sell, and did not allow the managers of the SOE to sell, all the remaining state assets of the factory to private purchasers; instead, it left some, probably the most valuable, state assets of the factory, the land of the enterprise and a building constructed in the early 1990s with seven thousand square meters,

[275] Zhu Yaozhong, "*Qian Xi Keti Qiye Zhigong Sixiang Zhuangkuang ji Jiaqiang Gaijin de Duice Cuoshi* (Analysis about the Thought of Workers and Staff at the Empty Shell Enterprises and the Way to Improve Political Work)," 62-63.

to the Shanghai New Silk Spinning LLC, So the shell company has been able to routinely collect certain amount of revenues through leasing space of the building.

Although this shell company has offered limited help to the laid-off workers of the SOE, the job of its staffs was not easy. A former secretary of the CEO of the SOE reported that a lot of laid-off workers thought they were sacrifice of the economic reform and were finally abandoned by the state, and these workers took the perception too much to heart.[276] In 2009 the director of the shell company mentioned that a lot of laid-off workers lived in hardship, while both husband and wife were laid off and could not find job at their mid age, and their children did not have job either, when China's economy was influenced by the 2008 worldwide financial crisis; a lot of them were sick for years but could not be properly treated, because the shell company was unable to fully reimburse their necessary medical expenditures. When the people in difficulties frequently complained, the staff of the shell company had to regularly visit one family by another, nicely listened to them, and tried best to calm them down, and convinced them that they were not ignored by the communist government.[277]

The case of the Shanghai Silk Spinning Factory implies that the basic policy of the central government in privatization was to leave the social security burdens of SOE employees as much as possible to local governments, SOE managers and the purchasers of SOEs. The privatization of industrial SOEs in China thus encountered a unique problem that had not been observed in other

[276] Ibid.

[277] Zhang Guoshun, "*Li Gang Zhigong Bang Kun Wending Gongzuo de Shijian yu Sikao* (The Practices and Thinking about the Work to Help Laid-off Workers to Solve Their Difficulties for Maintaining Social Stability)," *Qiye yu Wenhua* (Enterprise and Culture), No.5, 2009, 33-35.

transition societies: the priority of the privatization was seemingly not to restructure the enterprises, but to find ways to pay the social security payments, as observed in Shanghai, or simply abandoned the laid-off workers and SOE pensioners together with the obligation to pay the debts, as seen in many other provinces. So, the central government decentralized its social security obligations and released itself from the pressure; at the same time, it kept its eyes closed to the spontaneous privatization process, and let local governments, SOE managers or private purchasers of the enterprises do whatever they wanted to do, including the spontaneous arrangements of the social security issues. Shanghai is one of a few cities in China that made the largest efforts to prevent social protests caused by *gaizhi*, so the privatizations of a lot of SOEs in Shanghai were purposively incomplete and there exist many shell companies to fill the missing role of the central government. But, a lot of city governments in China did not so behave with mercy, and many laid-off workers of privatized SOEs in other provinces did not have such opportunities as their fellow Shanghainese had. The discussion of next chapter will show that in many provinces local governments were indeed ruthless to SOE workers

Appendix:

The Gains and Losses of China's Stock Market Investors

	2006 (%)	2007 (%)	2008 (%)
Change of Shanghai Stock Index in the Year	+130	+97	-65
Individual Investors who Gained in the Year	70	49	6
Of which:			
Gained more than 100%	5	7	…
Gained 50% to 100%	14	11	…
Gained 20% to 50%	30	17	…
Gained less than 10%	21	14	…
Individual Investors who Had no Gains Or Losses in the Year	14	13	0
Individual Investors who Lost in the Year	16	38	94
of which:			
Losses were Less than 10%	7	17	…
Losses were Less than 30%	…	…	5
Losses were between 20% to 50%	7	19	…
Losses were between 30% to 50%	…	…	7
Losses were More than 50%	2	2	…
Losses were between 50% to 70%	…	…	22
Losses were More than 70%	…	…	60

Note: In 2006, the Shanghai Stock Index grew from 1,161 points to 2,675 points; in 2007, the index grew from 2,675 points to 5,262 points; and in 2008 the index fell from 5,262 points to 1,821 points.
Source: Xie Tao, "*Diaocha Xianshi: 2006 Nian Qi Cheng Gumin Huoli, Jiu Cheng Ban Pao Shu Dapan* (A Survey Shows: In 2006 70 Percent of Individual Stock Investors Gained, but 90 Percent of them Did not Gained as Many as the Growth of Stock Index)," *Zhongguo Zhengquan Bao* (China Securiry News), Dec. 26, 2006; "*Touzizhe Jin Si Cheng Kuisun, Pao Yin Dapan Buzu Yi Cheng* (About 40 Percent of Individual Stock Investors Lost Money, and Only Less than 10 Percent Gained as Many as the Growth of Stock Index)," *Zhongguo Zhengquan Bao* (China Securiry News), Dec. 24, 2007; "*Gumin Shengcun Xianzhuang Diaocha: Yu Jiu Cheng Gumin Kuisun, Liu Cheng Kuisun Yu 70%* (A Survey about the Current Status of Individual Stock Investors: More than 90 Percent Lost Money, and 60 Percent Lost More than 70 Percent of Their Investment)," *Shanghai Zhengquan Bao* (Shanghai Securiry News), Dec. 29, 2008.

Chapter 9

Consequences of China's Privatization: The Dominance of Managers and Enduring Tensions at the Workplace

As of 2011, China has almost completed its privatization of industrial enterprises. The Chinese government has seemingly been reluctant to provide an overall assessment about the privatization process and its results for the public, although it allowed foreign scholars to conduct several research projects on the issue for international audiences.[1] The projects focused on ownership changes, and corporate governance and performance, but neglected study of management-worker relations. As discussed in chapter eight, in China the majority of industrial SOEs, particularly the medium- and small-sized enterprises, were privatized through MBO or employee shareholding; in other words, in insider privatization there was no presence of outside investors who could oversee managers, but relations of continuing members of the work units experienced dramatic changes. Without a wide-ranging analysis of the changing management-worker relations, one can hardly understand the post-privatization restructuring process that occurred in enterprises, which greatly shaped corporate governance and performance of firms. In this chapter the author will use survey data from various sources to analyze the

[1] See Shahid Yusuf, Kaoru Nabeshima and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, Washington, DC, the International Bank for Reconstruction and Development/ The World Bank, 2006; and Ross Garnaut, Song Ligang, Tenev, Stoyan, and Yao Yang, *China's Ownership Transformation: Process, Outcomes, Prospects*, Washington, DC, the International Finance Corporation and the International Bank for Reconstruction and Development/ The World Bank, 2005.

consequences of China's privatization,[2] not only in terms of ownership changes and corporate governance, but also management practices, management-worker relations, and firm performance as well.

In Chinese restructured companies, the functions of the board of directors were often manipulated by managers, distorting proper corporate governance. The majority of the managers lacked management capabilities, and did not know how to properly deal with relations with workers, but they were sophisticated at pursuing their personal interests—at cost to the companies—sometimes even using inappropriate or illegal methods. Being ruthless to their workers, many managers have simply built up personal fiefdoms; dialogue between bosses and workers is reduced, wages are cut, employee welfare diminished, working hours extended but no extra wages paid, and workers' legal rights infringed upon. In some workplaces, even military style management has been used to discipline employees. As workers' grievances and discontent have accumulated

[2] Two main sources of the data are the reports of the Chinese Entrepreneur Survey System (CESS) and the tabulated statistics from the All-China Federation of Trade Union (ACFTU) 2002 survey. As privatization in China has never been officially admitted, the CESS and ACFTU don't define privatized enterprises as a survey category; instead, they classify industrial enterprises by the following categories: 1. SOE (enterprises that have not been privatized); 2. Collectively owned enterprise (owned and run by the district administration of cities and rural township); 3. Domestic private enterprise (established and owned by several individuals); 4. Foreign enterprise (owned by residents of Hong Kong, Taiwan and foreign countries); 5. Joint stock company (partly foreign-owned); 6. Limited liability shareholding corporation (LLSC, with more than 50 shareholders); 7. Limited liability company (LLC, with more than 2 and less than 50 shareholders); 8. Shareholding cooperatives (employee shareholding company); 9. Other enterprise with mixed ownership. Before the privatization, the first five categories were the only enterprise types in China; the LLSC, LLC and shareholding cooperatives appeared after the privatization, and most of them are privatized SOEs. While privatization moved ahead in China, the percentage of LLSC and LLC in the sampled enterprises of the CECC surveys increased rapidly: in 2000 the percentage of the two types was 31 percent, in 2003 it was 49 percent, and in 2010 as high as 66 percent. Therefore, in this chapter the author will use the data of LLSC and LLC to observe the situations of privatized enterprises.

and their claims frequently rejected, more labor disputes have been observed and many large scale labor protests or demonstrations have been reported. As long as the interests and dignity of workers are not heeded by the state and managers, and mechanisms to effectively protect workers' rights are not institutionalized, Chinese workers are placed in a weak position and their working morale is diminished. Consequently, poor corporate governance and management-worker relations in the privatized enterprises undermine the performance of the firms.

1. Ownership Structure of Privatized Enterprises

In China how many SOEs were privatized and who became their owners have never been clarified. The Chinese central government did some surveys about the progress of privatization. According to Garnaut, Song, Tenev and Yao who gained access to internal government documents, an official national survey in 1998 revealed that a quarter of China's 87,000 industrial SOEs had been through some phase of *gaizhi*, and another quarter planned to take some measure of *gaizhi*, while 60 to 70 percent of the *gaizhi* firms were partially or fully privatized; three years later, another national survey estimated that 86 percent of industrial SOEs had been through *gaizhi* by the end of 2001 and about 70 percent had been partially or fully privatized.[3] The 1998 and 2001 official survey reports were released to selected scholars who participated in a foreign sponsored research project

[3] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 5. Garnaut et al. cited from unpublished official report of the State Statistics Bureau about the 1998 survey and from a report of the State Economy and Trade Commission about the 2001 survey.

about China's privatization,[4] but have been kept confidential to media and scholars in China. So far, official data about how China's privatization was completed have never been available to the public.

Table 9-1 Methods of *Gaizhi*

Forms of *Gaizhi*	1998 National Survey (%)	2001 National Survey (%)	2002 Survey A (%)
Employee shareholding	21	19	27
Internal restructuring (incorporated or spin-off)	7	18	20
Open sales and leased out	27	25	28
Bankruptcy	5	11	13
Merge with other SOEs	10	14	…
Public offering	…	…	8
New investors	23	…	…
Joint venture	3	13	4
Other	4		…
Total	100	100	100

Source: The percentages of the 1998 and 2001 national survey were cited from Ross Garnaut et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 23 and 51. Sample size of the 1998 survey carried out by the State Statistics Bureau of China was 57,881 firms; sample size of the 2001 survey by the State Economy and Trade Commission was 54,644 firms. The 2002 survey (survey A) in 375 firms was organized by Gaunaut et al.

[4] The project was organized by Australian National University, Beijing University, and the International Finance Corporation (IFC) of the World Bank Group, and was sponsored by Australian Government Overseas Aid Program (AusAid) and IFC. The former State Economic and Trade Commission of the Chinese government facilitated the study. The research project was conducted in 2002; it selected 683 enterprises in 11 cities, and collected data from 1995 to 2001. See Javed Hamid, Foreword, in Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, viii.

Garnaut et al. mentioned that the 1998 and 2001 unpublished official survey reports revealed some information about *gaizhi* methods (see Table 9-1). Garnaur et al. did their own survey in 375 privatized firms in eleven cities from December 2002 to April 2003 (the survey is referred to as Survey A below). Putting the data of the surveys together, the author compiles Table 9-1 to describe *Gaizhi* methods in China. First of all, about five to thirteen percent of SOEs entered into bankruptcy proceedings, and the rest of them (at least 85 percent of SOEs) were transformed through ownership diversification or restructuring. In 1998 SOEs made great efforts to find new foreign or domestic investors; but the 2001 surveys showed that only about one quarter of SOEs were sold, though purchasers of the firms were not properly identified (Gaunaut et al. realized that many of the purchasers were actually insider-managers[5]); and eight percent of the firms were listed on the stock market, while the rest of the SOEs were either privatized through employee shareholding, or restructured without explicit ownership changes, such as being incorporated into state-owned LLSCs, or merged with other SOEs. It is notable that manager privatization, the most frequently used method in China, was missing in survey questionnaires, although Gaunaut et al. mentioned it in their book.

In terms of the results of privatization in China, some scholars analyzed organizational forms of privatized firms. Reading China's official statistics, the author noticed that, since privatization in China was push forward in 1997 the total number of SOEs decreased, and the number of LLCs and LLSCs increased correspondingly (see Table 9-2).

[5] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 52.

Table 9-2 Number of Industrial SOE, LLC and LLSC

Year	SOE		LLC & LLSC	
	Number (Thousand)	Change from Last Year	Number (Thousand)	Change From Last Year
1992	103.3		-	
1993	104.7	+1.4	-	
1994	102.2	-2.5	4.6	
1995	118.0	+16.2	5.9	+1.3
1996	113.8	-4.2	8.3	+2.4
1997	98.6	-15.2	13.1	+4.8
1998	64.7	-33.9	11.4	-1.7
1999	61.3	-3.4	14.2	+2.8
2000	53.5	-7.8	18.3	+4.1
2001	46.8	-6.7	24.6	+6.3
2002	41.1	-5.7	28.5	+3.9
2003	34.3	-6.8	32.9	+4.4
2004	31.8	-2.5	N.A.	
2005	27.5	-4.3	N.A.	
2006	14.6	-12.9	54.3	
2007	10.1	-4.5	61.1	+6.8
2008	9.7	-0.4	72.3	+11.2

Source: The China State Statistics Bureau, *Zhongguo Tongji Nianjian* (Statistical Yearbooks of China): 1993, p.409; 1994, pp.3, 380; 1995, pp.94, 406; 1996, pp.401, 406; 1997, pp.411, 416; 1998, pp.431, 436; 1999, p.421; 2000, pp.407, 410; 2001, p.401; 2002, p.423; 2003, p.459; 2003, http://tjsj.baidu.com/pages/jxyd/27/71/e191522a13be58249be8074530688410_0; 2005, p.499; 2006 (CD Version), Table 14-1; 2007 (CD Version), Table 14-1; 2008, p.485; 2009, p.487. All the yearbooks are published by the China Statistics Publishing House in Beijing, China. After China promulgated the Company Law in 1993, the China State Statistics Bureau began to provide the data of LLC and LLSC from 1994 to 1998, while both LLC and LLSC were listed in a category named as shareholding companies. The Bureau did not release the data of LLC and LLSC for 2004 and 2005. The SOE numbers from 2004 to 2008 do not include companies whose shares are controlled by the state, so these numbers are different with that in Table 7-1.

In 2002, Yusuf, Nabeshima and Perkins conducted a survey in privatized firms in five cities, reporting changes of organizational structure: about two-thirds of SOEs were transformed into

LLCs or LLSCs.[6] In 2006, Guo, Gan and Xu did a nationwide survey sampled from all industrial firms in China (the survey is referred to as Survey B below), and found the percentage was even higher, 84 percent. A noticeable difference between the results of the two surveys is the percentage of joint venture: in the 2002 survey it was 27 percent, whereas in Survey B it was only two percent (see Table 9-3). The difference is probably caused by the geographical distribution of the sampled firms. Survey B used a nationwide sample, but the 2002 survey only sampled in several coastal cities such as Shanghai and Guangzhou where foreign investors were very active and more joint ventures were established. Therefore, the percentage of joint venture companies in the 2002 survey might be much higher than the average in most hinterland provinces. Another problem found in the 2002 survey was that the categories of "employee shareholding" and "listed company" overlapped with LLCs and LLSCs. A listed company is certainly an LLSC; an employee shareholding company is either an LLC (if it has less than 50 shareholders) or an LLSC (if it has more than 50 shareholders), according to China's Company Law.[7] Obviously, the "listed company" and "employee shareholding" should not have been listed together with the LLC and LLSC options in the 2002 survey questionnaire. It is possible that some interviewees in the 2002 survey reported their employee shareholding companies as LLCs or LLSCs;[8] therefore, the percentage of employee

[6] Shahid Yusuf, et al, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 163. Their survey was conducted in the latter half of 2002 by China's State Statistics Bureau in five major industrial cities and seven manufacturing sectors; it collected annual data from 266 enterprises for the period from 1996 to 2001.

[7] "*Zhonghua Renmin Gongheguo Gongsi Fa* (the Company Law of the People's Republic of China)," Beijing, China, *Renmin Ribao* (People's Daily), Dec. 31, 1993.

[8] For instance, in the Garnaut et al. survey, 53 percent of employee shareholding firms reported themselves as LLCs, 34 percent as LLSCs, and thirteen percent of them were unclassified. See Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 51.

shareholding in the survey was significantly lower than the results of other surveys (e.g., the data in Table 9-1).

Table 9-3 Organizational Forms of Privatized SOEs

Types of Organizational Forms	2002 Survey (%)	Survey B (2006, %)
Limited liability company (LLC)	49	48
Limited liability shareholding corporation (LLSC)	17	36
Individual-owned	…	10
Joint ventures	27	2
listed corporation	4	…
Employee shareholding	1	…
Cooperative	0	4
Foreign owned	…	0
Other types	2	…
Total	100	100

Source: 2002 survey, Shahid Yusuf, et al, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 163, sample size was 266; Survey B, Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," *Seoul Journal of Economics*, 2008, Vol.21, No.21, 10, sample size was 898. In the 2002 survey individual-owned firms were considered LLCs, but in Survey B the two types were separated. In Survey B, listed corporations and employee shareholding companies were considered LLSCs or LLCs, but in the 2002 survey they were separate.

Analyzing organizational forms and *gaizhi* methods can provide a better understanding of the privatization process; but the more important issue is what became of the owner of the privatized firms. The author analyzed various Chinese press reports from 1997 to 2011 and found that quite a large portion of small- and medium-sized SOEs were privatized into the hands of managers; at the same time, when employees became shareholders of their enterprises, the firms

were often under managers' control and the employee shareholders eventually lost their ownership rights; from 2003 to 2009 many large SOEs were partially privatized through employee shareholding and selling shares to the public, but the state still owned the dominant share in the LLSCs and the rights of the minority shareholders were often ignored.

Table 9-4 Owner of Privatized SOEs

Types of Primary Purchasers	Survey C (2002, %)	Survey B (2006, %)
Managers	61	47
Employees	10	10
Outsiders	23	22
Listed LLSC	…	1
Joint venture	…	2
Lease	…	8
Other	6	10
Total	100	100

Source: Survey C, "*Zhongguo Siying Qiye Yanjiu Keti Zu* (the Research Group for Study of China's Private Enterprises)," "*Zhongguo Siying Qiye Diaocha Baogao* (Survey Report of Private Firms in China)," Beijing, China, *Caijing* (Finance and Economy Magazine), No.4, Feb. 20, 2003, sample size was 837 (nationwide); Survey B, Gan Jie, "Privatization in China: Experiences and Lessons," in James R. Barth, John A. Tatom, and Glenn Yago, eds. *China's Emerging Financial Markets: Challenges and Opportunities*, Berlin, Germany, and New York, NY, Springer, The Milken Institute Series on Financial Innovation and Economic Growth 8, 2008, 584, sample size was 717 (nationwide).

Two nationwide surveys conducted in China provided data about the results of privatization in China. Survey B found that 47 percent of SOEs were privatized by managers. Asking interviewees to report their real identity before privatization, a survey of private firms by

Chinese scholars[9] (called Survey C below) revealed that about 61 percent of the privatized enterprises were owned by former managers (see Table 9-4). The percentage in Survey C was higher than that in Survey B, because the compositions of the two survey samples differed: 75 percent of the sampled firms in Survey C were previously collectively-owned enterprises which were smaller than SOEs and more likely to be privatized by managers, whereas 80 percent of the sampled firms in Survey B were privatized SOEs,[10] and the collectively-owned enterprises counted only twenty percent.

In the two surveys, the percentages of employee fully owned privatized firms and of outsider privately owned firms are similar or very close. In both surveys there was an unclassified "other type" portion, which might be a blend of manager-employee ownership or of insider-outsider joint ownership.[11] It should be pointed out that in an employee fully owned firm managers usually hold a certain amount of shares; and in a manager-owned firm employees might have shares as minority shareholders, because managers may carry out an MBO under the

[9] The survey was sponsored by the United Front Work Department of the Headquarter of the Chinese Communist Party, the Chinese Association of Industry and Commerce and the Association for Studies of Private Economy. It was conducted from April to July of 2002. At the end of 2001 there were 2.03 million private firms in China; the survey collected 3,258 questionnaires, 1.6 percent of the sample population. The sample covers both privatized SOEs and privatized collective enterprises previously controlled by rural townships and city districts. All together, 26 percent of the surveyed firms were privatized enterprises, and of them one quarter were privatized SOEs, three-quarters privatized collective enterprises. See "*Zhongguo Siying Qiye Yanjiu Keti Zu* (the Research Group for Study of China's Private Enterprises)," "*Zhongguo Siying Qiye Diaocha Baogao* (Survey Report of Private Firms in China)," Beijing, China, *Caijing* (Finance and Economy Magazine), No.4, Feb. 20, 2003.

[10] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," *Seoul Journal of Economics*, 2008, Vol.21, No.21, 9.

[11] As "other type" was interpreted by Garnaut et al. in their survey. See Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 52.

cover of employee shareholding. Therefore, the percentage of firms where employees hold some shares should be higher than the percentage of employee fully owned firms.[12]

Table 9-5 Shareholding of Insider Privatization

Types of Owners	Listed Companies (%)	Non-listed Shareholding Companies (%)	
		Small- Medium Sized Companies	Large Companies
Senior Manager Only (%)	46	15	13
Senior Manager, Mid-level Management Staff and Technicians only (%)	14	25	20
Managers & Employees Both hold shares (%)	40	60	67
Total	100	100	100

Source: *Zhongguo Qiyejia Diaocha Xitong* (The Chinese Entrepreneur Survey System, CESS), "*Qiye Chuangxin: Xianzhuang, Wenti, ji Duice-2001, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Innovation in Enterprises: Current Situation, Problems and Suggested Policies-A 2001 Special Survey about Entrepreneurship)," April 2001, 17 (http://www.ceoinchina.com/Item/488.aspx). The survey was carried out during August and October of 2000. Sample size of LLSC was 573.

[12] For example, China's official labor union, the All-China Federation of Trade Union (ACFTU), conducted a nationwide survey in 2002, and the survey data showed that fourteen percent of LLSC employees and twelve percent of LLC employees held transferable shares of their own enterprises, and twenty percent of LLSC employees and twelve percent of LLC employees held non-transferable employee shares, while the majority of employees in the firms did not have any shares The Research Department of the All-China Federation of Trade Union (ACFTU), ed. *Zhongguo Zhigong Zhuangkuang Diaocha: Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Survey Data), Beijing, Chinese Workers' Press, 2006, p.1045 (Sample Size: LLC, 900; LLSC, 1,181).

Table 9-6 Managers' Shareholding

Managers' Portion in Total Shares of Shareholding Companies	Types of Shareholding Company		
	Small & Medium Firm (%)	Large Firm (%)	Listed Firm (%)
>30%	36	18	3
10-30%	25	18	11
<10%	39	64	86
Total	100	100	100

Source: *Zhongguo Qiyejia Diaocha Xitong* (The Chinese Entrepreneur Survey System, CESS), "*Qiye Chuangxin: Xianzhuang, Wenti, ji Duice-2001, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Innovation in Enterprises: Current Situation, Problems and Suggested Policies-A 2001 Special Survey about Entrepreneurship)," April 2001, 17 (http://www.ceoinchina.com/Item/488.aspx). The survey was carried out during August and October of 2000. Sample size of LLSC was 573.

According to the 2001 survey by the China Entrepreneur Survey System (CESS), in firms privatized by insiders, fifteen percent of small- and medium-sized shareholding companies and thirteen percent of large shareholding companies were completely owned by senior managers, 25 percent of small- and medium-sized shareholding companies and twenty percent of large shareholding companies were owned by senior managers, mid-level management staff and technicians, and 60 percent of small- and medium-sized shareholding companies and 67 percent of large shareholding companies were owned by both managers and workers (see Table 9-5). Moreover, in small- and medium-sized firms, 36 percent of managers held more than 30 percent of shares, and 25 percent of them held 10 to 30 percent; in large firms, eighteen percent of managers held more than 30 percent of shares, and another eighteen percent held 10 to 30 percent of shares (see Table 9-6).

Table 9-4 shows a brief picture of the results of China's privatization: less than one fourth of enterprises were privatized by domestic outsiders; joint-venture and listed companies were both a very small portion; and insider privatization dominated China's *gaizhi*, while managers prevailed over workers. Comparing the percentage of employee shareholding in Table 9-1 and Table 9-4, one may notice that, from 1998 to 2001, about one fifth of enterprises adopted employee shareholding as the main *gaizhi* method, but in 2002 and 2006 only ten percent of enterprises were mainly owned by employee shareholders. Garnaut et al. found from their 2001 survey that employee shareholding was once the dominant form of *gaizhi* in the late 1990s, but its popularity declined. The Chinese "government encourages managers to buy the majority of their firm's shares. A government guideline, for example, suggests that shares sold internally should be distributed according to rank in the order of senior management, technicians, and ordinary employees."[13] As a result, "the shares owned by middle and top management have increased rapidly. Of the 32 percent of total shares held by individuals in 2001, top management held 13 percent."[14] After 2001, MBO became more and more popular, and various approaches for MBO had been developed, as discussed in chapter eight. Survey C found that in 1997 when large-scale privatization had not yet been implemented, among owners of registered private companies, only 23 percent were previous SOE managers; but in 2002 56 percent of private companies were owned by former SOE managers (see Table 9-7). It suggests that from 1998 to 2002 a quite large portion of SOE managers became owners of privatized firms through MBO.

[13] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 54, 65.
[14] Ibid, p.116.

Table 9-7 Previous Occupation of Private Firm Owners

Occupation	1997 (%)	2002 (%)
SOE manager	24	56
Small businessman	40	15
Worker	8	9
Technician	4	6
Staff	1	4
Official	3	3
Peasant	4	2
Unemployed	1	1
Other	15	4
Total	100	100

Source: "*Zhongguo Siying Qiye Yanjiu Keti Zu* (the Research Group for Study of China's Private Enterprises)," "*Zhongguo Siying Qiye Diaocha Baogao* (Survey Report of Private Firms in China)," Beijing, China, *Caijing* (Finance and Economy Magazine), No.4, Feb. 20, 2003, sample size 837.

Unlike in Russia where employee shareholding was more or less selected by workers, in many Chinese SOEs employee shareholding was a forced arrangement by managers in order to collect funds from workers. As discussed in chapter eight, under such arrangements, managers often ignore owners' rights as employee shareholders, even though they might hold a large portion of shares. According to the director of an equity exchange office, 90 percent of buyers in transactions of privatized equity through his office were former SOE managers; the same phenomenon was reported at other equity exchange offices: "They benefited most from *gaizhi*, because as insiders with executive power they could manipulate the transformation process and the

transactions of equity, with lower price offer and priority to purchase."[15]

The above data from various sources suggests that, while small- and medium-sized SOEs were privatized, the spontaneous privatization process led to an ownership change dominated by manager privatization, accompanied by asset stripping, and there is no doubt that SOE managers have been big winners in the process. Such a result can hardly be defended by the official socialist ideology of the Chinese regime. This is probably why the government has carefully prevented any systematic and accurate official data about ownership changes being released.

Table 9-8 Largest Shareholder of Restructured SOEs

The Largest Dominant Shareholder	Largest Shareholder of All Surveyed Firms (%)	Percentage of Shares Held
State controlling LLSC	51	64
State asset management company	13	62
Employee shareholders or their funds	10	63
Private company	7	65
Domestic individual investor	7	57
State or local government office	5	70
Foreign company	1	61
Managers and their companies	5	33
Other organizations	1	42
Total	100	-

Source: Liu Xiaoxuan, and Liu Shaojia, "*Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (Research Report on SOE *Gaizhi*)," May 2005 (www.sachina.edu.cn/download.php?optype=channel&channelid*)*.

[15] Zhou Ying, "*Gaige Xin Shouyi Jieceng Diaocha: Guoqi Ganbu 'Baofu' Jiedu* (An Investigation of the New Social Group Benefiting from the Reform: Interpretation of SOE Managers' Enriching Process)," Beijing, *Zhongguo Jingying Bao* (China Management News), Jan. 5, 2004.

In China, privatization or ownership diversification of large SOEs has lasted eight years, since 2003, and its outcome is so far unclear for paucity of data and lack of transparency. In 2004, the Institute of Enterprise of the Development Research Center of the State Council conducted a survey about *gaizhi* (Survey D below).[16] Its report provides some information about the ownership structure of restructured large- and medium-sized SOEs.[17] According to Survey D, in 2004 the largest shareholders of 31 percent of restructured SOEs were individuals and private companies (see Table 9-8); when the largest shareholder of 69 percent of the firms were still state-owned LLSCs, state asset management companies or governments, their second largest shareholders were often private.[18]

[16] The survey was sponsored by the World Bank and organized by the Institute of Enterprise under the Development Research Center of the State Council of China. It was conducted from August to December of 2004. Questionnaires were distributed to 6,627 SOEs in 16 provinces and municipalities; 4,138 qualified questionnaires were analyzed, of which 2,696 were filled by the *gaizhi* SOEs. In the 2,696 restructured firms, 1,044 were owned by ministries of the central government and 1,052 by provincial governments or city governments of provincial capitals; 60 percent were large and medium-sized enterprises (of 1,147 enterprises that had completed *gaizhi* 260 were large enterprises and 427 were medium-sized ones) and 40 percent were small. The sampled enterprises included firms in manufacturing, mining, construction, transportation, and some in retail, communications, real estate, and consulting. The data colleted by the survey might contain some bias, as 23 percent of the sampled enterprises refused to fill and submit a questionnaire, most of them being fully privatized SOEs.

[17] Liu Xiaoxuan, and Liu Shaojia, "*Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (Research Report on SOE *Gaizhi*)," May 2005 (www.sachina.edu.cn/download.php?optype=channel&channelid). The research was based on the data from Survey D and its report has been internally circulated but never formally published; however, it was recently posted on the website of Sociology and Anthropology in China. Having compared the content of the posted report with a speech of one of the authors (Liu Xiaoxuan, "*Guoyou Qiye Gaige yu Chongzu* (Reform and Transformation of SOEs), a speech at the Unirule Institute in Beijing)", May 27, 2005 (http://www.unirule.org.cn/symposium/c287.htm)), the author found that the content of the posted report was reliable.

[18] Ibid.

The ownership composition of the first and second largest shareholders of the companies is shown in Table 9-9. It shows that these shareholders together controlled more than 80 percent of the shares of the companies; 31 percent of the companies were incorporated but not really privatized, as most of their shares were in the hands of state owners; 46 percent were partially privatized, while state owners remained the dominant shareholder, employees, managers, or domestic private owners held a smaller portion; and eleven percent were almost fully privatized by employees, managers and domestic private owners; foreign companies or MBOs played only a minor role in the partial or full privatization of the large- and medium-sized SOEs; and finally, among the partially or fully privatized companies, 33 percent have been touched by insider privatization, particularly employee shareholding (27 percent)—or in other words, employees held many more shares than managers.

The large enterprise managers have much less opportunities to scoop up state assets through privatization than those of the small SOEs; nevertheless, a lot of them were still able to obtain an increasing share in their companies. In 2001, 64 percent of the managers held less than ten percent of the shares of their company, and only eighteen percent held more than 30 percent of the shares (see Table 9-6); but in 2007, among managers of large companies who held shares of their company, those held less than 10 percent decreased to 38 percent, whereas those who held more than 30 percent increased to 42 percent.[19]

[19] The Chinese Entrepreneur Survey System (CESS), "*Xin Shiming, Xin Suzhi, Xin Qiwang: 2008, Zhongguo Qiyejia Duiwu Chengzhang yu Fazhan Shiwu Nian Diaocha Zonghe Baogao* (New Tasks, New Quality, and New Expectation: 2008, An Investigation about the Development of Chinese Entrepreneurship in the Past 15 Years)," April 2008 (www.ceoinchina.com/Item/968.aspx).

Table 9-9 Ownership Structure of Medium and Large Firms

Ownership Type	Percentage
Not Privatized	31
Partially Privatized	46
of which:	
State and employee	27
State and outside private owner	17
State and manager	2
Fully Privatized	11
of which:	
Manager and outside private owner	4
Employee only	3
Outside private owner and employee	2
Managers and employee	2
Other	12
Total	100

Source: Liu Xiaoxuan, and Liu Shaojia, "*Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (Research Report on SOE *Gaizhi*)," May 2005.

About fifteen years ago, the Chinese government decided to "grasp the large and let the small go." What that meant for SOEs at the time was ambiguous. After one and a half decades, the outcome of the policy has become much clearer. Ultimately, a lot of the large SOEs were partially privatized; and the small and medium-sized SOEs were released for spontaneous privatization, at least a half of them being privatized into the hands of their managers. Government offices and SOE managers have played a crucial role in manipulating the privatization process; and in many cases decisions and transactions in privatization were made behind closed doors. It seems that the Chinese government has been more interested in getting rid off the heavy financial burdens of

SOEs and the pressure of redundant workers than in promoting a transparent and fair privatization process, and in building a proper system of corporate governance for restructuring the firms. While some Chinese economists defend the process of privatization, other scholars maintain that the widespread practices of asset stripping by managers should have been prevented.[20] Criticisms of the privatization policy abound in China, particularly on the Internet and its vibrant online electronic bulletin boards.

2. Corporate Governance in Privatized Enterprises

After privatization, what kind of corporate governance was established in industrial firms? Since China promulgated the company law at the end of 1993, corporate governance has often been emphasized in the SOE transformation process. The law details every aspect of corporate governance.[21] It regulates that in LLCs and LLSCs, the shareholders' congress may approve management and investment policy and elect and change the members of the board of directors and supervisory board.[22] Yet corporate governance practices in privatized companies are far from what the regulations dictate. Nee says that, despite the formal rules specified by the Company

[20] Zhou Ying, "*Gaige Xin Shouyi Jieceng Diaocha: Guoqi Ganbu 'Baofu' Jiedu* (An Investigation of the New Social Group Benefiting from the Reform: Interpretation of SOE Managers' Enriching Process)," Beijing, *Zhongguo Jingying Bao* (The Chinese Management News), Jan. 5, 2004.

[21] Victor Nee, "Organizational Dynamics of Institutional Change: Politicized Capitalism in China," in Victor Nee and Richard Swedberg, eds. *The Economic Sociology of Capitalism*, Princeton, NJ, Princeton University Press, 2005, 61.

[22] "*Zhonghua Renmin Gongheguo Gongsi Fa* (Company Law of the People's Republic of China)," Beijing, *Renmin Ribao* (People's Daily), Dec. 31, 1993, 2-3.

Law, much of the old repertoire of organizational rules and procedures remained in place.[23]

Corporate governance, particularly the problem of governance structure under the board of directors, mainly refers to large- and medium-sized firms. The majority of privatized SOEs are small companies whose primary owners were often former SOE managers. According to China's company law, in such companies, if there are only a few owners or the company is small, establishment of a board of directors is not required.[24] Indeed, in 2002 about 40 percent of the privatized small enterprises actually did not have a board of directors.[25] Among large- and medium-sized LLCs and LLSCs, listed LLSCs are usually better regulated by Company Law and other regulations than non-listed companies, because board composition and financial situation of the listed companies are released to the public for fulfilling the disclosure requirements of stock market regulators, whereas the data of most non-listed LLCs and LLSCs are usually unavailable. Therefore, most research about corporate governance in China also focuses on listed companies.[26] The author will start discussion about China's corporate governance from the practices of listed companies; then analyze the situation in non-listed companies.

In China most listed companies have a very concentrated ownership structure. In 2001, of the total shares of 1,134 listed companies, local governments owned 61 percent and central

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[23] Victor Nee, "Organizational Dynamics of Institutional Change: Politicized Capitalism in China," 63.

[24] "*Zhonghua Renmin Gongheguo Gongsi Fa* (Company Law of the People's Republic of China)," 2.

[25] "*Zhongguo Siying Qiye Yanjiu Keti Zu* (the Research Group for Study of China's Private Enterprises)," "*Zhongguo Siying Qiye Diaocha Baogao* (Survey Report of Private Firms in China)."

[26] Zhong Ninghua, "*Zhongguo Gaizhi Qiye yu Siying Qiye de Gongsi Zhili Jiegou Bijiao: Jiyu Laizi 12 ge Chengshi de Diaoyan Shuyu* (A Comparative Study of Corporate Governance of Privatized and Private Companies in China: Based upon the Data from 12 Cities)," Beijing, *Jingji Shehui Tizhi Bijiao* (Comparative Economic and Social Systems), No.2, 2009, 160.

governments held 15 percent. Moreover, 79 percent of the firms had a parent company that may instruct the operation of the listed companies.[27] When governments are controlling shareholders of most listed companies, their goals, from political stability to personnel arrangements, influence the operation of the firms.[28] Moreover, Bai, Liu, Lu, Song, and Zhang stated that the existence of such a controlling shareholder makes transferring resources out of listed companies into parent or other related parties' accounts possible. Several corporate scandals in China's capital markets have involved unconstrained large shareholders misusing firm resources.[29]

Chinese government offices and the state controlling companies often maintain control over listed firms by appointing officials to the board of directors and to the CEO position. About half of directors of the boards were appointed by state controlling owners, and another 30 percent were affiliated with various layers of governmental agencies.[30] Analyzing the composition of the board of directors of 741 listed companies, Chen, Zhang, and Zhang found that, as of 1999, 62 percent of the board members were current managers, while most of them worked for the companies as senior managers before their firms were listed; and the chairmen of the supervisory boards were either the former senior managers and the chairmen of official labor union, or the party secretaries of the

[27] Liu Qiao, "Corporate Governance in China: Current Practices, Economic Effects, and Institutional Determinants," *CESifo Economic Studies*, Vol.52, No.2, 2006.

[28] Wang Jun, "*Shanghai Gongsi Faren Zhili Jiegou de Ruogan Wenti* (The Problems in Corporate Governance in Shanghai)," *Shanghai Gaige* (Shanghai Reform), No.9, 1999, 33.

[29] Bai Chong-En, Liu Qiao, Lu Joe, Frank M. Song, and Zhang Junxi, "Corporate Governance and Market Valuation in China," *Journal of Comparative Economics*, Vol.32, 2004, 605.

[30] Liu Qiao, "Corporate Governance in China: Current Practices, Economic Effects, and Institutional Determinants."

companies.[31] Among insider board members, many were communist party secretaries. In 1999 Gu, Li, and Gao reported that in 104 listed firms, 62 percent of party secretaries of the companies joined the board of directors, and among them about half became chairman of the board of directors.[32] Using the 2000 data of 95 percent of listed companies, Bai et al. found that more than one third of CEOs were also the chairman of the board of directors; and on average, the proportion of the insider directors on the board was 52 percent.[33] Such a large portion of insider board members is significantly higher than that in the U.S., where insider board members are usually no more than one third.[34] Fan and Wong revealed that 28 percent of CEOs and directors of the boards of 625 listed companies that went public from 1993 to 2000 were current or former bureaucrats: "When a CEO is politically connected, the board is more political but less professional: the board has more politically-connected directors (in addition to CEO) but fewer directors with professional backgrounds."[35] As of 2000, although top managers in China typically owned very

[31] Chen Xiangyong, Zhang Jianwen, and Zhang Weiwen, "*Woguo Shangshi Gongsi 'Neibu Ren Kongzhi' Yanjiu* (Research about 'Insider Control' in the Listed Companies of Our Country)," Beijing, *Guanli Shijie* (The Management World), No.4, 2000, 104-105. In 1999 there were 949 listed companies in China. Chen et al. selected 741 listed companies with complete information about board members for the analysis; the 741 companies had 7,221 board members and of them 4,448 were insiders, and the average number of the board of directors of the companies is 9.7.

[32] Gu Shutang, Li Weian, and Gao Minghua, "*Zhongguo Shangshi Gongsi Neibu Zhili de Shizheng Fenxi: Zhongguo Shangshi Gongsi Neibu Zhili Wenjuan Diaocha Baogao* (Analysis of Corporate Governance of the Listed Companies in China: A Survey Report about Corporate Governance in China's Listed Companies)," Beijing, *Guanli Shijie* (Management World), No.6, 1999, 146. The 104 firms were randomly sampled from 745 listed firms in 1997.

[33] Bai Chong-En, Liu Qiao, Lu Joe, Frank M. Song, and Zhang Junxi, "Corporate Governance and Market Valuation in China," 610.

[34] Michael Useem, "Corporations and the Corporate Elite," *Annual Review of Sociology*, Vol.6, 1980, 54.

[35] Joseph P.H. Fan, and Wong T. J., "Politically-connected CEOs, Corporate Governance and Post-IPO Performance of China's Partially Privatized Firms," *Journal of Financial Economics*, Vol.84, 2007.

little shares of their companies, they were able to extract rents from the firms through other channels, for example from excessive bonuses or gains from insider trading.[36]

In 2001 the Chinese government realized the problems of insider control of boards, and made a new request that all listed companies recruit independent outside directors to represent minority shareholders, and that such independent board members should not be less than one third of each board.[37] Since then the boards of directors of listed firms have absorbed many outside, independent board members, and the composition of the boards has somewhat changed. At the end of 2011, 2,314 domestically listed companies have appointed 7,595 independent board members, 3.3 per company. The 7,595 positions were occupied by 5,593 people, which means that on average each person works for 1.36 companies.[38]

The independent board members are mainly composed of three groups of people. First, 40 percent of the independent board members are scholars from universities and research institutes. Among them, 123 serve on the boards of four companies, 60 on five boards, and two on six boards,[39] although the China Securities Regulatory Commission regulates that an individual is

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[36] Liu Qiao, "Corporate Governance in China: Current Practices, Economic Effects, and Institutional Determinants."

[37] Huang Zhangkai, Xu Xinzhong, and Yue Yunxia, "*Zhongguo Shangshi Gongsi Dongshihui Jiegou Fenxi* (Analysis of the Composition of the Board of Directors of the Listed Companies in China," Oct. 23, 2007 (http://www.zclw.net/article/sort015/sort016/info-49777.html).

[38] Zhou Xiaoyuan, "*Shangshi Gongsi Duli Dongshi Yi Lunwei Tequen Jieceng Fuli* (The Independent Board Membership of the Listed LLSC Have Become a Kind of Benefits for a Group of Privileged People)," Beijing, China, *Renmin Ribao, Haiwai Ban* (People's Daily, Overseas Version), May 5, 2012.

[39] Ibid.

only allow to take a position of independent board members in no more than five listed firms.[40] They usually receive high annual salaries or other funds from the companies they serve. For instance, at the end of 2001, 131 economists were invited to be independent board members of 274 listed companies, and they received salaries ranging from 10,000 to 50,000 yuan or more per year; among them, many of the distinguished economists received funds or consulting fees from the companies to advertise for the firms in media, or in policy consultations with government.[41] In 2011, 45 scholars served for thirteen listed banks as outside directors of the board or members of the supervisory board; the banks paid each of them 200 to 400 thousand yuan per year, with the highest salary one million yuan per year. The independent scholar board members have good academic reputations, but do not have experience in business administration and usually do not question CEOs' decisions in board meetings. Very often, they simply attend the board meetings, raise their hands when it is the time to vote, sign receipts for salary payments, collect their money, and go home.[42] A professor of Fudan University in Shanghai served as an independent director on five boards, and was appraised by CEOs as a good independent director, because in the eyes of minority shareholders he was "independent," but, from the point of views of CEOs he

[40] Xinhua News Agency, "*Renda Jiaoshou Shen Jian 6 Gongsi Dudong, Zhengjianhui Guiding Zuiduo bu Chao 5 Jia* (A Professor from Renmin University Accepted Offers from Six Listed Firms as Independent Board Member, but China Securities Regulatory Commission Regulates No More than Five), May 26, 2012 (http://finance.sina.com.cn/stock/s/20120526/122612153898.shtml).

[41] Wu Libo, "*Zhongguo Shi Da Xuezhe Beihou de Caituan* (The Corporations behind the Ten Well-known Scholars in China)," Beijing, *Liaowang Dongdang Zhoukan* (The Outlook-Oriental Weekly), Feb. 26, 2008.

[42] Zhou Xiaoyuan, "*Shangshi Gongsi Duli Dongshi Yi Lunwei Tequen Jieceng Fuli* (The Independent Board Membership of the Listed LLSC Have Become a Kind of Benefits for a Group of Privileged People)."

was cooperative and never made any trouble.[43] The second group is former senior government officials who have now retired and receive high salaries from companies for serving on the board. At the end of 2011, about 22 percent of the 5,593 independent board members were former officials. The third group includes accountants and attorneys; 17 percent of the 5,593 independent board members belong to this group.[44] In China, whether the outside board members really play an independent role in decision making is questionable, especially as they collect outsize paychecks relative to their other income, and act as advisors or consultants to the CEOs for drumming up business or conducting public relations. There is a suspicion that much of the time their role is simply symbolic.

The problems in corporate governance of listed firms in China are more complicated than that in a market economy: the concentrated ownership by the state hinders listed companies from improving corporate governance, paid directors dominate the board of directors, and CEOs often exercise control over the board. Bai et al. point out that, according to their econometrics analysis, a large holding by one shareholder, the influence of the parent company, and the largest shareholder being the government, all have statistically significant and negative effects on market valuation of the listed companies.[45] Moreover, when more than half of the board members are current

[43] Liu Wei, and Gao Liqin, "*Xuezhe Zhadui Yinhang Dang Duli Dongshi, Zuigao Ling Xin Guo Baiwan* (A Lot of Scholars Serve in Banks as Independent Director of the Board of Directors, and the Highest Salary is More than One Million)," Guangzhou, China, *Yangcheng Wanbao* (The Yangcheng Evening), Apr. 27, 2012.

[44] "*Shangshi Gongsi Duli Dongshi Yi Lunwei Tequen Jieceng Fuli* (The Independent Board Membership of the Listed LLSC Have Become a Kind of Benefits for a Group of Privileged People)."

[45] Bai Chong-En, Liu Qiao, Lu Joe, Frank M. Song, and Zhang Junxi, "Corporate Governance and Market Valuation in China," 612.

managerial team members appointed by the CEO, and independent board members paid by the company occupy another third, the board structure offers the CEO almost exclusive authority and power. The CEO may ignore not only the interests of minority outside shareholders but also that of employee shareholders (40 percent of the listed companies had employee shareholders, see Table 9-5). Functionally, the boards of directors in the firms are more like a managerial council, rather than a body that oversees the CEO and management team on behalf of shareholders. Naughton wrote that, in 2000 when the Shanghai Stock Exchange polled managers of listed firms and asked them to identify the most important internal and external constraints on their authority, only 29 percent chose the board of directors; the second most common internal constraint, named by 26 percent of respondents, was "self-restraint," meaning that they perceived no significant internal restraints at all; and another twenty percent of the respondents identified the shareholders' annual meeting as their most important internal restraint, a factor that was unlikely to wield much influence over regular operations.[46]

Corporate governance of listed companies in China has been improving slowly since 2000. Huang, Xu, and Yue analyzed data from 1,057 listed companies from 1998 to 2003, and found that the average portion of state ownership (including state controlling companies) in the shares of firms decreased by 5 percent from 1998 to 2003; and the cases where one person was both CEO and chairman of the board decreased from 22 percent to 11 percent.[47] In 2003, the World Economic

[46] Barry Naughton, *The Chinese Economy: Transitions and Growth*, Boston, MA, MIT Press, 2007, 321.

[47] Huang Zhangkai, Xu Xinzhong, and Yue Yunxia, "*Zhongguo Shangshi Gongsi Dongshihui Jiegou Fenxi* (Analysis of the Composition of the Board of Directors of the Listed Companies in China," Oct. 23, 2007.

Forum, a Switzerland-based international organization, did a research project about corporate governance in 49 economies. China's overall ranking was 44th, slightly better than Indonesia, and worse than other Asian economies such as Taiwan, Malaysia, Thailand, and India.[48]

Listed companies in China have a long way to go in terms of further improving their corporate governance. The accounting firm Deloitte conducted a survey in 2010 by distributing questionnaires to CEOs of listed companies and collected responses from about 100 firms. It found that the firms were familiar with China's regulations about listed companies, but only six percent considered as necessary reference international standards regarding corporate governance published by the Organization for Economic Co-operation and Development (OECD); twelve percent admitted that they did not really follow China's rules regarding corporate governance; 74 percent of the firms did not properly evaluate the performance of board members, as required; in 30 percent of the firms, the supervisory board did not really function; in 38 percent the percentage of employee members in the supervisory board did not reach the required ratio (no less than one-third); 24 percent reported that concentrated ownership was a big problem; sixteen percent of the interviewed CEOs were still appointed by government offices; eighteen percent of respondents reported that external mechanisms that help improve corporate governance, such as a takeover market, legal infrastructure, and protection of minority shareholders, had only weak effects; and nineteen percent mentioned that they did not feel a sense of real competition for their positions.[49]

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[48] Liu Qiao, "Corporate Governance in China: Current Practices, Economic Effects, and Institutional Determinants," 11.

[49] Deloitte, "*Gongsi Zhili, Ren Zhong Dao Yuan: 2010 Nian Zhongguo Shangshi Gongsi Zhili Diaocha Baogao* (Corporate Governance, A Heavy Task and a Long Way to Move: Survey Report about Corporate

In recent years a lot of Chinese LLSCs were listed on the New York stock market or NASDAQ, and the rising stars were once warmly welcomed by American investors. As the Deloitte survey pointed out, most CEOs of Chinese companies do not concern themselves with international standards of corporate governance; and thus, when they come to raise capital directly from the U.S. stock market, they brought their habits developed in China with them. However, some business practices that are widely used in China may be unacceptable in the United States. After American media exposed many of these inappropriate and sometimes illegal practices, American investors started paying attention. Jackson recently warned that a growing crisis in China involving bad corporate governance needs to be addressed immediately in order to prevent a major economic crisis. "There are increasingly voices within the United States cautioning investors against buying Chinese stocks because their financials and the rules of the game for doing business cannot be trusted."[50] He points out that poor corporate governance leads to corruption, and the Chinese business elites should not be allowed to take advantage of Chinese workers through paying themselves excessive bonuses or overstating earnings. Jackson wrote: "If there continues to be

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Governance of China's Listed Companies in 2010)," 2010 (www.deloitte.com/view/zh_CN/cn/services/corgov/6b5d1fa364f18210VgnVCM100000ba42f00aRCRD).

[50] Eric Jackson, "Why Corporate Governance is So Important to China", July 6, 2011 (http://www.forbes.com/sites/ericjackson/2011/07/06/). The author introduced a lot of cases of frauds of China's companies listed on the New York Stock Market. He mentioned: "Last year, there were several Chinese-based companies who had previously chosen to go public in the United States via a process called a reverse take-over (RTO), who were accused of fraud. In the last month, two such companies — China Media Express (CCME) and China Agritech (CAGC), who both had market capitalizations over $500 million last year — were delisted from NASDAQ because they are assumed by that exchange to be somewhat fraudulent…In May, the National Audit Office of China published financial problems at 17 state-owned enterprises (SOEs). The allegations included overstating earnings, understating asset values, forging invoices, and paying excessive executive bonuses."

evidence of more widespread fraud at large and well-known Chinese companies, there will eventually be a crisis of confidence in Chinese businesses… I hope each of these Chinese boards' have sufficiently strong-willed and knowledgeable directors who are willing to challenge their CEOs..."[51] However, if the board members in China are either senior managers or the outsiders paid by the companies, could the boards come into play as foreign investors expect?

Indeed, many of the U.S.-listed Chinese companies gave false financial information to American investors or were involved in fraudulent activities. After the problems were found or exposed, rather than admit their mistakes and try to make efforts to improve corporate governance, many of the companies decided to end their short lives in the U.S. with a whimper, by simply "going dark," that is ceasing to file with the SEC, leaving their once booming but now worthless stock to American holders. After failing to file, the companies are delisted. The Chinese companies misused the trust of American investors, obtained a large amount of money from the stock market, and then disappeared. From 2011 to August of 2012, more than 40 Chinese companies were delisted from NYSE or NASDAQ, and more Chinese firms will follow them; in this way companies are able to escape from further investigation and punishment.[52]

Most LLCs and LLSCs in China are not listed on the stock market. In the non-listed companies, could previous SOE cadres dominate the boards of directors? In the U.S. a large corporation is classified as fully owner-controlled if an individual or group of related individuals

[51] Ibid.

[52] Shi Shan, "*Zai Mei Shangshi Zhongguo Gongsi Mianlin Kunjing* (Chinese Companies Listed on U.S. Stock Market Encounter Dilemma)," Washington DC, Radio Free Asia, Aug. 15, 2012 (http://www.rfa.org/mandarin/yataibaodao/h-08152012091636.html).

holds at least ten percent of the company's voting stock, or holds five percent of the stock and has strong representation on the board of directors.[53] As Table 9-6 shows, in China, the portion of shares held by managers varies. In large companies, 64 percent of managers hold less than ten percent of the shares, and, very likely, government offices hold controlling shares. In such situations, the CEO and his managerial team might not have controlling stock. However, they may maintain their seats on the board of directors by consolidating their political relations with the government offices or officials. In other words, the managers with fewer shares but better political connections might have the same opportunity to sit on the board of directors as those who hold more shares but have poorer political connections. Obviously, when government offices play both the role of owner and that of political leader, they do not need to follow the rules of the road in a private economy, by counting shares held by each board member candidate. On the other hand, in small- and medium-sized companies, 61 percent of managers hold more than ten percent of the shares, while the rest of the shares might be held more or less by employees, and the state often does not have a controlling stake; thus, managers of these companies could arrange seats of the board of directors for themselves much more easily.

The CESS conducted a survey in 1999 and reported that about 45 percent of CEOs and chairmen of the board of LLCs and LLSCs were simply reappointed former CEOs, many selected by government offices; moreover, 42 percent of the LLSC CEOs or chairmen of the boards were also the communist party secretaries of the companies.[54] While the leadership of the communist

[53] Michael Useem, "Corporations and the Corporate Elite," 46.

[54] The CESS, "*Zhongguo Qiye Jingyingzhe Duiwu Zhiduhua Jianshe de Xianzhuang yu Fazhan-2000,*

party is considered unshakable in China, such a power structure linked with the party implies that the CEOs often possess an unchallengeable authority within the companies. The Research Institute of Economic System and Management under the State Commission for Development and Reform conducted a survey in the summer of 2004 in 320 large enterprises. The survey found that only thirteen percent of chairmen of the boards of directors were elected by their board members, while 39 percent were directly appointed by government offices, and another sixteen percent recommended by governments for approval by the boards; only 22 percent of CEOs were appointed by the board of directors, but 44 percent were appointed by governments, and 24 percent were recommended by governments for approval by the boards; 68 percent of the firms did not have independent outside board members, only four percent considered such board members necessary, while only two percent thought independent outside board members could play an effective role.[55] The situation implies that CEOs' political connection to government offices is very important for their appointment, when the state has controlling shares in the companies; i.e. as long as they are politically trusted by offices of the communist party and government, they can maintain their positions in the board of directors and as a CEO, even without controlling stock.

Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao (Current Status and Institutionalized Development of Entrepreneurship in China: 2000, Special Report about Development of China's Entrepreneurship)," April 2000 (www.ceoinchina.com/Item/457.aspx). The nationwide survey was done during August and November of 1999, with a sample size of 3,562.

[55] Zhang Xiaowen, Xu Guangdong, and Wang Jianmei, "*Dui Daxing Guoyou Qiye Gufenzhi Gaige de Diaocha yu Fenxi* (Analysis Based on a Survey about Organizing Shareholding Company in Large SOEs)," March 2005 (http://theory.people.com.cn/GB/40536/3275257.html). The survey was done during June and Sept. of 2004, and its sample size was 320, of which 44 percent were listed firms.

One may also identify the role of the board of directors in China by observing its functions. According to the CESS, in 2000 only in 47 percent of LLSCs and 44 percent of LLCs was manager performance appraised by the board of directors or congress of shareholders; on the other hand, many local government offices were still involved in appraising the performance of CEOs (see Table 9-10). It is worth noting that most LLCs are small firms and have been privatized, but in 52 percent of the enterprises, manager performance was still evaluated by government offices. While the government offices habitual intervened, most managers of LLSCs had to attend meetings arranged by various government agencies about three times per week, and about half of the meetings were perceived by the managers as a waste of time.[56] In terms of who decides CEO salary and bonuses, only in 48 percent of the LLSCs and 44 percent of the LLCs did the boards of directors make the decision, whereas in 40 to 42 percent of the companies the salary and bonus were decided by government offices (see Table 9-11).

Table 9-10 Appraisers of Manager's Performance

Appraiser	LLSC (%)	LLC (%)
Government offices	41	46
Board of directors	29	29
Shareholders' congress	18	15
State assets administration office	9	6
Congress of workers and staff	2	2
Other	1	2
Total	100	100

[56] The CESS, "*Yingjie Zhishi Jingji Tiaozhan: Shiji Zhi Jiao de Zhongguo Qiye Jingyingzhe-1999, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Welcome the Challenge of Knowledge Economy: Chinese Entrepreneurs at the End of Century-1999 Special Survey about China's Entrepreneurs," April 1999 (www.ceoinchina.com/Item/450.aspx). The nationwide survey was conducted during August and October of 1998. The sample size of LLSCs was 742.

Source: The CESS, "*Zhongguo Qiye Jingyingzhe Duiwu Zhiduhua Jianshe de Xianzhuang yu Fazhan-2000, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Institutionalized Development of Entrepreneurship in China: 2000, Special Report about Growth and Development of China's Entrepreneurship)," April 2000, sample size is 3,562, of which 495 are LLSCs, and 606 are LLCs (www.ceoinchina.com/Item/457.aspx).

Table 9-11 Decision Makers of Manager's Salary and Bonus

Decision Maker	LLSC (%)	LLC (%)
Board of directors	48	44
Government office	40	42
CEO himself	3	6
Other	9	8
Total	100	100

Source: The CESS, "*Zhongguo Qiye Jingyingzhe Duiwu Zhiduhua Jianshe de Xianzhuang yu Fazhan-2000, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Institutionalized Development of Entrepreneurship in China: 2000, Special Report about Growth and Development of China's Entrepreneurship)," April 2000, sample size is 3,562, of which 495 are LLSCs, and 606 are LLCs (www.ceoinchina.com/Item/457.aspx).

In 2005, evaluating China's corporate governance, the International Finance Corporation (IFC) affiliated to the World Bank, stated in a report: most managers and boards remained unaware of basic governance procedures, often confusing governance with general management; the state-owned enterprises that were diversifying ownership on their way to becoming private enterprises suffered from a different set of governance problems; when these companies took on private ownership, they carried the legacy of the state-dominated decision making regime; they often had complex and opaque corporate ownership structures, overlapping new and traditional bodies of corporate control, and reporting practices that were focused on satisfying the information

requirements of the authorities rather than the needs of investors.[57] Analyzing the 2006 survey data of IFC,[58] Zhong pointed out that local governments regularly intervened in the operation of *gaizhi* firms, by appointing chairmen of the boards and CEOs, and that such intervention made corporate governance poor and ineffectual; corporate governance of non-listed firms could thus barely protect shareholder interests, and the firms did not respond to external mechanisms that are supposed to help improve corporate governance (a takeover market, legal infrastructure and protection of minority shareholders, etc.).[59]

As the author finds in Russia's privatization, in China many CEOs of the fully or partially privatized enterprises are the former managerial communist elite who have transformed themselves into businessmen through privatization. After *gaizhi*, many CEOs and chairmen of the board of directors did not really understand what kind of role they were supposed to play. In 2004, when most SOEs had already been privatized for years, a CESS survey asked CEOs and chairmen the question: "Let's use a metaphor, if your company were a soccer team, what kind of role should you play at your position?" About 50 percent of the interviewed chairmen of the board of directors thought they were a captain or coach, and 30 percent of the CEO respondents thought themselves

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[57] International Finance Corporation, *Step by Step, Corporate Governance Models in China: The Experience of the International Finance Corporation*, Washington, DC, April 2005 (www.ifc.org/ifcext/eastasia.nsf/AttachmentsByTitle/Governance_Pub/$FILE/Step+by+Step+final).

[58] The survey was conducted by the IFC in twelve cities in 2006 for a project about sustainable development in China's private sector. Its sample includes 101 SOEs, 248 *gaizhi* firms and 563 private enterprises. Most enterprises in the sample were non-listed firms.

[59] Zhong Ninghua, "*Zhongguo Gaizhi Qiye yu Siying Qiye de Gongsi Zhili Jiegou Bijiao-Jiyu Laizi 12 ge Chengshi de Diaoyan Shuju* (Comparative Corporate Governance of *Gaizhi* Firms and Private Firms in China: A Study Based on Survey Data from 12 Cities), Beijing, China, *Jingji Shehui Tizhi Bijiao* (Comparative Economic and Social Systems), No.2, 2009, 156-162.

club manager (see Table 9-12). Such role perceptions imply that in a lot of privatized firms, the role of the CEO and chairman of the board were mixed up; or, the CEOs and chairmen did not really mind if they played the role of the other party. The answers reflected the poor status of the corporate governance in the companies.

Table 9-12 Role Perception of CEOs and Chairmen of the Board of Directors

Role	CEO (%)	Chairman of the Board of Directors (%)
Key athlete	5	5
Captain	31	18
Couch	34	32
Club manager	30	45
Total	100	100

Source: The CESS, "*Zhongguo Qiye Jingyingzhe Jiazhi Quxiang: Xianzhuang yu Tezheng-2004, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Characteristics of Value Orientation of Chinese Entrepreneurs: 2004, Special Report about Growth and Development of China's Entrepreneurship)," April 2004 (www.ceoinchina.com/Item/789.aspx). Sample size = 3,192.

Although China's company law was revised in 1999, so far the responsibilities of the board of directors have not been defined in the law yet.[60] In many privatized firms, the board of directors often functions poorly, whereas CEO or the chairman of the board holds most power, without or with weak oversight from the board. According to the CESS 2010 survey, among the LLSCs and LLCs that have established boards of directors, the board of directors in a half of LLSCs and in 57 percent of LLCs did not really play a role in decision making or strategic issues at the companies;

[60] Ibid, 160.

instead, in 39 percent of LLSCs and 47 percent of LLCs, such decisions were made individually by CEOs or chairmen of the board of directors (see Table 9-13).

Table 9-13 Decision Makers of Strategic Issues

Decision Maker	LLSC (%)	LLC (%)
Board of directors	50	43
Chairman of the board or CEO	39	47
Managerial team	7	7
Government office	4	3
Committee of the communist party	0	0

Source: The CESS, "*Zhongguo Qiye Zhanlue, Xianzhuang, Wenti, ji Jianyi: 2010, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Enterprise Strategy in China, Current Status, Problems and Proposals: 2010, Special Report about Growth and Development of China's Entrepreneurship)," April 2010 (http://www.ceoinchina.com/Item/16713.aspx). The survey was done during Aug. and Oct. of 2009. Sample size is 5,016, of which 853 are LLSCs, and 2,433 are LLCs.

A lot of researchers emphasize the importance of rule of law and the legal environment for improvement of corporate governance. From the political and legal perspective, China is significantly different from other transition economies because it remains a country ruled by the communist party, and the party's authority is above the law. As the leadership of the ruling party and its government is so positioned, notions of the rule of law in the country have always been a question, and one cannot assume that the existence of a Company Law would effectively prevent practices that are harmful to good corporate governance. China's political system has thus greatly shaped the institutional changes during the privatization. As Nee writes, "[D]espite formal changes

embodied in the Company Law, informal rules reflecting path dependent norms and entrenched practices from the earlier era of state-owned enterprises can and do operate as oppositional norms, which combine to cause organizational inertia in these older form."[61] In China, government intervention in corporate governance of companies does not only reflect the rights of state owners in partially privatized enterprises; it also represents the need for control of an authoritarian communist state. As long as China maintains the current political system, the cessation of government intervention in corporate governance appears impossible.

On the other hand, backed up by the government, the communist managerial elite has now turned themselves into entrepreneurs, and dominated business administration of privatized companies. In smaller firms that were fully privatized, the managers hold controlling stock and rule the firms, with little need for proper corporate governance; in larger firms, the state maintains controlling shares and government intervention persists, with managers relying on political connections with the state, while exercising control over the board of directors for their own ends. In particular, it is now much easier for CEOs to manipulate asset transactions, whereas before the reform they were not allowed to arrange any asset transaction without government approval. Unlike their Russian counterparts, Chinese managers had already accumulated market experiences before privatization. Do they have strong incentives or pressure to improve their managerial skills after privatization? This question will be taken up in the next section.

[61] Victor Nee, "Organizational Dynamics of Institutional Change: Politicized Capitalism in China," 71.

3. Value Orientations, Ability and Behavior of the New Entrepreneurs

After privatization, many former SOE managers became owners of their firms and their economic status significantly improved. They often pay themselves high salaries and bonuses. In 2002, the average annual wage of the staff and workers of LLSCs was 13,850 yuan (US$1,673) and that of LLCs 11,997 yuan (US$1,449).[62] The average annual salary of LLSC managers was 151,000 yuan (US$18,241) and that of LLC managers 149,000 yuan (US$18,000),[63] ten times more than that of their workers and much higher than that of the managers of SOEs that had yet to be privatized (see Table 9-14). It is worth noting that the remaining SOEs in 2002 were usually large firms and their managers were, on average, more talented than those of the small LLCs. If considering manager quality or effort, one may argue that the salaries of small, privatized firms are not supposed to be much higher than that of large firms. However, as discussed in the last section, many managers of the small- and medium-sized privatized firms are able to dominate their board of directors, thus pay themselves high salaries. Even so, 56 percent of LLSC managers and 66 percent of LLC managers were still dissatisfied with their economic status, because they expected an even higher income (see Table 9-15).

Most of the LLSC and LLC managers had long been members of the communist elite in China. Now that they had turned themselves to capitalists, were they satisfied with their new sociopolitical status? More than half of them felt unsatisfied. They had quite high expectations of

[62] China's State Statistics Bureau, *Zhongguo Tongji Nianjian 2009* (China Statistical Yearbook 2009), Beijing, China' Statistics Press, 2009, 148.
[63] The average annual salary of LLSC and LLC managers is calculated with the data in Table 9-14.

their role in China's political environment. But such opinions by no means imply that the managers would have liked to see greater political freedoms. Actually, what they want is a higher position and bigger reputation in the party-state system. A 2007 research report about political attitudes of entrepreneurs reveals that only a small minority were in favor of the existence of multiple political parties (28 percent) and opposed the current one-party dictatorship (13 percent); with respect to the valuation of individual liberty, less than one-third favored individual liberties such as the right to demonstrate (17 percent) and the right to organize over the need for social stability (32 percent); a majority of the respondents (60 percent) were willing to defer to the decision-making authority of government leaders almost unconditionally; the capitalists surveyed showed a high level of regime support, and registered low levels of support for most measures of democratic values and institutions.[64]

Table 9-14 Annual Salary of Managers

Salary Level	LLSC Manager (%)	LLC Manager (%)	SOE Manager (%)
Less than 40,000 yuan	33	33	57
40,000 – 100,000	35	38	34
100,000 – 500,000	26	22	9
Above 500,000	6	7	0
Total	100	100	100

Source: The CESS, "*Zhongguo Qiye Jingyingzhe Jiazhi Quxiang: Xianzhuang yu Tezheng-2004, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Characteristics of Value Orientation of Chinese Entrepreneurs: 2004, Special Report about Growth and Development of China's

[64] Chen Jie, and Bruce J. Dickson, "Allies of the State: Democratic Support and Regime Support among China's Private Entrepreneurs," *China Quarterly*, No.196, Dec. 2008, 792-793, 802.

Entrepreneurship)," April 2004 (www.ceoinchina.com/Item/789.aspx). Sample size is 3,192, of which 485 are LLSCs, 1,076 are LLCs, and 833 are SOEs.

Table 9-15 Managers who were Satisfied with own Socioeconomic and Political Status

Types of Status	LLSC Manager (%)	LLC Manager (%)
Social status	45	36
Economic status	44	34
Political status	44	34

Source: The CESS, "*Zhongguo Qiyejia Duiwu Chengzhang Xianzhuang yu Huanjing Pingjia: 2003, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Environment of the Development of Entrepreneurship in China: 2003, Special Report about Growth and Development of China's Entrepreneurship)," June 2003 (www.ceoinchina.com/Item/646.aspx). The survey was done during Aug. and Sept. of 2002. Sample size is 3,539, of which 460 are LLSCs, and 1,094 are LLCs.

While their income expectations were quite high, the new capitalists admitted that only a small portion of Chinese managers were highly qualified for their job and tasks (see Table 9-16). There seemed no reason for them to disparage their colleagues or themselves; and indeed, the majority of managers trained in the *nomenklatula* culture were not good in appraising and placing personnel; their abilities in learning, expression, and public relations were even worse; their strongest ability was decision making and coordinating. After privatization, the managers made some progress in improving their innovation and learning ability, but moved forward very slowly in other aspects (see Table 9-17).

Table 9-16 Self-Evaluation of Entrepreneurs' Quality

Evaluation	LLSC Manager (%)	LLC Manager (%)
High	9	9
Fair	50	49
Low	41	42
Total	100	100

Source: The CESS, "*Zhongguo Qiyejia Duiwu Chengzhang Xianzhuang yu Huanjing Pingjia: 2003, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Environment of the Development of Entrepreneurship in China: 2003, Special Report about Growth and Development of China's Entrepreneurship)," June 2003 (www.ceoinchina.com/Item/646.aspx). The survey was done during Aug. and Sept. of 2002. Sample size is 3,539, of which 460 are LLSCs, and 1,094 are LLCs.

Table 9-17 Self-Evaluation of Manager's Ability

Evaluation of Managers' Ability	Percentage of respondents who selected the item as "my strongest ability"	
	1997	2002
Decision making	79	62
Coordinating	55	57
Innovation	24	35
Appraise and place personnel	40	31
Forecasting	30	30
Marketing	23	28
Learning	14	20
Expression	15	12
Public relations	9	10

Note: Multiple choices.

Source: The CESS, "*Zhongguo Qiyejia Duiwu Chengzhang Xianzhuang yu Huanjing Pingjia: 2003, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Environment of the Development of Entrepreneurship in China: 2003, Special Report about Growth and Development of China's Entrepreneurship)," June 2003 (www.ceoinchina.com/Item/646.aspx). The survey was done during Aug. and Sept. of 2002. Sample size is 3,539, of which 460 are LLSCs, and 1,094 are LLCs.

The author further analyzed their attitudes toward power and human relations in the workplace and found that the managers perceived “decisive decision making” and “accepting new thoughts” the most needed abilities, while “disseminating information” and “participating in employee’s discussions” the least needed abilities (see Table 9-18). Such views imply that managers are somewhat open-minded, but are used to working more on the level of their personal authority and command, paying little attention to communicating with employees.

Table 9-18 Comparison of the Most Needed Abilities of American and Chinese Managers

Manager’s Ability	Ranking of American Managers	Ranking of Chinese Managers	Answers of Chinese Private Entrepreneurs (%)
Understand others	1	5	40
Being wise	2	4	43
Accept new thoughts	3	2	65
Decisive decision making	4	1	86
Expression	5	7	27
Solicit opinions	6	8	27
Disseminate information	7	16	2
Admit mistakes	8	10	22
Participate in employees’ discussion	9	13	9
Understand technology	10	11	19
With sense of humor	11	14	8
Respect others	12	6	32
Overall planning	13	3	48
Follow rules	14	9	24
Good personal image	15	12	16
Able to do employee’s job	16	15	5

Note: Multiple choices.

Source: The CESS, "*Zhongguo Qiyejia Duiwu Chengzhang Xianzhuang yu Huanjing Pingjia: 2003, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Environment of the Development of Entrepreneurship in China: 2003, Special Report about Growth and Development of China's Entrepreneurship)," June 2003 (www.ceoinchina.com/Item/646.aspx). The survey was done during Aug. and Sept. of 2002. Sample size is 3,539, of which 2,215 are privately owned firms. The CESS did not provide the source from where they obtained the data about the views of American managers.

Perrow mentioned that the rapid economic expansion of the U.S. at the end of nineteenth century was also accompanied by ruthless treatment of workers, and success and riches were regarded both as signs of progress for the nation; changes occurred gradually from the early 20th century, along with the development of labor unions. "The ideologies of management had gone from Social Darwinism to social cooperation in about half a century." Now, when discussing qualities of management in the U.S., it is emphasized more that managers should be worthy of their authority and eager to acquire new information, having willingness to learn from subordinates and be anxious to see them develop, and be able to take criticism and acknowledge mistakes.[65] The CESS included a question in its 2003 survey to compare the abilities of Chinese managers with that of American managers (see Table 9-18). Description about the views of American managers in the report is somewhat close to what Perrow discussed. The author noticed that the sharpest difference between Chinese and American managers is the attitudes toward human relations at the workplace: American managers care more about "understanding others," "disseminating information" and "participating in employee discussions" than their Chinese counterpart, whereas many Chinese

[65] Charles Perrow, *Complex Organizations: A Critical Essay*, New York, McGraw-Hill, Inc., 1986, p.59.

managers decline to disseminate information and participate in discussions, although they do somewhat agree that they should "respect others." The attitudes of the Chinese managers suggest that they are more likely to choose an autocratic model to deal with workers. This issue will be further explored in the following sections.

In contrast to their Russian counterparts, after privatization the new Chinese capitalists had obvious advantages. They had already accumulated experience in a market-oriented economy for more than a decade before privatization was initiated, and the business environment in China did not change after privatization was done, so the Chinese new capitalists do not have to adapt to their new role in a completely unfamiliar market environment as the Russian new capitalists had to. What were the Chinese new capitalists most concerned with after privatization? Analyzing their working time distribution, the author noticed that, after the privatization the percentage of the managers who spent most time looking for new opportunities for enterprise development dropped significantly, while the percentage of those spending most time on sales and maintaining relations with government offices both increased (see Table 9-19). Such changes imply that the privatization approaches applied in China did not really produce enough incentives for the new capitalists to make efforts for the long-run performance of their enterprises, or their confidence in enterprise development through more resource input was weak; on the other hand, they paid more attention to solving short-run issues such as expanding sales or obtaining help from government offices than R&D.

In China, good relationship with government remains important to the majority of the managers of privatized firms. In their 2006 survey, Guo et al found that, after privatization, 57 percent of managers reported no changes in their relationships with governments, 23 percent reported closer relationships with governments, and only twenty percent reported more distant relationships with governments; at the same time, they many need to spend time and money due to corruption or rent seeking of government officials; on the other hand, the managers could benefit a lot from the relationships, for instance, they may directly acquire land from governments at prices lower than market prices.[66] During the period from 2007 to 2009, when asked about the distribution of their working time, manager respondents reported that about half of their time was used for internal management, 30 percent of that for marketing and investment, and about fifteen percent spent on dealing with government offices, whereas R&D and looking for new opportunities for enterprise development occupied only a very small portion.[67]

[66] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," 16-19.

[67] The CESS, "*Zhongguo Qiye Zhanlue, Xianzhuang, Wenti, ji Jianyi: 2010, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Enterprise Strategy in China, Current Status, Problems and Proposals: 2010, Special Report about Growth and Development of China's Entrepreneurship," April 2010 (http://www.ceoinchina.com/Item/16713.aspx). Sample size: LLSC, 853; LLC, 2,433.

Table 9-19 The Most Time Consuming Job
Before and After Privatization

The Most Time Consuming Job for Managers	1994 (%)	2002 (%)
Looking for new opportunities for enterprise development	43	30
Internal management	27	24
Sales	15	24
Coordinate with government offices	9	18
Construction project or technological upgrading project	4	3
Developing new products	-	-
Other	2	1
Total	100	100

Source: The CESS, "*Zai Biange Zhong Chengzhang, Zai Chuangxin Zhong Fazhan: 1993-2003, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Shi Nian Diaocha Zong Baogao* (Growing in Reform, Developing in Innovation: 1993-2003, the Growth and Development of China's Entrepreneurship in the Decade)," Sept. 2003 (www.ceoinchina.com/Item/782.aspx). The survey was done during Aug. and Sept. of 2002. The report was drawn based on survey reports done in the ten years. The sample size of 1994 survey is not provided in the 2003 report; the sample size of 2002 survey is 4,695.

In 2000, when explaining why the managers lacked incentives in R&D, 60 percent of the manager respondents reported that they did not have qualified technicians, about 40 percent did not have sufficient funds, and about 20 percent complained that in China intellectual property rights were not really protected and the risks of technological innovations being plagiarized were too high, thus the return on R&D was low.[68] When asked what factors negatively affected managers' efforts in institutional, managerial and technological innovation, more than one third of respondents said

[68] The CESS, "*Qiye Chuangxin: Xianzhuang, Wenti, ji Duice-2001, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Innovation in Enterprises: Current Situation, Problems and Suggested Policies-A 2001 Special Survey about Entrepreneurship)," April 2001 (www.ceoinchina.com/Item/488). The survey was carried out during August and October of 2000. Sample size: LLSC, 573; LLC, 1,157.

that government intervention and incomplete property right reform were the key institutional barriers; besides that, outdated laws and regulations and an underdeveloped social security system were also problems (see Table 9-20). While government intervention remains active and the legal environment imperfect, the managers may likely lack motivation in pursuing enterprise development, but seek short-run profit by cutting wages and producing low quality products. A CESS 2004 survey revealed that only about 40 percent of the interviewed CEOs considered competitive products, marketing, and better management the factors crucial to the success of their enterprises (see Table 9-21). Obviously, improvement of the business environment requires institutional transformation, but such transformation often falls behind due to the unchanged political system in China.

Table 9-20 Institutional Barriers Reported by Manager

Institutional Barrier	LLSC (%)	LLC (%)
Government intervention	38	37
Property rights reform incomplete	39	37
Social security system underdeveloped	29	30
Laws and regulations outdated	28	31
No professional entrepreneurship	29	29
Lacking motivation For innovation	22	22

Note: Multiple choices.

Source: The CESS, "*Qiye Chuangxin: Xianzhuang, Wenti, ji Duice-2001, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Innovation in Enterprises: Current Situation, Problems and

Suggested Policies-A 2001 Special Survey about Entrepreneurship)," April 2001 (www.ceoinchina.com/Item/488). The survey was carried out during Aug. and Oct. of 2000. Sample size: LLSC, 573; LLC, 1,157.

Table 9-21 Factors Crucial to Success of Enterprise

Factors	LLSC (%)	LLC (%)
High quality products with advanced technology	42	40
Strong marketing	44	41
Advanced managerial capability	36	35
Good personal background and relations	32	35
Excellent human resource	35	35
Strong managerial team	32	33
More capital or strong capability in financing	27	29
Good relations with customers	27	28

Note: Multiple choices.
Source: The CESS, "*Zhongguo Qiye Jingyingzhe Jiazhi Quxiang: Xianzhuang yu Tezheng-2004, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Characteristics of Value Orientation of Chinese Entrepreneurs: 2004, Special Report about Growth and Development of China's Entrepreneurship)," April 2004 (www.ceoinchina.com/Item/789.aspx). Sample size is 3,192, of which 485 are LLSCs, and 1,076 are LLCs.

4. Authoritarian Management-Worker Relations

After privatization, a large portion of former SOE managers became owners or controllers of their enterprises, with little to no investment of their own money, and at the same time gained the freedom to set up the organizational rules at the workplace. While privatization has obviously strengthened the position of the managers, how do the new capitalists treat their workers and how has the status of workers changed? So far these issues have not been explored in the literature on China's privatization. In this section the author will analyze employment practices, incentives for

employee and worker interaction with management, and then identify what sort of management-worker relationship is created in the privatized enterprises. Observing the practices of the majority of the managers, the author finds that, in more than half of the privatized enterprises, management-worker relations are quite similar to the authoritarian management-worker relations in Russia discussed in chapter six.

The SOE workers in China had been indoctrinated for decades with an ideological propaganda that, unlike in capitalist countries where workers are simply wage earners, says that both managers and workers are master of the enterprise. After the privatization, according to a 2002 survey by the All China Federation of Trade Unions (ACFTU), 39 percent of LLSC employees and 26 percent of LLC employees became shareholders of their companies (see Table 9-22).

Table 9-22 Employee Shareholders in LLSCs and LLCs

Types	LLSC (%)	LLC (%)
Hold transferable shares	14	12
Hold non-transferable employee shares	20	12
Hold both shares	5	2
Do not have any shares	61	74
Total	100	100

Note: The question is "Do you hold shares of your company?"
Source: The Research Dept. of the All-China Federation of Trade Union (ACFTU), ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), Beijing, Chinese Workers' Press, 2006, p.1045. Sample Size: LLC, 900; LLSC, 1,181.

Do workers feel that they now become real masters of their firms? The ACFTU survey finds that only seventeen to eighteen percent of worker respondents felt that their status at the workplace as the master of enterprise improved (see Table 9-23). Why did the workers reply so pessimistically? Indeed, since privatization was initiated in China, the status of workers began to fall. In order to liberate SOE managers from the long existing institutionalized lifetime employment of SOE workers, during the privatization process the Chinese government encouraged the managers to terminate the lifetime employment agreements by paying the workers certain amount of compensation. While workers lost their old employment status, some of them were recruited back to the same workplace, now with a fragile employment status. A large number of others were simply laid off. Among those who were recruited, many had to lower their wage and benefit expectations, including job security, medical insurance, and pension, all of which was lost. Table 9-24 shows that those SOE employees whose enterprises had not been privatized cared more about the wage amount but did not worry about the package of benefits, because in SOEs the benefits were guaranteed; however, the employees of LLCs and LLSCs cared more about benefit packages and a stable job, as benefits and job security were often not available in the companies.

Table 9-23 Workers' Self-Evaluation of Status at Workplace

Answers.	LLC (%)	LLSC (%)
Significantly decrease	28	23
Somehow decrease	27	27
No change	28	32
Somehow increase	16	16
Great increase	1	2
Total	100	100

Note: The question is "How do you evaluate the change of your status as the master of your enterprise during the past 5 years?"
Source: The Research Dept. of the All-China Federation of Trade Union (ACFTU), ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), p.1261. Sample Size: LLC, 792; LLSC, 1,031.

Table 9-24 Workers' Concerns when Seeking for Employment

Types of Concerns	1997 SOE Employees (%)	2002	
		LLC Employees (%)	LLSC Employees (%)
High income	46	22	22
Stable job	25	32	32
Benefits available	5	22	27
Opportunities for development	15	14	11
Other	9	10	8
Total	100	100	100

Note: The question is "What do you care about most when seek for employment?"
Source: The Research Dept. of the ACFTU, *1997 Zhongguo Zhigong Zhuangkuang Diaocha, Shuju Juan* (Survey of the Status of Chinese Staff and Workers in 1997: Data Volume), Beijing, Xiyuan Press, 1999, pp.1413-1414, sample size is 30,773); the Research Dept. of the ACFTU, *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 989-990. Sample size: LLC, 903; LLSC, 1183.

The author has further analyzed labor contracts, wage amounts, and welfare benefits in privatized enterprises, and found that the real situation in the firms is generally disappointing. According to a 2004 survey by the official labor union of Hubei Province, 85 percent of SOE workers lost their lifetime employment; in 60 restructured enterprises, only 52 percent of workers were recruited to employment at the same workplace; among the recruited workers, 18 percent did not have any labor contract thus could be fired at any time; among those who got a new labor

contract, 40 percent had only a one-year contract and 30 percent had labor contracts for less than three years.[69] The ACFTU 2002 survey found this phenomenon all over China, where nineteen percent of LLC workers and twenty percent of LLSC workers did not have any labor contract,[70] and, among those who had labor contracts, 27 to 30 percent were simply assigned a labor contract without any validity term (see Table 9-25). All together, 41 percent of LLC workers and 45 percent of LLSC workers were employed without the protection of labor contracts. Moreover, in some *gaizhi* enterprises, particularly in industrial towns, when both husband and wife had worked at the same workplace for years, after their lifetime employment was terminated, managers only allowed one from each family to go back to his or her job, with the excuse that cutting redundancy needed sacrifices from every family, and only the one-job-for-one-family policy could ensure that all families will survive. It was reported in summer of 2005 that, in the Northern China Old Field, many husband and wife couples had to dissolve their marriages in order to each keep their jobs; a reporter found that, when workers of the enterprise met on their way to work, instead of saying "hello," they would ask each other: "have you divorced?"[71]

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[69] Wang Sixin, and E Shengong, "*Hubei Diaocha: Gaizhi Qiye Zhigong Quanyi Zhuangkuang bu Lingren Manyi* (Status of Workers' Rights are not Satisfactory: An Investigation in Hubei Province," Beijing, China, *Gongren Ribao* (Workers' Daily), Dec. 24, 2004.

[70] The Research Dept. of the ACFTU, *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), Beijing, Chinese Workers' Press, 2006, p.958. Sample Size: LLC, 883; LLSC, 1,167.

[71] Guo Zhichun, "*Cong 'Lihun Keyi Shanggang' Xiangdao 'Zhiduxing Xiuru'* ('Get Divorced to Retain a Job': An Institutionalized Humiliation to Workers)," Shijiazhuang, China, Aug. 17, 2005, *Yanzhao Dushi Bao* (Yanzhao Urban Daily). The company was a large SOE and was transformed into a listed LLSC in 1999.

Table 9-25 Labor Contract Duration

Labor Contract Duration	LLC (%)	LLSC （%）
Without validity term	27	30
For a single task only	0	1
Less than 1 year	6	5
One to Two years	18	15
More than 2 years but less than 5 years	22	24
More than 5 years	27	25
Total	100	100

Note: 57 percent of the LLC respondents and 65 percent of the LLSC respondents worked in manufacture, 9 percent of them worked in construction and transportation industry, and the rest of them in service industry.
Source: The Research Dept. of the ACFTU, *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), Beijing, Chinese Workers' Press, 2006, 965-966. Sample Size: LLC, 718; LLSC, 927.

After the privatization, a lot of managers treated their workers ruthlessly, as if their employees were simply redundant, cheap labor, no matter whether they were skilled workers, technicians, or unskilled. They extended working hours, and cut wages and benefits. From 1997 to 2002, two thirds of the workers in foreign firms had their income increased; eighteen percent had their income dropped. Taking the wage changes as a reference, the author noticed that in 2002, about 30 percent of LLSC and LLC workers reported that their income was lower than that in 1997, 20 percent did not have any wage increase from 1997 to 2002, and only half of the workers in the privatized firms had wage increases (see Table 9-26). It seems that the red capitalists of the privatized firms treated their former worker comrades worse than managers of foreign owned firms or joint-ventures.

Table 9-26 Workers' Income

Evaluation	In 2002, compared with 1997		
	Employees of Foreign Companies (%)	Employees of LLC (%)	Employees of LLSC (%)
Decrease a lot	5	9	11
Decrease somewhat	13	19	20
No change	17	21	20
Increase somewhat	57	45	44
Increase a lot	8	6	5
Total	100	100	100

Source: The Research Dept. of the ACFTU, *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1030. Sample Size: foreign companies, 242; LLCs, 877; LLSCs, 1,150.

Moreover, in the privatized firms, after workers had done overtime work, 19 to 24 percent of them did not get any payment for the extra hours, and 40 percent of them were paid only a part of what they were due (see Table 9-27), though China's labor law regulates that extra hour wages should be paid. In other words, in about 60 percent of the enterprises managers had forced their workers to work longer with little if any overtime payment. The red capitalists reduced labor costs so they could raise profits.

Table 9-27 Overtime Work Payment

Payment Method	LLC (%)	LLSC (%)
Fully paid	30	33
Paid only a part	34	32
Did not pay at all	20	16
Did not have overtime work	16	20
Total	100	100

Source: The Research Dept. of the ACFTU, *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), p.976. Sample Size: LLC, 877; LLSC, 1,139.

In 2002, when workers of privatized enterprises were asked to compare their wages with that of other people in same city or province, about 60 percent of them considered their income was either at low or at a lower middle level.[72] According to the official labor union of Tianjin city, 47 percent of worker respondents to its 2001 survey reported that their enterprises owed them unpaid wages: among them five percent did not receive their wages for more than a year, and nine percent did not get paid for more than six months.[73] The unpaid workers even dared not to quit their jobs, because if they had left their work they could hardly have found another job and would never have received the unpaid wages. The wage cutting practices in the enterprises are seemingly not a temporary measure. Five years later, a 2007 survey of the ACFTU found that the wages of 72 percent of workers were below the average wage of all employees in China, 27 percent of them did not get wage increases from 2002 to 2007, and the monthly wages of 56 percent of them were less than one thousand yuan ($119),[74] close to the average monthly income of an employed person in the lowest income urban households of the country.[75]

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[72] The Research Dept. of the ACFTU, *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), p.1024. Sample size: LLC, 879; LLSC, 1,145.

[73] "*Tianjin Shi Zonggonghui, Shi Gonghui Guanli Ganbu Xueyuan Zhuanti Yanjiuzu* (The Research Group of the Labor Union of Tianjin City and the Tianjin Institute for Labor Union Officials," "*Kunnan Zhigong Qunti: Yige Tebie Zhide Guanzhu de Shehui Wenti* (The Workers in Financial Difficulties: A Social Problem to be Resolved)," 2001, drafted by Zheng Yunru, Wang Binqi, Xin Shizhong, Wang Haifeng, Chen Hanming and Yu Jun (http://www.edu.cn/20020401/3024011.shtml).

[74] Xia Xiaolin, "*Jiedu Quanguo Zhigong Duiwu Zhuangkuang Diaocha Zong Baogao* (Interpreting the Report of the Survey of the Status of Chinese Staff and Workers in 2007)," Feb. 19, 2009 (www.chinavalue.net/blog/BlogThread.aspx?EntryID=127552).

[75] According to China's 2007 official urban household survey, the average family income of the lowest income

Is the wage determination in privatized enterprises unique in China? The author compared the opinions of employees in privatized enterprises with that of foreign companies (owned by Westerners or businessmen from Hong Kong and Taiwan), and found that, while other factors do not have significantly different effects between the privatized enterprises and foreign companies, education of employees was much less rewarded in the former, and wage differentials between privatized enterprises was significantly greater than between foreign companies (see Table 9-28). In other words, in contrast to the managers of foreign companies, managers of privatized enterprises cared less about the contribution of employees with greater education; and the employees working for the privatized enterprises are much more likely to receive very different wages than those working for foreign companies. The privatized enterprises and foreign companies hire workers from the same labor market and the wage rate for workers with the same quality should be similar. The large wage difference across the privatized enterprises implies that some privatized firms ignore the market wage rate and purposely keep the wages of their employees low; however, their workers often have no choice but to accept those conditions, particularly if they live in hinterland provinces and do not want to become jobless and indigent; most foreign or joint-venture firms are located in coastal areas, and job opportunities in foreign firms for middle-age workers hailing from hinterland

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households (the lowest 10 percent of the sample) was 15,193 yuan (average number of employed persons per household was 1.34), and the average monthly income of an employed person in the lowest income households was 945 yuan; the average family income of the low income households (the second 10 percent of the sample) was 22,376 yuan (average number of employed persons per household was 1.55), and the average monthly income of an employed person in the low income households was 1,203 yuan. State Bureau of Statistics of China, *Zhongguo Tongji Nianjian 2008* (China Statistical Yearbook 2008), Beijing, China Statistics Press, 2008, 321.

provinces are far from abundant. In terms of bonuses, Guo et al found that, compared with non-privatized SOEs or private firms, bonuses of employees in privatized firms "appear to rely more on firm-level profits, rather than group or personal performance in determining bonuses."[76]

Table 9-28 Main Factors that Determine Wage Amount

Main Factor	Foreign Company (%)	Firms owned by HK and Taiwan Businessmen (%)	LLC (%)	LLSC (%)
Seniority	5	8	3	2
Education	19	16	9	12
Occupation	20	10	15	17
Professional capability	18	30	16	14
Relations with superiors	7	2	4	5
Achievements and Contribution	3	2	5	3
Risks and responsibility	0	0	0	1
Work unit	27	29	45	43
Other	1	3	3	2
Total	100	100	100	100

Note: The question is "Which factor do you think is the primary determinant of your personal income?"
Source: The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), pp.1052-1053. Sample Size: Foreign company, 257; HK and Taiwanese company, 106; LLC, 903; LLSC, 1,182).

The managers of privatized enterprises do not only cut the wages of their workers. Many of them also deprive workers of their rights to benefits, such as arrangements for pension and medical

[76] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," 10-11.

insurance that are set forth in government regulations.[77] According to the 2002 ACFTU survey, only 43 to 48 percent of the respondents in privatized firms reported that they could have their medical expenses fully reimbursed because their firms were enrolled in the state-sponsored medical insurance system by regularly paying the employer's part of premium, while nineteen percent of the respondents had to pay all medical expenses by themselves as they had no medical benefits at all; and about 71 to 75 percent of the respondents thought their medical benefits were either worse off or not better off after privatization (see Table 9-29).

Table 9-29 Availability of Medical Benefits and Evaluation

Medical Benefits	LLC Workers (%)	LLSC Workers (%)
Paid by medical insurance system	48	43
Part of them was reimbursed at workplace	24	25
Receive a fixed amount of subsidy for medical expenses	8	11
Not reimbursed at all	19	19
Other methods	1	2
Total	100	100
Comparing the Post-*Gaizhi* Medical Benefits with that before *Gaizhi*		
Now obviously worse off	11	13
Somewhat worse off	11	13
Not better off	53	46
Somewhat better off	22	25
Obviously better off	3	3
Total	100	100

Note: The first question is "Have your medical expenses been reimbursed?" The second question is Does the post-privatization medical expense reimbursement system make you better off or worse off?"

Source: The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), p.1087

[77] Shao Daosheng, "*Rang Shu Qianwan '40-50 dai' Gongren Wu Gong Ke Gan de Guoqi Gaizhi* (*Gaizhi* of SOE: It Led More than Ten Million of Workers 'Being Laid off'," July 28, 2007 (http://blog.sina.com.cn/s/blog_4be3ef1201000cbr.html).

(sample size: LLC, 902; LLSC, 1,184), p.1210 (sample Size: LLC, 690; LLSC, 948).

In some provinces, local official labor unions reported a much worse situation. For instance, the labor union of Tianjin city found in 2001 that, from 2,924 interviewed workers, totally 28 million yuan in medical expenses was not reimbursed, about 9,458 yuan per person;[78] and in 2008 in Anhui Province, only 24 percent of interviewed workers could have their medical expenses partially or fully reimbursed, whereas the rest of them had no medical benefits at all.[79]

When monetary incentives in more than half of the privatized enterprises have become weaker than before, workers' opportunities for development are significantly reduced as well. As shown in Table 9-30, after privatization, the training opportunities provided to workers were much less than before. While managers of the privatized enterprises talk about improvement of product quality and human capital (see Table 9-21), many of them actually do not do much of that, even though they understand that the training at workplace is an important measure of improvement.

[78] "*Tianjin Shi Zonggonghui, Shi Gonghui Guanli Ganbu Xueyuan Zhuanti Yanjiuzu* (The Research Group of the Labor Union of Tianjin City and the Tianjin Institute for Labor Union Officials," "*Kunnan Zhigong Qunti: Yige Tebie Zhide Guanzhu de Shehui Wenti* (The Workers in Financial Difficulties: A Social Problem to be Resolved)."

[79] The Anhui Province Federation of Trade Union, "*Anhuisheng Zhigong Zhuangkuang Diaocha Baogao* (Survey Report of Status of Staff and Workers in Anhui Province)," Aug. 2008 (http://yxlw.acftu.org/template/6/file.jsp?cid=15&aid=220).

Table 9-30 Employees' Training before and after the Privatization

Annual Training	1997 SOE Employees (%)	2002	
		Employees of LLC (%)	Employees of LLSC (%)
None	25	53	49
Once	31	14	13
Twice	19	12	16
Three times or more	25	21	22
Total	100	100	100

Note: The question is "How many times were you trained in the past year?"
Source: The Research Dept. of the ACFTU, *1997 Zhongguo Zhigong Zhuangkuang Diaocha, Shuju Juan* (Survey of the Status of Chinese Staff and Workers in 1997: Data Volume), p.1455 (sample size, 30,421); the Research Dept. of the ACFTU, *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), p.1108 (sample size: LLC, 902; LLSC, 1,184).

As mentioned in chapter four, pre-reform management-worker relations in the Soviet Union and China have a double faceted feature: the tension between the two parties, and the paternalistic culture that reduced the possible conflicts between them. After privatization, the role of managers as the paternal caretakers of workers has been more or less terminated or altered. A few scholars have studied the transition process of paternalism at the workplace. In 1999, when did field work in Shanghai at three joint-ventures that were transformed from SOEs, Zhang identified the management-worker relationship at an enterprise as the paternalist benevolence model, but that at another two factories as the paternalist despotism model. She states that, in the despotic model, managers rely mainly on strict labor discipline and close monitoring to exert authority; they make a few benevolent gestures (such as the possibility of promotion or expressing concern for personal

well-being) to a few key workers, but rarely take the initiative in having such exchange with the majority of workers; in the benevolent model, however, favor exchanges blur the actual conflict of interest between management and workers; instead, these practices accentuate the interdependent and cooperative side of their relations.[80] Also, Unger and Chan in their case study at an SOE in Sichuan province in 2004, found that managers still carried out the paternal caretaker role that was quite similar with the post-war Japanese model. However, the two authors admitted that after the enterprise was privatized through MBO in 2004, the paternalism approach might be abandoned by the manager-owners.[81] Certainly, one cannot exclude the possibility that the paternal caretaker model might still exist in some privatized enterprises, but the author has not found any cases of post-privatization benevolent paternalism observed or studied in China since 2004. Actually, survey data shown in this section about the conditions of workers' employment, wages, and benefits, all suggest that after the privatization at least more than half of the managers quickly eschewed the caretaker function.

Unlike Chinese migrant laborers who moved from rural to urban areas and work under harsh conditions without the consciousness of being masters of enterprise, most workers in privatized

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[80] Zhang Xiaodan, *Bargain without Union: Paternalist Labor Relations in China's Reform Era*, manuscript of Ph.D. Dissertation, Dept. of Sociology, Columbia University, July 2005, UMI Dissertation Services, No.3159768 (http://hdl.handle.net/10022/AC:P:6026), p.252.

[81] Jonathan Unger, and Anita Chan, "*Yige Zhongguo Danwei Shequ de Neibu Zhengzhi: Guoyou Qiye Zhigong Yingxiang Qiye Juece de Ge'an Yanjiu* (The Internal Politics of an Urban Chinese Work Unit: A Case Study of Employee Influence on Decision-Making at a State Owned Factory," in Feng Tongqing, ed. *Zhongguo Jingyan: Zhuanxing Shehui de Qiye Zhili yu Zhigong Minzhu Canyu* (China's Experiences: A Sociological Study of Workplace Governance and Workers' Democratic Participation in a Transitional Society), Beijing, Social Science Academic Press, 2005, 193-218.

firmd had been SOE employees and were long taught the socialist ideas about worker participation in management. Exactly as the author found in Russia, Chinese workers of privatized firms have strong desire to participate in decision making on issues related to worker interests. According to the ACFTU 2007 survey report, 96 percent of the workers thought such participation would help defend their interests, about 91 percent thought that employees should have rights and opportunities, and 71 percent expressed a desire to participate in decision making.[82] The strong desire reflects the legacy of the socialist enterprise culture that is still sponsored by the official ideology of the Chinese government. Sometimes, workers would utilize the ideology to defend their interests.[83] However, Feng points out that the Chinese managers hold a common perception that management issues do not have to be understood by workers.[84] Such a view could also be found in the CESS surveys about managers' value orientation, as the manager respondents admitted that they lacked the motivation and ability for disseminating information and discussing things with workers.

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[82] The Research Dept. of the ACFTU, "*Zhigong Duiwu Sixiang Daode Guannian*" *Ketizu* (the Research Group of "The Thoughts and Moral Views of Workers and Staff"), "*Woguo Zhigong Sixiang Daode Zhuangkuang Yanjiu* (Study about the Thought and Moral Views of Staff and Workers in China)," Beijing, *Gongyun Yanjiu* (Labor Movement Studies), No.16&17, Sept. 2008.

[83] Zhu Xiaoyang, "'Misreading' of the Law and the 'Imagined Home' in Z Factory," Armonk, NY, *Chinese Sociology and Anthropology*, Vol.38, No.1, Fall 2005, 3-41; translated from the Chinese text in Feng Tongqing, ed. *Zhongguo Jingyan: Zhuanxing Shehui de Qiye Zhili yu Zhigong Minzhu Canyu* (China's Experiences: A Sociological Study of Workplace Governance and Workers' Democratic Participation in a Transitional Society).

[84] Feng, Tongqing, "*Guojia, Qiye, Zhigong, Gonghui Zhijian Guanxi de Liangxing Tiaozheng: Shangcun Guoyou Qiye zai Gaige zhong de Zhigong Canyu Anli Yanjiu* (Positive Adjustment of the Relations among the State, Enterprise, Employees and Trade Union: A Case Study of Chinese Employees' Participation in a State-owned Enterprise)," in Feng Tongqing, ed. *Zhongguo Jingyan: Zhuanxing Shehui de Qiye Zhili yu Zhigong Minzhu Canyu* (China's Experiences: A Sociological Study of Workplace Governance and Workers' Democratic Participation in a Transitional Society), 113.

In order to analyze the decision making patterns by managers on strategic issues, the CESS categorized four decision making patterns in its 2010 survey and asked manager respondents which pattern they liked more: 1. the command pattern, where only managers make decisions; 2. the perspective pattern, when managers inspire workers with perspectives on their enterprises through interaction among CEOs, the management team, and workers; 3. the planning pattern, including the drafting of strategic plans and market analysis; 4. the participation pattern that encourages most workers to participate in decision making and to share risks, and provides incentives for innovative work to employees. The survey results show that manager respondents in privatized enterprises more valued the first two patterns, while the command pattern was chosen as the top priority and the participation pattern the least preferred. The value orientation suggests that many managers prefer the command pattern, and are much less interested in employee participation.[85]

Workers' participation in China's SOEs had been encouraged since 1981 when a regulation about establishment of the Staff and Workers' Representative Council (SWRC) in SOEs was promulgated, though the real function of SWRCs varied.[86] According to the ACFTU 1997 survey, right before large scale privatization started, SWRC existed in 84 percent of SOEs,[87] but only about

[85] The CESS, "*Zhongguo Qiye Zhanlue, Xianzhuang, Wenti, ji Jianyi: 2010, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Enterprise Strategy in China, Current Status, Problems and Proposals: 2010, Special Report about Growth and Development of China's Entrepreneurship."

[86] Feng Tongqing, "*'Zhongguo Shehui zhuanxing zhong de Qiye Zhili yu Zhigong Minzhu Canyu' Diaocha he Yanjiu Xiangmu Zhu Baogao* (Main Report on Workplace Governance and Workers' Participation in China's Transitional Economy: China's Experiences, a Sociological Study on Workplace Governance and Workers' Participation," in Feng Tongqing, ed. *Zhongguo Jingyan: Zhuanxing Shehui de Qiye Zhili yu Zhigong Minzhu Canyu* (China's Experiences: A Sociological Study of Workplace Governance and Workers' Democratic Participation in a Transitional Society), 11.

[87] The Research Dept. of the ACFTU, ed. *1997 Zhongguo Zhigong Zhuangkuang Diaocha, Shuju Juan* (Survey of the Status of Chinese Staff and Workers in 1997: Data Volume), 1539.

one third of SWRCs could really determine the use of welfare funds for employees[88] and actively evaluate CEO's performance.[89] Even though a lot of SWRCs were simply another rubber stamp, like the official labor union, it could serve as a channel for interaction and communication between managers and workers and as a platform for worker participation, if managers wanted to utilize it in such a manner. China's company law promulgated in 1993 also stipulates that when managers make decisions regarding workers' interests, and determine important issues in production and management, or draft important regulations, they should listen to the opinions of the labor union and workers.[90]

After privatization, are the SWRCs still alive, and if so how do they function? From the data in the ACFTU 2002 survey, the author found that only in 66 percent of LLCs and 72 percent of LLSCs SWRCs still existed,[91] less than the figures for 1997; about one third of worker respondents thought the information regarding important issues about production and worker interests was transparent at the workplace, and, among them, about 46 to 49 percent reported that the SWRCs regularly approved the important decisions regarding workers' interests, and 24 to 38 percent replied that they could take some actions against the managers who violated SWRC's decision, intensified conflicts with workers and undermined the stability of enterprise (see Table 9-31).

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[88] Ibid, p.1548.

[89] Ibid, p.1551.

[90] "*Zhonghua Renmin Gongheguo Songsi Fa* (The Company Law of the People's Republic of China)," Article 55, 56, 121 and 122, *Renmin Ribao* (People's Daily), Dec. 31, 1993.

[91] The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1117.

Table 9-31 Information Transparency at the Workplace

Answers to Three Questions	LLC (%)	LLSC (%)
Information Transparent		
Yes	34	37
No	32	25
Do not know	34	38
Total	100	100
The SWRC Approve Important Decisions		
Always	49	46
Sometimes	39	43
Not at all	5	5
Do not know	7	6
Total	100	100
Could Workers Take Actions against Managers?		
Yes, we can	38	24
Sometimes	20	23
No, we can't	14	10
Do not Know	28	43
Total	100	100

Note: Question 1: "Is important information transparent at your workplace?" Question 2: "If important information is transparent at your workplace, are important decisions regarding workers' interests approved by the SWRC?" Question 3: "If CEO violated the decision of the SWRC, intensified conflicts and undermined the stability of enterprise, could workers take actions against him?"
Source: The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1123 (sample size: LLC, 893; LLSC, 1,179), 1126 (sample size: LLC, 308; LLSC, 430), 1135 (sample size: LLC, 306; LLSC, 431).

The data implies that in more than 60 percent of the privatized enterprises, managers do not disseminate important information to their employees; only in about sixteen percent of the privatized companies do SWRCs work as a platform for interaction and communication between managers and workers, where the latter might participate in decision making; and only in about ten

percent of the firms are workers able to fight against the managers who seriously offended workers interests. Obviously, where the desire for worker participation is strong and the possibility of real participation very low, workers will become unhappy and unmotivated. The data about the role of the SWRS in privatized firms could be an important indicator regarding management-worker relations.

Summarizing the status of workers after privatization, the author finds that: about 40 to 45 percent of workers in privatized firms have to work without the protection of labor contracts; about a half the workers did not get wage increases from 1997 to 2002; 27 percent did not get wage increases from 2002 to 2007; about two thirds did not get full payment for overtime work; medical benefits of half of the workers were lower than in 1997; the possibility of participating in discussion of important issues regarding workers' interests is small; and about 60 percent of workers reported that at their workplaces managers decline to disseminate information to workers. The ACFTU 2002 survey shows that 44 percent of workers thought they did not benefit from *gaizhi*, and 27 percent in LLCs and 24 percent in LLSCs considered their interests injured in the process; and only less than eighteen percent of them had a little optimism about their future (see Table 9-32). While in 2002 about 25 percent of the employees of LLCs and LLSCs reported that their social status was lower than 1997,[92] the ACFTU 2007 survey found that 25 percent of Chinese workers thought their social status was even lower than five years ago, and 70 percent of them, particularly those who worked in

[92] Ibid, 1237.

the privatized enterprises, were dissatisfied with their social status.[93]

Table 9-32 Workers' Evaluation of *Gaizhi*

Evaluation	LLC (%)	LLSC (%)
Evaluation of *Gaizhi*		
My interests obviously injured	13	11
Somewhat injured	14	13
I did not benefited from *gaizhi*	44	45
Somewhat benefited	26	28
Obviously benefited	3	3
Total	100	100
Opinions about Future opportunities		
A lot of opportunities	1	2
Some opportunities	17	14
Little opportunities	31	34
Almost no opportunities	32	30
Do not know	19	20
Total	100	100

Note: Question 1: "How did *gaizhi* affect your interests?" Question 2: "Do you think you would have opportunities to improve your living and working conditions in the future?"
Source: The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1219 (sample size: LLC, 703; LLSC, 918), 1234 (sample size: LLC, 901; LLSC, 1,183).

Taking all these aspects into consideration, the author would like to point out that, at least in half of the privatized firms, managers have forced workers to accept fragile employment conditions,

[93] The Research Dept. of the ACFTU, "*Quanmian Jianshe Xiaokang Shehui Xin Zhengcheng Zhongde Zhongguo Zhigong Duiwu-'Di Liu Ci Quanguo Zhigong Duiwu Zhuangkuang Diaocha Zong Baogao'* (The Chinese Workers and Staff on Their Way to Build up a Better-off Society- 'Main Report of the Sixth Nationwide Survey of the Status of Staff and Workers')," Beijing, *Gongyun Yanjiu* (Labor Movement Studies), No.16&17, Sept. 2008, 12.

low wages, overtime work with no payment, and few benefits; at the same time as they are kept in this weak position, they are dissatisfied but have no recourse to any institutionalized channel, such as the Staff and Workers' Representative Council (SWRC) or labor union, to defend their interests. Management-worker relations in these firms take an authoritarian pattern. Such a pattern more likely exists in the privatized firms where managers became primary owners, and where the value orientation of managers has autocratic features. However, it is possible that in some workplaces, a cooperative management-worker relationship, such as that found in Russia, might be alive, though the author has not yet found such a case.

5. Despotic Management-Worker Relations Under Militarized Management

The authoritarian management-worker relationship mentioned above can be found in many societies and is not fresh to scholars of US industrial history.[94] However, in China after privatization there appeared a unique pattern of management-worker relations under a militarized management approach, which has never been explored by scholars outside China. The militarized management, or paramilitarized management as it is sometimes called, has been discussed for years in China and been adopted in many enterprises. Such an approach was originally developed by the Soviet Union during World War II, when Soviet society underwent militarization to support war needs,[95] and

[94] Richard Edwards, *Contested Terrain: The Transformation of the Workplace in the Twentieth Century*, New York, NY, Basic Books, 1979.

[95] Deborah A. Kaple, *Dream of a Red Factory: The Legacy of High Stalinism in China*, New York, Oxford University Press, 1994, 8.

large sections of the Soviet workforce were placed under military law.[96] Under this form of management factories became a battlefield: not only were military terms pervasively used in daily management and indoctrination,[97] but military discipline was employed at the workplace. For instance, working hours were fixed at twelve to sixteen hours per day; three hours compulsory overtime was introduced; and absenteeism and lateness were treated as desertion; repeated offences meant being sent to labor camp.[98] China's militarized management is obviously different. The method was not employed in Mao's era when China got involved in the Korean War. Surprisingly, China's militarized management has been developed in the peaceful years of the 21st century, with no concurrent military requirements. Bai and Fan state that the militarized or paramilitarized management in China means to introduce the organizational forms, behavioral standards, and strict control and discipline characterized by military organizations into industrial enterprise management, so workers can be guided to behave like soldiers. Under this model, orders from manager are to be implemented completely, unconditionally, and effectively. The supposed result is that the firms become more competitive.[99]

An early star of militarized management can be found in the Zaozhuang Coal Mine Company in Shandong province. This is a large company with 68,000 workers, and was partially privatized through employee shareholding in 2001. Since then, under the instruction of China's

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[96] Richard Overy, *Why the Allies Won*, New York, NY, W. W. Norton & Co. 1995, 187.

[97] Deborah A. Kaple, *Dream of a Red Factory: The Legacy of High Stalinism in China*, 8.

[98] Richard Overy, *Why the Allies Won*, New York, W. W. Norton & Co., 1995, 187.

[99] Bai Xiaoguang, and Fan Anxin, "*Shixing Zhun Junshihua Guanli, Cujin Meitan Qiye Fazhan* (Carrying out Paramilitarized Management, and Promote Development of Coal Mines)," *Cangsang* (Vicissitudes), Taiyuan, China, No.4, 2007.

Association for Thought and Political Works in Workers and Staff of Coal Mines,[100] managers of the company had worked for ten years to develop a paramilitarized management system. According to a 2005 company document, their goal is "to construct the coal mine as a military camp, and shape workers into soldiers."[101] In 2007, a slogan was hung in many workshops of the company: "control workers with military discipline; workers should follow commands like soldiers."[102] Under the paramilitarized management, workers must walk, or march, in file, raise their hands in salute to any superior upon first encounter every day, and obey all commands unconditionally, with no excuses.[103] Inspection teams pervasively check to ensure all workers follow the rules.

A worker told a reporter that various fines are levied for noncompliance. For example, if a worker cannot remember the content of the daily speech of his director, he will be fined; if a worker walks with hands behind his back, he will be fined too. Another worker said that under the paramilitarized management, workers must obey orders unconditionally. For instance, when overtime work payments were cancelled, that was an order that workers had to obey; on another occasion workers were made to extend their hours until 4 a.m. the following morning, after the regular day of work, with no overtime payment—that was another command from management that

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[100] Xinhua News Agency, "*Shandong Zaokuang Jituan Qiye Wenhua Chengwei Quanguo Shouge Wenhua Pinpai* (The Enterprise Culture of the Zaozhuang Mine in Shandong Becomes the First Enterprise Culture Model in China)," June 9, 2011 (www.mtglzx.ibicn.com/news/d177825.html).

[101]"*Zaozhuang Kuangye Jituan Gongsi Zhun Junshihua Guanli Xize* (Detailed Rules for Paramilitarized Management at the Zaozhuang Coal Mine Group" (http://www.03964.com/read/2f25d8030268899be548b137.html).

[102] Ye Tieqiao, "*'Zhun Junshihua Guanli' Jianwen* (Report about 'Paramilitarized Management')," Feb. 12, 2007, Beijing, *Zhongguo Qingnian Bao* (Daily for Chinese Youth).

[103] "*Zaozhuang Kuangye Jituan Gongsi Zhun Junshihua Guanli Xize* (Detailed Rules for Paramilitarized Management at the Zaozhuang Coal Mine Group."

they had to obey. Workers at the workplace complained that, under the militarized management, they always felt nervous and their personality and self-respect were injured. But the director of propaganda department of the company said: "Now the unemployment rate is high, the heavy pressure puts workers in a weak position, thus they dare not disobey."[104]

In 2005 the paramilitarized management of the company was recommended by the Shandong provincial government as a model of enterprise culture, and the company received a government special award for its achievements in developing the enterprise culture.[105] In June 2011 at the Zaozhuang Coal Mine a meeting organized by the Association for Thought and Political Works in Workers and Staff of China's Coal Mines was held to recommend the enterprise culture model to four hundred CEOs from coal mines all over China.[106]

Actually, the ruthless militarized management at the Zaozhuang Coal Mine is not a rare case; similar practices can also be found in the Jilin Petrochemical Company in Jilin Province.[107] Some workers of the factory revealed the management approaches applied at the workplace in a chat-room on the Internet: "According to the current disciplines of our factory, you will have to pay a fine if you chat with fellow workers, if you walk to restroom during a shop-floor meeting, if you put a

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[104] Ye Tieqiao, "*'Zhun Junshihua Guanli' Jianwen* (Report about 'Paramilitarized Management')."

[105] "*Qiye Wenhua Gushi, Zaozhuang Kuangye Qiye Wenhua Jianjie* (Stories about Enterprise Culture: A Brief Introduction of the Enterprise Culture of the Zaozhuang Coal Mine)," 2005 (http://www.cec-ceda.org.cn/huodong/2005qywh/31.htm).

[106] Xinhua News Agency, "*Shandong Zaokuang Jituan Qiye Wenhua Chengwei Quanguo Shouge Wenhua Pinpai* (The Enterprise Culture of the Zaozhuang Coal Mine in Shandong Becomes the First Enterprise Culture Model in China)," June 9, 2011 (www.mtglzx.ibicn.com/news/d177825.html).

[107] The enterprise was partially privatized twice in 1994 and 1999 and has been a listed LLSC, see "Jilin Petrochemical Company of China Petrochemical Group," (www.cnpc.com.cn/cnpc/cyqy).

wiping rag in an incorrect place, or if you sit on a chair with one leg on the other, or your arm on the back of the chair…"[108] Also in Jilin Province, at the Tonghua Steel Company, managers of the privatized firm employed corporal punishment and fines to discipline workers.[109]

Militarized management has been a heated issue in China. In November 2010 it was reported that on China's Internet there were 1.6 million pages about militarized management, and 1.5 million pages about paramilitarized management.[110] Although there are no precise numbers about how many privatized enterprises have adopted a militarized or paramilitarized management approach in China, the author found that the approach is becoming popular recently in the energy industry, including coal mining,[111] power supply,[112] and in some firms in other industrial sectors as well;[113]

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[108] Guo Songmin, "*Miandui Jilin Shihua Gaogao de Moguyun* (When the Mushroom Cloud Arose)," Nov. 15, 2005 (http://news.xinhuanet.com/comments/2005-11/15/content_3783385.htm).

[109] Wang Jianjun, "*Tonggang Beiju de Luoji* (The Logic behind the Tragedy at the Tonghua Steel)," Beijing, *Liaowang Xinwen Zhoukan* (The Outlook News Weekly), Aug. 10, 2009.

[110] Dong Boya, "*Zhongguo Qiye Zhun Junshihua Guanli Xiang Hechu Qu* (Where would the Paramilitarized Management Move Forward?)," Aug. 9, 2011 (www.globrand.com/2011/522916).

[111] Bai Xiaoguang, and Fan Anxin, "*Shixing Zhun Junshihua Guanli, Cujin Meitan Qiye Fazhan* (Carrying out Paramilitarized Management, and Promote Development of Coal Mines);" "*Hegang Shi Meikuang Qiye Shixing Zhun Junshihua Guanli* (Coal Mines in Hegang City Carried out Paramilitarized Management)," Beijing, *Guoji Meitan Wang* (International Coal Newsnet), June 7, 2007 (http://coal.in-en.com/html/coal-20072007060799861.html); Deng Likui, "*Shishi Zhun Junshihua Guanli, Goujian Tese Qiye Wenhua* (Carrying out Paramilitarized Management, and Constructing Special Enterprise Culture in the Yanzhou Coal Mine Group)," Beijing, *Zhongguo Meitan Gongye* (China's Coal Mining Industry), No.3, 2009, 69-70; Qujing City Government of Yunnan province, "*Qiling Qu 50 Hu Meikuang Qiye Shixing Junshihua Guanli* (50 Coal Mines in Qiling District Carry out Military Management)," Dec. 9, 2009 (http://yx.xxgk.yn.gov.cn/canton_model1/newsview.aspx?id=695229); Su Li, "*Jin Mei Jituan Tuixing Zhun Junshihua Guanli* (Shanxi Coal Mine Group Carries out Paramilitarized Management)," Aug. 23, 2012 (http://www.china-cdt.com/news/networktalk/11989888.html).

[112] "*Nancheng Xian Gongdian Gongsi Shixing Junshihua Guanl* (Power Supply Company of Nancheng County Carries out Militarized Management)," Beijing, *Zhongguo Nong Dian Wang* (China's Rural Power Supply Newsnet), Mar. 5, 2009 (http://www.sp.com.cn/dlsc/aqscdt/200903/t20090305_118403.htm); Sheng Yongli, "*Tuixing Zhun Junshihua Guanli, Cujin Qiye Wenjian Fazhan* (Carrying out Paramilitarized

and more and more firms have adopted the approach in recent years.

While emphasizing the efficiency of executing an order from CEO or foreman, the militarized management treats workers as slaves or working machines with no self-esteem, even though many of the employees are shareholders of their company. Many Chinese scholars point out that workers are not soldiers, and firms are not military barracks; militarized management could foster hatred against managers, and is very unlikely to produce enthusiasm, innovation, or loyalty. The author would like to point out that, just fifteen years ago, the same managers often repeated that the workers were the master of their enterprise; however, after privatization the workers suddenly fell into a status completely different with where they were before, whether they held shares in the enterprise or not. For the workers, privatization followed by despotic management was not simply an ownership change; it was a distressing culture shock. The despotic militarized or paramilitarized management inflames tensions between workers and managers, but workers are unable to mount a challenge because their position was weakened through the battery of measures described above, and further, because militarized management enjoyed the support of the authoritarian government.

Management, and Promoting Steady Progresses of Enterprise)," Chengdu, China, *Sichuan Gongren Bao* (Workers' Daily in Sichuan), June 14, 2010; Zhu Weiguo, "*Cong Junshihua Guanli Kan Qiye Guanli* (The Implication of Militarized Management in Enterprise Management)," Sept.20, 2010 (http://www.china-cdt.com/news/networktalk/11989888.html).

[113] "Zhengzhong Technology Blended the Militarized Management Element into the Enterprise Cultural Construction Process and Won the Applause of the Servicemen," Dec. 21, 2010 (http://1.69yc.com/zzkejie2/news/html/?5.html).

6. Labor Disputes and Labor Conflicts after Privatization

During and after privatization, tension between managers and workers has become enduring in China. Managers often infringe on the rights of workers, but the latter cannot count on the official labor unions for help, nor organize their own labor organization to defend their interests. Unlike in Russia, China's Constitution and laws do not allow workers to organize or attend strikes or demonstrations, and offenders can encounter sever punishment. It is therefore reasonable to assume that Chinese workers are subsequently less likely to participate in protests or demonstrations. However, during and after privatization, a huge number of labor disputes were not resolved in China, and caused many labor protests and demonstrations, some of which were large in scales. Labor conflicts in China have reflected the nature of authoritarian management-worker relationships and that of China's authoritarian political rule.

China's official statistics show that, from the mid-1990s when China began its enterprise reform and privatization, labor disputes dramatically increased: in 1994 the labor disputes processed by the Labor Disputes Arbitration Committees at the county or city level all over China numbered 19,000 cases; in 1995 the number was 33,000;[114] it increased to 447,000 in 2006,[115] and further to

[114] "*Laodong Zhengyi Anjian Dafu Shangsheng* (Cases of Labor Disputes Rapidly Increasd), *Zhongguo Gaige Bao* (China Reform News), Aug. 27, 1996.

[115] Zhang Yanning, and Chen Lantong, eds. *2007 Zhongguo Qiye Laodong Guanxi Zhuangkuang Baogao* (The Status of Labor Relations in China's Enterprises: A 2007 Report), Beijing, the Press for Enterprise Management, 2007, 107. The number was provided by the Ministry of Labor and Social Security, and can also be found in Ching Kwan Lee's *Against Law: Labor Protests in China's Rustbelt and Sunbelt* (Berkeley, CA:

690,000 in 2008.[116] Labor disputes between laid-off workers and SOE managers have drawn the attention of scholars outside the country,[117] but labor disputes in privatized enterprises have not been carefully analyzed. In the mid-1990s, from 38 to 44 percent of the labor disputes occurred in restructuring SOEs,[118] while millions of SOE employees were laid off; after the privatization of small-SOEs was almost done, the ratio dropped to 20 percent since 2003,[119] but the total number of cases taking place in *gaizhi* firms rapidly increased from 19,000 in 1996[120] to 63 thousand in 2005.[121]

University of California Press, 2007), 44.

[116] Yang Lin, "*Laozi Maodun Youhuan* (Worries about Labor Disputes)", Beijing, *Liaowang Xinwen Zhoukan* (The Outlook News Weekly), No.50, Dec. 14, 2009.

[117] Chen Feng, "Subsistence Crises, Managerial Corruption and Labour Protests in China," *The China Journal*, No.44, 2000, 41-63; William Hurst, and Kevin J. O'Brien, "China's Contentious Pensioners," *China Quarterly*, No.170, 2002, 345-360; Jonathan Morris, Sheehan Jackie, and John Hassard, "From Dependency to Defiance? Work-Unit Relationships in China's State Enterprise Reform," *Journal of Management Studies*, Vol.38, No.5, 2001, 697-717; Lee Ching Kwan, "The 'Revenge of History': Collective Memories and Labor Protests in Northeastern China," *Ethnography* 1/2, 2000, 217-37, and "From the Specter of Mao to the Spirit of the Law: Labor Insurgency in China," *Theory and Society*, Vol.31, No.2, 2002, 189-228; Dorothy Solinger, "The Potential for Urban Unrest: Will the Fencers Stay on the Piste?," in David Shambaugh, ed., *Is China Unstable?* Armonk, M.E. Sharpe, 2000, 79-94, and "Chinese Urban Jobs and the WTO," *The China Journal*, No.49, 2003, 61-88.

[118] Wang Zhenqi, "*Woguo Laodong Zhengyi Chuli Zhidu Huifu Shi Zhounian Jiankuang* (Brief Review of Labor Dispute Arbitration in the Past Ten Years)," Beijing, *Zhongguo Laodong Kexue* (Labor Relation Studies in China), No.10, 1997.

[119] Zhang Yanning, and Chen Lantong, eds. *2006 Zhongguo Qiye Laodong Guanxi Zhuangkuang Baogao* (The Status of Labor Relations in China's Enterprises: A 2006 Report), Beijing, The Press for Enterprise Management, 2006, 87.

[120] Wang Zhenqi, "*Woguo Laodong Zhengyi Chuli Zhidu Huifu Shi Zhounian Jiankuang* (Brief Review of Labor Dispute Arbitration in the Past Ten Years)."

[121] Zhang Yanning, and Chen Lantong, eds. *2006 Zhongguo Qiye Laodong Guanxi Zhuangkuang Baogao* (The Status of Labor Relations in China's Enterprises: A 2006 Report), 83, 87.

According to a survey by the ACFTU, from 1998 to 2002, in about thirteen to fourteen percent of privatized enterprises, labor disputes took place, mainly caused by workers' grievance against privatization practices and employment and wage issues (see Table 9-33). From other sources it can also be found that China's spontaneous privatization often caused labor disputes. In the first half of 1997, 51 percent of the labor disputes in Shanghai took place in *gaizhi* firms, primarily with regard to privatization practices and termination of labor contracts.[122] In 1998, among 6,035 labor disputes in Shandong Province, 51 percent occurred in SOEs, due to lay-offs or possible dismissal if workers refused to buy shares of their enterprises, and unpaid wages and pensions.[123] According to the Henan provincial government, in 1998, 53 percent of labor dispute cases took place in *gaizhi* firms; most of the disputes related to *gaizhi* practices, while some SOE managers laid off workers or removed workers so managers would be able to sell the land, buildings, and equipment of the enterprises, often taking the opportunity to terminate labor contracts.[124]

Feng and Zhao point out that privatization seriously depressed workers' incentives; they are frustrated with the increasing pressure of the constantly growing work load, deteriorating working

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[122] Liao Mingtao, and Hua Shanqing, "*Jiti Laodong Zhengyi he Tufa Shijian de Zhuyao Tedian he Chuli Yanjiu* (Main Features and Resolutions of Collective Labor Disputes and Conflicts)," Shanghai, China, *Shanghai Gongyun* (The Workers' Movement in Shanghai), No.3, 1998, 12.

[123] The Labor Dispute Division of the Labor Office, Shandong Provincial Government, "*1998 Nian Shandong Sheng Laodong Zhengyi Jixu Cheng Dafudu Shangsheng Qushi* (The Continuous Trend of Rapidly Growth of Labor Disputes in Shandong Province in 1998)," Beijing, *Laodong yu Zhengyi* (The Labor and Disputes), No.5, 1999.

[124] The Arbitration Division of the Labor Office, Henan Provincial Government, "*Laodong Zhengyi Xingshi Yanjun, Gongshang Zhengyi Youwei Tuchu-1998 Nian Henan Sheng Laodong Zhengyi Chuli Qingkuang Fenxi* (The Serious Situation in terms of Labor Disputes: A 1998 Analysis of the Labor Dispute Cases in Henan Province)," Beijing, *Laodong Zhengyi Chuli* (The Labor Disputes and Resolution), No.4, 1999.

conditions, threats of being laid off, unemployment, and poverty; and the relationship between management and workers continues to deteriorate.[125] The widespread labor disputes and labor conflicts have drawn social attention in China. Several Chinese sociologists report that, in a 2002 urban public opinion survey, about 53 percent of interviewees agreed that "labor conflicts are becoming more and more serious in China."[126]

Table 9-33 Labor Disputes in Privatized Enterprises

Frequency of Disputes and Reasons	LLC (%)	LLSC (%)
Frequency		
Four times or more	3	2
Three times	1	2
Twice	4	4
Once	5	6
None	87	86
Total	100	100
Reasons		
Gaizhi	31	18
Employment and unemployment	17	10
Wage and benefits	34	43
Pension	1	4
Other insurance	3	3
Working conditions	0	1
Managers' corruption	3	5
Workers' rights	0	2
Labor contract	3	7
Other reasons	8	7
Total	100	100

[125] Feng Tongqing, and Zhao Minghua, "Workers and Trade Unions under the Market Economy: Perspectives from Grassroots Union Cadres," Armonk, NY, *Chinese Sociology and Anthropology*, Vol.28, No.3, 1996, 5.

[126] Li Peilin, Zhang Yi, Zhao Yandong, and Liang Dong, *Shehui Chongtu yu Jieji Yishi: Dangdai Zhongguo Shehui Maodun Wenti Yanjiu* (Social Conflicts and Class Consciousness: Study of Current Social Problems in China), Beijing, Social Sciences Academic Press, 2005, 182.

Note: Question 1: “How many times did collective labor disputes take place in your enterprise during the past five years?” Question 2: “What were the reasons of the latest collective labor disputes at your workplace?”
Source: The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1186 (sample size: LLC, 902; LLSC, 1,183), 1190 (sample size: LLC, 105; LLSC, 163).

Table 9-34 Resolution of the Labor Disputes

Resolution Channels and Results	LLC (%)	LLSC (%)
Channel for Disputes Resolution		
Consultation between workers and managers	26	21
Conciliation by government offices	17	13
Negotiation	1	1
Arbitration by government offices	8	5
Litigation	1	2
Intervention by government offices	14	14
Other	4	4
No channel at all	29	40
Total	100	100
Result		
Problem fully resolved	10	23
Problem partially resolved	19	15
Problem not resolved at all	71	62
Total	100	100

Note: Question 1: “What channel was the latest collective labor dispute at your workplace placed in for resolution?” Question 2: “What is the final result of the labor dispute between you and your manager?”
Source: The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1196 (sample size: LLC, 112; LLSC, 164), p.1177 (sample size: LLC, 31; LLSC, 52).

In 2002, when labor disputes took place, workers either negotiated with managers or looked for help from government offices for resolution (if the offices took the claims); rarely would they

pursue their interests through legal channels. In about 30 to 40 percent of the labor disputes, the workers could find no channels for dispute resolution, very likely because managers refused to negotiate and the related government offices declined to intervene; on the other hand, even after both parties to the disputes negotiated, or government offices intervened, the percentage of fully resolved disputes was quite low (see Table 9-34). Since 2002, the situation seems to have improved a little. The ACFTU 2007 survey found that about 32 percent of labor disputes were not resolved at all and 43 percent were only partly resolved.[127]

Why were so many labor disputes not resolved? A research fellow of the ACFTU recorded a case in which a labor dispute ended without any positive result in an SOE in Beijing: before the Chinese Spring Festival of 1995, each manager of the enterprise received several thousands yuan as bonus, but workers got nothing; angry workers went to the manager's office, however, their grievances were ignored; thus the workers started a strike for two days; the managers then threatened that anyone who refused to work would be punished by a 200 yuan fine, and the fine could increase as long as the strike continued; finally the workers had to stop the strike and the managers compromised by reducing the fine to 50 yuan.[128] Because any independent union activities are banned in China, and the official labor unions work for the government and managers, the right of workers to strike and protest are not legally protected, courts are not independent from

[127] The Research Dept. of the ACFTU, "*Woguo Zhigong Sixiang Daode Zhuangkuang Yanjiu* (Study about the Thought and Moral Views of Staff and Workers in China)," 2008.

[128] Feng Tongqing, "*Qiye Gaige Zhong Gongren de Zizun- Dui Yizhong Gongren Shehui Xingdong de Kaocha* (The Esteem of Workers during Enterprise Reform: A Review about Workers' Social Actions," Beijing, *Dangdai Shijie yu Shehui Zhuyi* (The Contemporary World and Socialism), No. 4, 2001, 21.

the communist party, and the government often takes a biased position favorable to management. Chinese workers have thus been in a severely weak position, and do not have many options in labor disputes. A Chinese sociologist has pointed out that organized collective action is usually not workers' first choice, because they are aware of the threat of being punished, and many would rather get a free ride from the workers that do dare to get involved in a struggle against management.[129]

The Chinese government declares that the Chinese Constitution does not allow workers to organize strikes.[130] However, when workers' grievances and discontent accumulated, their claims were rejected and some worker activists were able to mobilize their fellow members. In those cases, labor disputes can ignite street protests, despite the fact that strikes and protests violate China's laws, and workers run high risks for their actions.

Since the mid-1990s, labor discontent or unresolved labor disputes often led to protests. In 1994 there were about 10,000 demonstrations, strikes and protests of laid-off SOE employees in China; from January to September of 1996, two million workers joined 1,500 demonstrations in more than 120 cities, and during that period there were 1,700 strikes in SOEs; in the first four months of 1997, more than two million people joined strikes and demonstrations in 230 cities of 25 provinces and municipalities;[131] and in 1998 such protests involved four million workers.[132] Many

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[129] Liu Aiyu, *Xuanze:Guoqi Biange yu Gongren Shengcun Xingdong* (Choices: State-owned Enterprises Reform and the Workers' Subsistence Action), Beijing, Social Sciences Academic Press, 2005, 281-284.

[130] "*Laodong Bu: Gongren Wuquan Zuzhi Bagong* (The Minister of Labor: Workers Do not Have the Rights to Organize Strikes," New York, NY, *Shijie Ribao* (The World Journal Daily), July 16, 1994.

[131] Shi Kaiming, "*Dalu Gongchao Fasheng Lu Jinnian Shenggao* (the Rise of Labor Protests in Mainland China in Recent Years)," Taipei, Taiwan, *Lianhe Bao* (The United Daily), July 18, 1997; quoted from Chiang

of the protest participants were workers at privatized enterprises. A research fellow of the ACFTU pointed out that, before privatization, in order to survive many workers chose to suppress their indignation;[133] but, the 2007 survey of the ACFTU found that, if there was any labor dispute at their workplaces, 61 percent of workers wanted to participate in protests.[134]

As the Chinese regime insists on media control,[135] and the ACFTU and its branches at different administrative levels decline to openly discuss the issue, systematic information about the labor protests in China has never been available for research. Hurst has pointed out, "[T]here are no public quantitative data on the frequency, intensity, or types of workers' protests; but from sporadic media reports, scholars' field observations, and leaked internal estimates and reports, we know that there were at least hundreds, probably thousands, of episodes of laid-off workers' contention in China every year between about 1998 to 2008."[136]

According to a recent report by China Labor Bulletin (CLB), from 2001 to 2011, the main approach by workers' is to strike. Although the official ACFTU encourages workers to take an

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Chenchang, "*Xiagang Zhigong yu Dalu Gongchao Wenti* (Laid-off Worker and Labor Protests in the Mainland China)," Taipei, Taiwan, *Zhongguo Dalu Yanjiu* (Mainland China Studies), Vol.40, No.11, 1997, 76.

[132] *South China Morning Post*, Hong Kong, March 26, 1999.

[133] Feng Tongqing, "*Qiye Gaige Zhong Gongren de Zizun- Dui Yizhong Gongren Shehui Xingdong de Kaocha* (The Esteem of Workers During Enterprise Reform: A Review of Workers' Social Actions," Beijing, *Dangdai Shijie yu Shehui Zhuyi* (The Contemporary World and Socialism), No. 4, 2001, 19.

[134] The Research Department of the ACFTU, "*Zhigong Duiwu Sixiang Daode Guannian" Ketizu*" (the Research Group of "The Thoughts and Moral Views of Workers and Staff)," "*Woguo Zhigong Sixiang Daode Zhuangkuang Yanjiu* (Study on the Thought and Moral Views of Staff and Workers in China)," 15.

[135] Details of media control in China and how media workers make efforts to break it up are discussed by He Qinglian, *The Fog of Censorship: Media Control in China*, published by Human Rights in China, a New York-based human rights organization, in 2008.

[136] William Hurst, *The Chinese Worker after Socialism*, Cambridge, UK, Cambridge University Press, 2009, 108.

alternative approach through collectively negotiating with managers, among 553 cases of workers' collective actions the CLB has not found any case in which the collective negotiation approach was adopted and helped resolve the problems.[137]

Most of the workers protests were suppressed. Very often the activists in the strikes or protests were arrested; some of them were even sentenced in prison for years. According to the reports of media based in Hong Kong and Taiwan, Fang listed fourteen large scale labor protests of SOE workers or laid-off workers in six municipalities and provinces, from March 1997 to January 1998.[138] The protests were caused either by the privatization practices of SOE managers or by unpaid wages and lay-off subsidies. Among the fourteen events, the largest demonstration took place in Mianyang city of Sichuan Province and involved about 100,000 workers, and in the conflict between the demonstrators and police about 100 workers were wounded by armed police, and more than 80 arrested.[139] A report of the CLB also lists fourteen labor protests taking place between January 2005 and July 2006, the smallest protest in those cases involved about a hundred workers, and the largest had about ten thousand participants. The protests were caused by workers' disapproval of privatization practices (for instance, managers sold a factory with low price to a private company for profiting), complaints against the lay-off policy and low compensation for that,

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[137] The China Labor Bulletin, *Gongren Jiti Xingdong Shiyi Nian: Jiyu 533 ge Ge'an de Fenxi* (Workers' Collective Actions in the Past Eleven Years: Analysis Based on 553 Cases), Dec. 2011 (www.clb.org.hk).

[138] Fang Shan, "*Dalu Guoqi Gaige xia de Shiye Zhuangkuang* (The Status of Unemployment in the SOE Reform of China)," Taipei, Taiwan, *Zhongguo Dalu Yanjiu* (The Mainland China Studies), Vol.41, No.8, 27.

[139] Chiang Chenchang, "*Xiagang Zhigong yu Dalu Gongchao Wenti* (Laid-off Workers and Labor Protests in the Mainland China)," Taipei, Taiwan, *Zhongguo Dalu Yanjiu* (The Mainland China Studies), Vol.40, No.11, 78.

and against corruption of their managers in privatization; some of the protests were suppressed violently.[140] One of the best in-depth case analyses about such protests was contributed by Lee, as she introduced the background, process and consequences of a well-known labor protest at the Liaoyang Ferro-Alloy Factory.[141]

In order to learn more about labor protests in privatized enterprises, the author analyzed 26 cases that took place from 2002 to January 2012 (see Appendix of this chapter).[142] Such cases are rarely reported by media in China; of the 26 cases, only one was reported; when workers' strikes, protests, and demonstrations took place, in most situations local governments would prohibit journalists from reporting on them, and even cut wireless and Internet services to prevent the dissemination of the event information. Therefore, the 26 cases are only a group of examples of such events, where information was leaked out, whereas more protests and strikes were almost certainly covered up by government. Of the 26 cases, that took place in fourteen provinces (out of 31 provinces and municipalities China), all were rooted in the schemes or consequences of the privatization of the enterprises, and were caused by lay-offs due to privatization (eleven cases),

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[140] The China Labor Bulletin, *Zhongguo Gongren Yundong Kaocha Baogao, 2005-2006* (Report about China's Workers' Movement, 2005-2006), May 2007 (www.clb.org.hk).

[141] Lee Ching Kwan, *Against Law: Labor Protests in China's Rustbelt and Sunbelt*, Berkeley, CA: University of California Press, 2007, 101-111.

[142] During the period, the author regularly visited several web sites based in the US and Hong Kong which often have their own sources to report such events, i.e. the website of Radio Free Asia, the Epoch Times, and the China Labor Bulletin; at the same time, the author also found several non-official web sites in China that may report labor protests, and monitored the posts on the web sites everyday, as such posts might be deleted within days once they were found by China's cyber police. The cases colleted from the latter are often reported by participants or their friends and relatives, and are not formally reported by media outside China. Only the cases with precise event date (when), place (where), participants (who), reason (why), details about process and consequences (how) are recorded for the analysis.

managers' asset stripping (six cases), delayed or unpaid redundancy compensation (four cases), MBOs (three cases), and income disparity between managers and workers (two cases). The protests were usually mobilized through workers' personal networks; and no informal or formal labor organizations were established for the protests, nor were any workers elected as protest leaders. Even though the protests were not well organized, half of the 26 cases could be classed as large-scale protests, while each of them had more than 1,000 participants. Very often, during the protests, managers were rude to workers and refused to negotiate (twenty cases); nine protests were violently suppressed by police; and only in four cases did management and local governments compromise, and the protesters meet some of their goals. In the other cases they were unsuccessful.

Privatization practices in China have encountered resistance from workers in many places, but their voices are often ignored by the state and managers. Workers do not necessarily oppose privatization; however, they are dissatisfied with the privatization practices that benefit managers at the costs of workers. According to Feng and Zhao, workers are particularly concerned with two issues: firstly, they demand that they should be genuinely consulted before any reform program is implemented or tried out; secondly, workers earnestly hope for a say in the selection of enterprise managers.[143] Such ideas have reflected workers' consciousness about their rights in privatization and their concerns in terms of social justice, and are quite similar to the wishes of Russian workers. Reading the materials about workers' protests, the author finds that in most of the cases the workers

[143] Feng Tongqing, and Zhao Minghua, "Workers and Trade Unions under the Market Economy: Perspectives from Grassroots Union Cadres," 42.

complained of the privatization schemes that were arranged behind closed doors by managers and government officials, and were only released at the last minute, making workers furious. If workers enjoyed freedom to strike and demonstrate, there would have been many more labor protests and spontaneous privatization would have moved forward with much greater difficultly.

Political pressure and the lack of independent labor organization are the two reasons why workers in China often fail to defend their interests in privatization. Having collected some cases of labor protests during the period from 1999 to 2001 and done interviews in China, Chen points out that workers' protests in China are not a kind of social movement; instead, they are simply gatherings mainly against the lay-offs by and corruption of managers; most of the actions are not guided by labor organizations and have no leaders.[144] "They do not take a clear organizational format and many of them can be easily defused by a government promise of a couple of *yuan* as compensation."[145] Hurst also believes that the labor protests in China could hardly be strategically constructed by movement leaders, if there are any, in the way often described in social movement literature.[146] The author thinks that the labor protests in China might be considered a type of unorganized collective action. The difference and similarity between these actions and other collective actions based on unorganized interests in China[147] can be explored in another research.

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[144] Chen Feng, "Industrial Restructuring and Workers'Resistance in China," *The Modern China*, Vol.29, No.2, 2003, 237-262.

[145] Chen Feng, "Privatization and Its Discontents in Chinese Factories," *China Quarterly*, No.185, 2006, 47.

[146] William Hurst, *The Chinese Worker after Socialism*, Cambridge University Press, 2009, 116.

[147] Zhou Xueguang, "Unorganized Interests and Collective Action in Communist China," *American Sociological Review*, Vol.58, No.1, 2003, 54-73.

During the privatization, what position did the official labor unions take and what kind of role did they play? In China, official labor unions exist both in enterprises and in governments at different administrative levels. According to the ACFTU 2002 survey, in 83 to 85 percent of privatized enterprises there were labor unions.[148] However, the enterprise labor unions have been in a very awkward position, as operations of the labor unions have to rely upon financial support from their enterprises, and officials at the labor unions are appointed by CEOs. Thus, labor union officials usually do not dare offend managers; moreover, while many CEOs are also communist party secretaries of enterprises, union officials have no choice but to listen to the CEOs, because politically the absolute leadership of the communist party demands that union officials obey party secretaries.[149] An interpretation of an enterprise labor union official well clarifies the meaning of obeying the party: when an interviewer mentioned that "now the priority of the labor union is supposed to defend the rights of…," the labor official responded, "Defend whose rights? We have to defend the power of the party!"[150] Occasionally, some labor union officials have tried to fight for workers' rights in labor disputes, but they are often punished by CEOs. For example, in an LLSC in Guangzhou, workers found that the shares owned by labor collectivity were quietly transferred to the hands of the CEO, and then began raising questions about the legality

[148] The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1264.

[149] Feng Tongqing, and Zhao Minghua, "Workers and Trade Unions under the Market Economy: Perspectives from Grassroots Union Cadres," pp.16, 44.

[150] Feng Tongqing, ed. *Zhongguo Jingyan: Zhuanxing Shehui de Qiye Zhili yu Zhigong Minzhu Canyu* (China's Experiences: A Sociological Study of Workplace Governance and Workers' Democratic Participation in a Transitional Society), 2005, 128. In Chinese, both rights and power are pronounced as *quanli*.

of the process; Lei Hanping, the deputy CEO and chairman of the labor union of the factory, chose to stand on the side of workers; weeks later, he was suddenly fired by the CEO of the company with the excuse that he had gathered a crowd and made trouble.[151]

Enterprise labor unions in China usually play the role as a part of the management body, and official labor unions at different administrative levels take the role of quasi-governmental organizations. Based on his research into the role of labor unions, Chen points out that the state wants the official labor union officers to relax workers' dissatisfaction and eliminate their resistance, and at the same time prevent any independent labor associations from being organized; when the official labor unions get involved in arbitration, they usually only deal with the cases between individual workers and management, but avoid arbitration in matters of workers' collective actions against management, or the privatization decisions of governments.[152] In Shanghai, where labor protests were much less observed, the official machinery and electronic engineering labor union office of the city introduced its experiences, tracing sensitive issues at workplaces that were politically sensitive to the government, colleting and analyzing information about workers' attitudes, finding potential sources of labor disputes or conflicts for the government, and working hard to prevent any incidents from taking place.[153] The model labor union was thus like an extended arm of

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[151] "*Guangzhou: Weiquan Nan, Yi Gonghui Zhuxi Wei Gongren Shuohua Diu 'Fanwan'* (Guangzhou: It's So Hard to Defend Workers' Rights, as the Chairman of a Labor Union Spoke for Workers then Lost His Job)," June 15, 2007 (http://news.xinhuanet.com/local/2007-06/15/).

[152] Chen Feng, "Between the State and Labour: The Conflict of Chinese Trade Unions' Double Identity in Market Reform," *China Quarterly*, No.176, 2003, 1006-1028.

[153] Xinhua News Agency, "*Shanghai Jidian Gonghui: Guanyu Jianli Laodong Guanxi Yujing Jizhi de Shijian yu Sikao* (The Machinery and Electronic Engineering Labor Union of Shanghai: Practices and Thoughts about Establishing an Alarming Mechanism in Terms of Labor Relations," Beijing, *Neibu Canyuan* (The Internal

the party, meant to control and manage workers rather than represent them.

In China, although workers continuously complain about their low wages, reduced benefits, poor working conditions, and bad relations with managers, and sometimes even express their grievances through protests or demonstrations, the necessary mechanism to effectively protect their rights and interests have yet to be institutionalized in China,[154] and workers are kept in a weak position. Under these conditions, the possibility of improving manager-worker relations seems slim.

7. The Nationwide Lay-off Policy and the Fate of Laid-off Workers

Labor conflicts in China during and after the privatization are more complicated than that in Russia. They are observed not only at the workplace between managers and workers, but also at the front door of government offices when laid-off employees protest against their previous managers. Unlike in Russia where the government did not implement an official large-scale lay-off policy, the Chinese government has carried out a nationwide lay-off policy in SOEs to pave the way for privatization, thus initiating a unique type of labor conflict between managers and former SOE employees outside the workplace. Chapter seven and eight already discussed the lay-off policy, and how the Chinese government requests *gaizhi* firms to take care of the needs of laid-off workers. This section will analyze these arrangements further.

Reference), No.4, 1999, 17-21.

[154] The American Center for International Labor Solidarity, "The Struggle for Worker Rights in China," Washington DC, Dec. 2004 (www.solidaritycenter.org/files/JusticeforAllChinaFrontMatter).

The lay-off policy of the central government did not have any clear target in terms of how many SOE workers should be laid off. Carrying out the policy, some local governments distributed lay-off quotas to each SOE. The CLB found that, in order to achieve the layoff targets, SOE managers used many deceitful tactics to force workers to sign "agreements to voluntarily terminate their labor contract;" the tactics that were often used included notifying workers that the factory was about to go bankrupt or to be closed, and if workers terminated their labor contracts as soon as possible there would be a compensation available, otherwise they would get nothing whatsoever. Several years after *gaizhi*, some laid-off workers realized that their companies had not closed or gone bankrupt, but rather had achieved a gradual improvement, and those workers still employed there were better off. This led to labor disputes and protests against the managers of their former workplaces for requests of reemployment.[155]

Regarding the numbers of laid-off workers, "government statistics are murky and often presented in a way that suggests that the numbers are not all that large."[156] Estimates of the numbers vary. At the end of 1997 an official source admitted that there were twelve million laid-off workers;[157] according to a survey of the State Statistics Bureau, 70 percent of the laid-off workers were 25 to 40 years old;[158] at the end of 1998 only about 40 percent of the laid off workers were

[155] China Labor Bulletin, "Speaking out: The Workers' Movement in China (2005-2006)", Hong Kong, *CLB Research Reports* No.5, Dec, 2007, 17 (www.clb.org.hk/en/files/File/research_reports/).

[156] Dorothy Solinger, "Labor Market Reform and the Plight of the Laid-off Proletariat," *China Quarterly*, No.170, 2002, 304.

[157] Information Office of the Ministry of Labor of China, *Gongyun Cankao Ziliao* (The Reference Materials for Workers' Movement), No.3, 1998.

[158] Yang Yiyong, *Shiye Chongji Bo: Zhongguo Jiuye Fazhan Baogao* (The Shock of the Unemployment Wave: A Report about China's Employment), Beijing, China Today Press, 1997, 234.

reemployed;[159] in June 2002 it was reported that the total number of the laid-off SOE employees reached 26 million, among them 51 percent were unemployed for more than three years at an average age of 50;[160] and in September of 2001, a Chinese journalist reported that since the early 1990s more than half of the 80 million SOE employees were laid off.[161]

The large-scale lay-off policy suddenly raised the urban unemployment rate to a very high level. Feng Lanrui predicted in early 1998 that, including 45 million laid-off workers and those to be laid off, and 137 million redundant laborers in rural areas as well, China's unemployed would soon reach 183 million, making the unemployment rate as high as 28 percent.[162] After conducted a survey in five cities in 2002, Giles, Park and Cai reported their findings: in the cities, the unemployment rate for working-age adults (aged from 16 to 60) increased from seven percent in January 1996 to thirteen percent in November 2001.[163] In 2004, He pointed out that China's official urban employment data actually included millions of people who did not work in any economic sector (54 million in 1999 and 63 million in 2000); deducting the "working-nowhere" number from the official employed working population, she reported that China's real unemployment rate in 2000

[159] The Research Group of "SOE Reform and Development" under the Research Center of the State Council for Development, "*Tuoshan Jiejue Guoqi Xiagang Renyuan Fenliu Wenti* (Carefully Resolve the Lay off Issues)," Beijing, *Zhongguo Jingji Shibao* (The China Economic Times), Aug. 16, 1999.

[160] Hu Yifan, "*Chengzhen Dengji Shiye Lu: Bingshan Yi Jiao* (Unemployment Rate: The Facts Different from the Official Data)," Beijing, *Caijing* (Finance and Economy Magazine), No.18, Sept. 20, 2002, 30.

[161] Jiang Xueqin, "Fighting to Organize," Hong Kong, *The Far Eastern Economic Review*, Sept. 6, 2001, 72-75.

[162] Feng Lanrui, "*Disan Ci Shiye Gaofeng Jijiang Daolai* (The Coming Third Unemployment Peak)," Beijing, *Xinxi Cankao Bao* (The Information Reference), Apr. 6, 1998.

[163] John Giles, Albert Park, and Cai Fang, "How has Economic Restructuring Affected China's Urban Workers," *China Quarterly*, No.185, 2006, 67.

was twenty percent.[164] Analyzing official data, I find that, when China experienced its economic boom in 2008, the real unemployment rate of the country is actually as high as 25 percent.[165]

In order to lessen the unemployment pressure, the Chinese government decided to expand enrollment in colleges and graduate schools in 1999; so young surplus labor could be absorbed into college campuses. From 1999 to 2004, enrolling students in colleges increased from four million to thirteen million; but, after the students graduated, the oversupply of college graduates has caused a rapid fall off in wages, if they manage to find jobs.[166]

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[164] He Qinglian, "*Weiquan Tongzhi xia de Zhongguo Xianzhuang yu Qianjing* (Current Situation and Perspectives of China under Authoritarian Rule)," Princeton, NJ, *Dangdai Zhongguo Yanjiu* (Modern China Studies), Vol.11, No.2, 2004, 39-40.

[165] In China's official employment data, the total employed population in 2008 is 775 million. Deducting those who are hired by various organizations or are self-employed from the number, the author finds that 95 million in the official figure of the urban employed population (302 million) are not hired by any organization, nor are they self-employed. The 95 million could be considered the urban unemployed population hidden in official employment figures. Deducting the hidden unemployed population from the official figures of urban and rural employed population, the author gets a number of real employed population, 680 million (207 million in urban areas, and 473 million in rural areas). The author then divides 680 million by 901 million of the population between 15 and 64 years old (66 million students in high schools, colleges, specialized secondary schools, vocational senior secondary schools, and technical schools have been excluded), and estimates that China's real unemployment rate is 25 percent. It should be mentioned that the official rural employed population actually defines all laborers in rural population cohorts between 15 and 64 years old as either self-employed or hired, even though many of them are actually unemployed. So the 25 percent of unemployment rate might be an underestimate. In recent years, a shortage of young migrant labor from rural areas has often been reported. The phenomenon is not contradictory to the high unemployment rate, because it is only a shortage for a special cohort of working population, i.e. the unmarried young migrant labor from rural areas who can work long hours for low wages under poor working conditions at factory assembling lines in coastal areas; the shortage does not affect the oversupply of labor in other cohorts of population. See *Zhongguo Tongji Nianjian 2009* (China's Statistics Yearbook 2009), 90, 112-113, 792.

[166] Zheng Zuoshi, "*Daxue 'Kuozhao' Zhengce Chutai jiqi Yingxiang* (The Implementation of Policy for 'Expanding College Enrollment' and its Impact)," Guangzhou, China, *Nanfengchuang* (the Window for the Wind from South), No.2, 2006.

As unemployment rate has been high, the reemployment opportunities for laid off workers became quite small. A deputy minister of China's Ministry of Labor and Social Security admitted that the reemployment rate of laid-off workers decreased quickly from 50 percent in 1998 to 30 percent in 2001, and further down to nine percent in the first six months of 2002.[167] The high unemployment rate and low reemployment rate implied that laid-off workers can hardly find jobs and rely upon social security payments from their previous workplaces for survival. While most of the laid-off workers were still at working age, 38 percent have completed education in technical schools, high schools, and colleges,[168] and have families to support. However, in many cities neither governments nor managers of their previous work units provided sufficient unemployment benefits.

Obviously, the lay-off policy is supposed to be carried out after a necessary social security system has been established, and the system should include at least four parts: unemployment benefits, low income family allowance, pensions, and medical insurance. China had a low income family allowance system with very little resources, but the system did not provide support to laid-off workers because the lay-off policy regulated that they were not supposed to be detached from their previous workplaces and should be taken care of by their former managers. The Chinese central government started its experiments in establishing the pension and medical insurance system in

[167] Zhao Xiaojian, Hu Yifan, Huang Peijian, and Zhu Xiaochao, "*Jujiao Zai Jiuye: Zhuangfang Laodong he Shehui Baozhang Bu Fu Buzhang Zhang Xiaojian* (Focusing on Reemployment: An Interview with Zhang Xiaojian, the Deputy Minister of the Ministry of Labor and Social Security)," *Caijing* (Finance and Economy Magazine), No.18, Sept. 20, 2002, 29.

[168] Wang Chengying, *Zhongguo Zai Jiuye* (Reemployment in China), Chengdu, China, Sichuan University Press, 1998, 17.

1995, but the experiments moved forward very slowly and made only limited progress.[169] Because the central administration controlled a major portion of tax revenues but was reluctant to contribute funds that the social security system needed,[170] accomplishment of the mission of developing the social security system could only rely upon the willingness and available financial resources of local governments. As a lot of local governments did not have sufficient financial resources to cover the expenses of the social security system, they simply set the task aside. The central administration addressed the issue of operating an unemployment benefits system for years since the mid 1990s, in most cities and provinces the promise was more or less like lip service during the peak years of unemployment when millions of SOE employees were laid off.[171] As the necessary services of the social security system were not really available for the laid-off workers, not only were the workers confused about available resources for survival, but managers also had no idea how they could help laid off workers obtain social security benefits (see Table 9-35), if any were available.

[169] More details could be found in William Hurst's *The Chinese Worker after Socialism*, Cambridge, UK, Cambridge University Press, 2009, 60-85.

[170] Wang Chengying, *Zhongguo Zai Jiuye* (Reemployment in China), ii.

[171] Lu Peng, "*Zhidu shi Ruhe Fengbi de*? *Yi Guoyou Qiye Xiagang Zhigong Shehui Baozhang Zhidu de Shiji Yunxing Weili* (How the Institutions Became Dysfunctional: The Case of Social Security System for the Laid-off Workers)," originally published on *Xuehai* (Broad in Learning), Beijing, No.1, 2006; posted on *Shehuixue Renleixue Zhongguo Wang* (Website for Sociology and Anthropology in China, Jan. 9, 2008 (http://www.zggr.cn/article/2008/0109/article_579.html).

Table 9-35 Perceptions of SOE Managers about Unemployment Benefits

Perceptions	Percentage
Know nothing about unemployment benefits	21
Know the concept but have no idea about the related regulations	12
Could not identify unemployment benefits from pension	41
Know concept and regulations about unemployment benefits	12
Did not answer	14
Total	100

Source: Wang Chengying, *Zhongguo Zai Jiuye* (Reemployment in China), Chengdu, China, Sichuan University Press, 1998, 233.

When the government-sponsored social security system was not available in most cities, the lay-off policy of the central administration and local governments suggested that "one has to take care of his own babies."[172] The policy words then popularly used in government offices implied that the laid-off workers' former managers were responsible for paying the workers a certain amount of living subsidies for three years;[173] on the other hand, the governments did not guarantee the necessary funds for paying the subsidies if the enterprises lacked financial resources. Therefore, many privatized enterprises chose their own "Three-No policy" (no payment for pension insurance, no payment for medical expenditures, and no payment for other social security insurance to the laid off workers),[174] and paid their laid-off workers only very little money, barely enough to cover the

[172] Wang Chengying, *Zhongguo Zai Jiuye* (Reemployment in China), p.ii.

[173] The Research Group of "SOE Reform and Development" under the Research Center of the State Council for Development, "*Tuoshan Jiejue Guoqi Xiagang Renyuan Fenliu Wenti* (Carefully Resolve the Lay off Issues)."

[174] Wang Shuiping, "*Zeng Yige 'Guannian' Liaode* (Was It the Fault of the Laid-off Workers)?" Beijing,

minimum needs of the laid-off workers' families. To avoid paying the living subsidies, some privatized enterprises even arranged their workers to retire early and informally,[175] at the age of 45 for females and 50 for males;[176] thus the early retired workers fell into an extremely difficult situation when neither the governments nor the previous work units were responsible to pay any money for their survival.[177] In 2001, the official labor union of Tianjin city revealed that 65 percent of laid-off workers did not get financial compensation and help for reemployment from their previous workplaces, though such arrangements were required by the central administration's lay-off policy.[178]

Most laid off workers in China were plunged in the depths of misery. When the government pursued reducing a large amount of SOE employees, many of the laid-off workers were treated not simply as redundant labor but also as redundant lives, and very often found no financial support for

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Zhongguo Gaige Bao (China Reform News), Oct.16, 1997.

[175] Lu Peng, "*Zhidu shi Ruhe Fengbi de*? *Yi Guoyou Qiye Xiagang Zhigong Shehui Baozhang Zhidu de Shiji Yunxing Weili* (How the Institutions Became Dysfunctional: The Case of Social Security System for the Laid-off Workers)." The informal retirement practice in China is named as "internal retirement", which implies that the workers were actually forced to retired early, but their enterprises refused to pay the employer's portion to the state-sponsored pension system, thus the governments don't recognize these workers as qualified pensioners and the retired workers couldn't receive any pension.

[176] Zhang Ruiying, and Zhang Guoxiang, "*Yikao Shehui Ge Fangmian Liliang, Qianfangbaiji Zuohao Xiagang Zhigong Zai Jiuye Gongzuo* (Trying to Improve Reemployment Services with Helps of Various Social Sources)," originally published in *Gonghui Gongzuo Tongxun* (Labor Union Bulletin), No.1-2, 1998, cited from *Gongyun Cankao Ziliao* (The Reference Materials for Workers' Movement), Beijing, No.3, 1998, 14.

[177] Lu Peng, "*Zhidu shi Ruhe Fengbi de*? *Yi Guoyou Qiye Xiagang Zhigong Shehui Baozhang Zhidu de Shiji Yunxing Weili* (How the Institutions Became Dysfunctional: The Case of Social Security System for the Laid-off Workers)."

[178] The Research Group of the Tianjin Labor Union and the Tianjin Institute for Management, "*Kunnan Zhigong Qunti: Yige Zhide Tebie Guanzhu de Wenti* (The Workers in Financial Difficulties: A Social Problem to be Concerned with)," 2001, drafted by Zheng Yunru, Wang Binqi, Xin Shizhong, Wang Haifeng, Chen Hanming, and Yu Jun (http://www.edu.cn/20020401/3024011.shtml).

their survival; they had to live on limited savings or the help of relatives. In 1997 an official nationwide survey found that less than 30 percent of laid-off workers could count on their previous workplaces for a minimal, basic living.[179] Another survey reported that in 1997 only four percent of laid-off workers got some financial support from governments, and 27 percent received living subsidies from their pervious workplaces.[180] Moreover, a lot of the enterprises owed the laid off workers unpaid wages, medical expenses that were not reimbursed, and the individual investments in the enterprises.[181] According to a Chinese scholar, at the end of 1996, in the families of the laid-off workers who were yet to be reemployed, the average monthly income per household was only $36 (298 yuan), while the income of 59 percent of the households was from the still-employed spouses, and only 30 percent of the income was paid by their previous workplaces.[182] The official labor union of Henan Province found in 1996 that, in 6,508 interviewed laid-off workers, 34 percent had to sell their durable goods and cut daily family expenses for survival, 20 percent lived on money given by relatives, and only three percent received unemployment subsidies.[183] In the end a

[179] Wang Chengying, *Zhongguo Zai Jiuye* (Reemployment in China), 19.

[180] "The Research Group for the Survey about Re-employment of the Urban Laid-off Workers," "*Kunjing yu Chulu: Guanyu Woguo Chengzhen Qiye Xiagang Zhigong Zai Jiuye Zhuangkuang Diaocha* (Paradigm and the Way Out: the Survey about Re-employment of Urban Laid-off Workers in China)," Beijing, *Shehuixue Yanjiu* (Sociological Research), No. 6, 1997, 31.

[181] The Research Group of "SOE Reform and Development" under the Research Center of the State Council for Development, "*Tuoshan Jiejue Guoqi Xiagang Renyuan Fenliu Wenti* (Carefully Resolve the Lay off Issues)."

[182] Wang Chengying, *Zhongguo Zai Jiuye* (Reemployment in China), 17-19.

[183] Xu Ming, ed., *Guanjian Shike: Dangdai Zhongguo Jidai Jiejue de Ershiqi ge Wenti* (The Critical Moment: The Twenty Seven Problems Need to be Resolved Urgently in Today's China), Beijing, The Press for Today's China, 1997, 253.

number of laid-off workers that could find no way to survive simply committed suicide.[184]

The municipal government of Shanghai, China's largest industrial center, has much more in the way of financial resources than other local governments; and, in contrast to other cities or provinces, the Shanghai municipal government made the greatest progress to establish a government-sponsored social security system. Shanghai's pension system was established in 1993, and by mid-1997 it covered 95 percent of work units. The medical insurance system in Shanghai began in 1995 and by 2001 the system was well established. "Several interviewees in the Shanghai municipal government admitted, however, that the programs' costs were extremely high. At least two State Council officials went so far as to say that it was 'fundamentally impossible' to apply the Shanghai model of comprehensive social security almost anywhere else due to insufficient funds."[185] It has to be pointed out that even in Shanghai the system of unemployment benefits was not properly developed, as it served only for a one-time relief payment.[186] While in the city laid-off workers had more opportunities to receive subsidies from their previous workplace than in other

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[184] Han Dongfang, *Gaige yu Geming Weiji: Han Dongfang yu Zhongguo Gongren Duihualu* (Reform and the Crisis for Revolution: The Record of the Dialogue between Han Dongfang and Workers in China), Hong Kong, the China Labor Bulletin, May, 2000, 24. The China Labor Bulletin is a Hong Kong-based Chinese dissident labor organization. In the course of conducting phone interviews with workers in China, one worker mentioned a suicide that took place in January of 1998 in his neighborhood. According to the interviewee, both the husband and wife were laid off workers and were receiving only 60 yuan ($7) per month for themselves and a school child. They exhausted their savings and could no longer borrow from relatives. As they didn't eat meat for months, the husband stole a piece of meat from a peasant, and was caught and beaten. When the peasant heard the misery of the family, he gave him some meat; after their final meal the three family members hung themselves.

[185] William Hurst, *The Chinese Worker after Socialism*, 74.

[186] Zhang Laimin, "*Shanghai Chubu Xingcheng Shehui Baozhang Tixi Jiben Kuangjia* (Shanghai Has Established a Primary Framework for Social Security System)," Beijing, *Jingji Ribao* (Economic Daily), June 19, 1997.

cities or provinces (see the last section of chapter eight about shell companies in Shanghai), the amount they got was small. A survey revealed that about one third of the laid-off workers in Shanghai received less than $24 (200 yuan) per month, and eight percent of received only nine USD (80 yuan).[187] Analyzing the data from the China Urban Labor Survey conducted at the end of 2001 in five large cities,[188] including Shanghai, Giles, Park and Cai conclude that most laid off workers did not receive other benefits (health insurance, pension contributions) as promised, and most received no help from re-employment centers in learning new skills or finding new jobs; even for workers lucky enough to receive subsidies, the amounts received were often relatively small.[189]

Although the problems in terms of the poor fate of laid-off workers are not all the fault of managers, the tension between laid-off workers and the managers of their previous workplaces would certainly produce negative effects on the management-worker relationship of the privatized firms. This unique issue should never be ignored when one studies privatization in China and analyzes its social consequences.

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[187] "*Zhua Hao Zai Jiuye Gongcheng Zhongdian, Jiejue Zui Kunnan Xiagang Zhigong* (Grasp the Key Point of Reemployment Project, Solve the Most Difficult Problems for the Laid-off Workers)," *Zhongguo Gaige Bao* (China Reform News), May 8, 1997.

[188] The survey was done by the Institute of Population and Labor Economics of the Chinese Academy of Social Sciences, with the aids of provincial and municipal offices of the State Statistics Bureau. John Giles, Albert Park and Cai Fang collaborated in the survey design and execution of the survey.

[189] John Giles, Albert Park, and Cai Fang, "How has Economic Restructuring Affected China's Urban Workers," *China Quarterly*, No.185, 2006, 93-94.

8. Performance of the Privatized Enterprises

Since privatization was done, the Chinese government has never officially published any survey report about the performance of privatized enterprises or workers' morale and attitudes. China's media has not published any systematic report regarding the issue either. It seems that the Chinese government does not want the public to discuss the issue at all. However, the government allows scholars outside mainland China to conduct research projects on China's privatization and the performance of privatized enterprises for an international audience. These survey reports have provided various evaluations.

Yusuf, Nabeshima and Perkins have researched the effects of privatization in China.[190] Through econometric analysis, they found that the restructuring effort itself did not seem to improve the efficiency of the privatized firms, and the actual impact of restructuring was quite limited.[191] Garnaut, Song, Tenev and Yao also assessed the impact of the restructuring (*gaizhi*) on the performance of the privatized enterprise.[192] They find a declining trend of profitability in the *gaizhi* firms; when focusing on the performance of the privately owned firms, the authors observed a fluctuation pattern, i.e., the profitability of the enterprises dropped during the period from 1995 to

[190] Shahid Yusuf, Kaoru Nabeshima and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 151-155.
[191] Ibid, 208.
[192] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*.

1997 and went up in 1998, then declined continuously till 2001.[193] It is worth noting that 1997 was the year that large-scale privatization was pushed forward in China, and 1998 was the first post-privatization year for many privatized SOEs. Privatization appears to have only brought a temporary positive impact to profitability in sampled privatized firms in 1998; the indicator showed an opposite trend afterwards. The authors conclude that "*gaizhi* has a positive impact on firm profitability, although a weak or insignificant impact on unit cost and labor productivity."[194] Based on their 2006 nationwide survey, Guo, Gan, and Xu also reported that, although the performance of privatized firms fell behind that of privatized firms, there appeared a significant improvement than before privatization.[195]

But, Lu and Dranove argue that the conclusion of Garnaut et al. about the improved performance of privatized firms is questionable. Analyzing the same data set Garnaut et al. used, Lu and Dranove divided the data of each privatized firm into three stages (prior privatization stage, privatization stage, and post-privatization stage), and found that the firms that have been privatized into the hands of managers experienced a U-shaped pattern of profitability; in other words, prior to the privatization, there appeared a significant reduction in profitability and productivity, then, after the privatization the profitability simply returned to the level it was at before it declined. The two authors think that the observed improvement of the post-privatization performance in the firms by Garnaut et al. is actually caused by the significant decline in performance immediately before the

[193] Ibid, 159 and 161.

[194] Ibid, 159, 161 and xii.

[195] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," 18-20.

restructuring; they suggest that the managers who arranged MBO or similar privatization approaches deliberately manipulated accounting and/or real activities of their enterprises so as to more affordably acquire their firms; therefore the performance of the firms fell before the privatization and then returned to the pre-*gaizhi* levels after the privatization.[196] Liu and Liu also found the same phenomenon, and point out that the firms that were privatized into the hands of managers or other private owners usually showed worse performance before the privatization than other firms did. Within two years post-privatization their profits would return, but there would be no more improvement thereafter.[197] The criticism from Lu and Dranove could also be applied to the findings of Guo et al., because Guo et al. did not divide their firm data into prior- and post-privatization stages. Readers would no doubt be interested to know whether there are U-shaped patterns in their firm data, and whether their conclusions were affected by the variance in the pattern.

Moreover, the author would like to point out another ignored measurement problem in the analysis of Guo et al. China's economy experiences fluctuation, as that of any other country's does. So if one compares the data in economic boom years with that from the years at the bottom of an economic cycle, his findings regarding the performance improvement of privatized firms would include the mixed effects of economic boom; thus, whether the performance improvement itself is positive or negative would remain unclear. According to Zhang, Huang, and Lu, from 1998 to 2003

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[196] Susan F. Lu, and David Dranove, "Profiting from *Gaizhi*: Management Buyouts during China's Privatization," Dec. 2009 (http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1348277).

[197] Liu Xiaoxuan, and Liu Shaojia, *Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (A Research Report on SOE Gaizhi), May 2005.

(except 2001), the net profit rate of China's all-private industrial firms was between one to two percent; but, from 2004 to 2007 the rate grew to three to four percent,[198] because the economic growth of the country went up from 2003.[199] In other words, on average, an increase of profit rates of private firms (including privatized firms) can be observed if the numbers of the firms from 2004 to 2007 are compared with that of 1998 or 1999. Guo et al. drew their conclusion by comparing 2005 data with that from 1998. Readers would thus want to know if their conclusion reflects only the performance improvement.

In terms of the performance of privatized firms, Yusuf et al. pointed out several problems in corporate governance: first, minority shareholders do not have effective influence over the board of directors and management, as having a shareholder meeting has no effect on a firm's performance; the second, actual composition and appointment (or approval) of the members of the boards does not influence the performance of firms, probably because the operation of the boards often does not contribute to the performance; the third, changes of managers have no impact on firm performance, very likely due to a circulation of former SOE managers that have the same experience and backgrounds as those they replace.[200] Research on the performance of listed companies in China has also found that, after partial privatization, the performance of listed companies has not improved

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[198] Zhang Jie, Huang Taiyan, and Lu Zhe, *Zhongguo Qiye Lirun Laiyuan yu Chayi de Jueding Jizhi Yanjiu* (Research about the Mechanism that Determines Profit Sources of China's Enterprises)," Beijing, *Zhongguo Gongye Jingji* (China Industrial Economies), No.1, 2011, 28.

[199] The growth rate of China's industrial output from 1998 to 2007: 1998, 8.9 percent; 1999, 8.5 percent; 2000, 9.8 percent; 2001, 8.7 percent; 2002, 10.0 percent; 2003, 11.7 percent; 2004, 10.6 percent; 2005, 11.6 percent; 2006, 12.9 percent; 2007, 14.9 percent. See China's State Statistics Bureau, *Zhongguo Tongji Nianjian 2009* (China's Statistics Yearbook 2009), Beijing, China Statistics Publishing House, 2009, 41.

[200] Shahid Yusuf, et al, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 194-201.

and sometimes reduced.[201] As discussed in chapter eight, most listed companies still have the state as large shareholder. Deng, Gan, and He point out that the behavior of large shareholders to expropriate minor shareholders underpins the limited success of partial privatization; the listed companies often under-perform and experience a large loss of economic efficiency, and cause China's stock market to be more prone to financial crisis.[202] Analyzing financial data of the listed companies whose managers implemented MBO, Peng found that MBO does not improve the performance of the companies. Further, a lot of managers purposely provided false financial information in order to reduce the purchase price before MBO.[203]

Yusuf et al. also find that, although China has experienced a marketization process for three decades, domestic competition has no real impact on firm productivity.[204] From the point of view of the author, the phenomenon might imply that internal social relations of the enterprises, rather than outside market pressure, account more for firm performance. For example, Garnaut et al. find that management shares had negative and significant impact on labor productivity.[205] This might be explained by the tension between the managers and workers caused by managers' asset stripping and their ruthless attitudes toward workers. Obviously, whether managers pursue their own interests

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[201] Sun Qian, and Wilson Tong, "China Share Issue Privatization: The Extent of Its Success," *Journal of Financial Economics*, Vol.70, No.2, 2003, 183-222.

[202] Deng Jianping, Gan Jie, and He Jia, "Privatization, Large Shareholders' Incentives to Expropriate, and Firm Performance," *Hong Kong University of Science and Technology Working Paper*, May 2008.

[203] Peng Hong, *Zhongguo Shangshi Gongsi MBO de Shichang Fanying ji Jixiao Fenxi* (The Market Responses and Performance of MBO of China's Listed Companies), Master thesis, Changchun, China, Jilin University, Business School, April 2006.

[204] Shahid Yusuf, et al, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 193.

[205] Ross Garnaut, et al, *China's Ownership Transformation: Process, Outcomes, Prospects*, 168.

at cost to workers greatly shapes the post-privatization management-worker relationship and employees work morale.

The discussion in this chapter about labor disputes and conflicts shows that managers' asset stripping is one of the reasons tension between managers and workers has intensified during and after the privatization. The treatments of workers, such as wage and welfare cuts, increasing work loads, and extensions of work hours without overtime payments, even militarized management, are other reasons that trigger tension and undermine worker commitment to the workplace. While workers use hidden or open resistance to protect themselves against injustice during and after privatization, managers use their power of hiring and firing to force workers into compliance. There is no doubt that old employees of privatized enterprises are more likely to question managers' asset stripping or ruthless treatment; therefore, in order to get rid of the potential pressure from old employees, many managers laid off more and more old employees (including technicians) and replaced them with unskilled but more compliant peasants. Garnaut et al. point out that, while privatized firms began to lay off workers four years before privatization, and the laid-off numbers reached a climax in the first years of *gaizhi*, there appeared a clear trend of more and more casual workers, most likely hired from rural areas, having replaced the full-time workers before and after *gaizhi*.[206] Such an approach may reduce the tension at workplace, but also makes the enterprises rely on unskilled labor and undermines productivity and R&D. Moreover, without sufficient incentives and proper working conditions, privatized enterprises cannot attract technicians either, so their R&D

[206] Ibid, 97, 102.

is restrained. Actually, Liu and Liu have reported that, according to their survey data, in contrast to other privatized enterprises, the firms that were privatized into the hands of managers made the least investment after the privatization, even less than companies owned by employees.[207]

The slow progress in R&D can be observed in export-oriented enterprises. China's high economic growth has mainly been sustained by government investment, export, and over-expansion in the real estate sector. Export products encounter international competition, and firms that produce the products are supposed to make more efforts to improve their technologies than those who produce for domestic markets. However, according to Jin, Lu and Deng, although China's exports have grown very rapidly, Chinese companies have not much improved their own technologies; on the contrary, they heavily rely on the design, components, and equipment provided by their foreign partners, and make only a small amount of money in labor intensive assembling.[208] Thirty years ago when China just began its economic liberalization and opening up policy, this situation was the case. Now, the same problem remains.

As of 2011, China had completed the privatization of industrial enterprises, while small and medium SOEs have been privatized and large SOEs been transformed into LLSCs. However, the Chinese government has seemingly been reluctant to assess the privatization process and its results. Certainly, the ideological doctrine of insisting on the road of socialism is still a barrier;

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[207] Liu Xiaoxuan, and Liu Shaojia, "*Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (Research Report on SOE *Gaizhi*)," May 2005.

[208] Jin Pei, Lu Tie, and Deng Zhou, "*Zhongguo Gongye Jiegou Zhuanxing Shengji: Jinzhan, Wenti yu Qushi* (Transformation and Upgrading of China's Industrial Structure: Progresses, Problems and Trends)," *Zhongguo Gongye Jingji* (China Industrial Economies), No.2, 2011.

but there is another possible reason why the government avoids discussing the topic, viz. many laid-off workers and current employees of privatized enterprises disapprove of the privatization process, and an enduring tension between managers and workers undermines the performance of the privatized enterprises. Why managers have not made the necessary efforts to reduce tensions remains an unexplored topic. The topic is difficult to investigate because neither managers nor the government are likely to find it convenient to submit to surveys on the subject.

Appendix:

26 Cases of Labor Protests

No.	Time.	Place	Case Brief
1	3/1/2002 -4/6/2002	Daqing city, Heilongjiang Province,	From March 1 several thousand workers of the Daqing Oil Field began protesting against the lay-off policy near the entrance of the Oil Field office building; on March 4 more than 50,000 workers joined an on-street demonstration; the protesters occupied a square opposite the office building for weeks, no negotiation with managers took place; on April 19 police occupied the square and hundreds of protesters were detained.
2	3/28/2002	Beijing Municipality	Two hundred pensioners of the Beijing Automobile and Motorcycle Co. stood outside company headquarters to protest delayed pension payments. The protesters accused the managers of the privatized enterprise of selling the land of the factory and using the money to buy apartments for themselves, while refusing to pay workers' pensions. The managers of the company agreed to negotiate, and police exhorted the pensioners all to leave.
3	4/22/2002-7/30/2002	Songyuan city, Jilin Province	Several hundred laid-off workers gathered in front of the office building of the Jilin Oil Co. to protest against the MBO and lay-off policy implemented over the past two years. The protest was suppressed by police.
4	7/16/2003	Danyang city, Jiangsu Province	Two thousand workers of the Danyang Textile Co. went to the office building of the city government, to protest against MBO of the company and CEO's cruel treatment of workers. At 11:00 p.m. the mayor of the city came out and workers' representatives knelt down to hand him a petition. The MBO at the enterprise was then stopped and the CEO resigned.
5	10/9/2003-10/10/2003	Nanchong city, Sichuan Province	The workers of the Nanchong Textile Factory were notified that, although they were shareholders of the factory, all the employees over 50 years old had to leave because the factory was sold to a foreign owner. The workers protested, but on the next day more than 1,000 police forced the workers to give up.
6	8/18/2004-8/30/2004	Chongqing Municipality	Three thousand workers of the No.3403 Military Factory occupied the enterprise to prevent the privatization arranged by its CEO. The protest lasted 13 days. On Aug. 30 about 1,200 police suppressed the protest, and several workers were seriously wounded, then arrested.

26 Cases of Labor Protests ---Continued

No.	Time.	Place	Case Brief
7	8/15/2005-10/2/2005	Chongqing Municipality	Several thousand workers of the Chongqing Special Steel Co. participated in an on-street protest lasting from mid-August to early October. The workers blocked a highway to protest against the spontaneous privatization that caused bankruptcy of the company. Police arrested workers' representatives and fought the protesters; about 20 workers and their family members were wounded and several workers were arrested.
8	8/16/2006-8/25/2006	Ha'erbin city, Heilongjiang Province	Thousands of workers of the Harbin Flax Textile Factory demonstrated in front of the provincial government office building against the restructuring of the factory and asset stripping by managers; later they blocked traffic near the factory.
9	6/29/2007	Jiangyou city, Sichuan Province	Hundreds of workers of the Twin-Horse Cement Factory protested against the privatization scheme of the factory, while employee-shareholders were laid off.
10	8/2007-10/2007	Emeishan city, Sichuan Province	The workers of the Nuclear Special Automobile Factory participated in a three-month protest against asset stripping by managers after the factory declared bankruptcy in May 2004.
11	2/18/2008-2/25/2008	Santai County Sichuan Province	The workers of the First Textile Factory of the Santai Cotton and Flax Group participated in a strike for eight days, to protest against managers' very high income and the extremely low wages paid to workers after the privatization of the factory.
12	3/12/2008-3/17/2008	Shijiazhuang city, Hebei Province	Several thousand workers from four factories of the Changshan Textile Co. joined a strike for six days and asked wage increase, because their wages after the privatization of the factories were too low.
13	11/9/2008-11/12/2008	Jiangyan city Jiangsu Province	Two thousand of workers of the Jiangyan Diesel Engine Factory participated in a four day protest against the privatization scheme of the factory, after their CEO absconded with the funds of the enterprise and caused bankruptcy of the factory.

26 Cases of Labor Protests ---Continued

No.	Time.	Place	Case Brief
14	3/29/2009-4/8/2009	Baoding city, Hebei Province	Several thousand workers of the Baoding Yi-Cotton Co. protested against the privatization process at the factory and questioned suspicious asset stripping by managers.
15	7/9/2009-7/28/2009	Wuhan city, Hubei Province	Several hundred workers of the Wuhan Boiler Factory protested against a lay-off decision by the privatized enterprise, blocking traffic three times. Officials of the city government finally engaged in and promised canceling the lay-off decision.
16	7/24/2009	Tonghua city, Jilin province	At the privatized Tonghua Steel Factory the tension between managers and workers had lasted for years. On July 24 a conflict between workers and managers broke out, as the provincial government supported the managers to lay off more workers. CEO Chen Guojun was beaten to death by angry workers. After the event, the provincial government withdrew its support for management and calmed down the workers.
17	8/13/2009-8/16/2009	Puyang city, Henan Province	Four hundred workers of the Linzhou Steel and Iron Co. protested against a privatization scheme where the factory would have been sold at a very low price and a large number of workers would have been laid off, and compensated only 1,000 yuan. A local government official was detained, and the government finally promised to stay the decision.
18	8/22/2009-9/1/2009	Lengshuijiang city, Hunan Province	Five thousand workers of the Jinzhushan Coal Mine Co. protested against of the privatization and listing scheme of the company.
19	11/5/2009-11/7/2009	Chongqing Municipality	Several hundred workers from the Jiangling Machinery Factory joined a strike against a decision that dismissed half of the workers without compensation. Two worker activists were arrested.
20	11/9/2009	Luzhou city, Sichuan Province	About a hundred workers and pensioners of the Changjiang Second Hydraulic Press Factory protested the city government for the unresolved problems of the privatization of the factory. Police wounded three pensioners who were 70 to 80 years old.

26 Cases of Labor Protests ---Continued

No.	Time.	Place	Case Brief
21	5/18/2010-5/20/2010	Datong city, Shanxi Province	Three official labor union staff of the Xinhuo Medicine Factory organized about 10,000 workers and their family members to protest against the decision of the city government to sell the factory to real estate developer. Police wounded more than 30 workers, and the three labor union staffs were detained 10 days and each was fined 12,000 yuan.
22	6/4/2010-6/7/2010	Nantong city, Jiangsu Province	Workers of the Jianghai Capacitor Co. went on a three-day strike against the MBO of the company.
23	8/23/2010	Guangzhou city, Guangdong Province	Three thousand workers of the Guangzhou Steel Factory protested at the headquarters of the factory against the restructuring process that had laid-off workers lose basic social security benefits.
24	12/17/2010-12/20/2010	Baoji city, Shaanxi Province	The workers of the Shaanxi Ninth Textile Factory protested against a privatization scheme and detained two managers, then conflict broke out between the Workers and police.
25	1/5/2012-1/9/2012	Qingdao city, Shandong Province	Five hundred workers of the Huanghai Rubber Factory went on a strike to protest against the restructuring process that led to their social security benefits going missing. On Jan. 9 the demonstrators blocked traffic in the city.
26	1/14/2012-1/15/2012	Jingdezhen city, Jiangxi Province	Hundreds of workers of the Changhe Automobile Factory went on strike against CEO's decision to transfer the whole production to another company. When the CEO said, "As long as I am alive, I will make you suffer," he was beaten by angry workers. The decision was postponed by the local government.

Source:

Case No.1, China Labor Bulletin, "*Zhongguo Laogong Tongxun jiu Zhongguo Daqing Gongren Kangzheng de Shuoming* (A Statement of the China Labor Bulletin on the Protest of the Workers of the Daqing Oil Field)," Hong Kong, March 2002.

Case No.2, "*Bei Qi Mo Gongchao Huo Zai Jingcheng Liansuo Fanying* (The Labor Protest at the Beijing Automobile and Motorcycle Co.," March, 28 2002 (http://muzi.com/news/ll/fanti/1202778.shtml?cc=23475&ccr=&a=&ccp=1&q=).

Case No.3, Gong Yan, "*Jilin Sheng Songyuan Shi Shiyou Gongren Shangfang Yibai Tian de Diaocha Baogao* (An Investigation Report of the 100-Day Protest of the Workers of the Jilin Oil Co.)," July 25, 2002

(www.changanyuan.com/yuan-wenhua/2009/0904/shidai_33164.html).

Case No.4, "*Qi Yi Liu Gongren Qingyuan Shijian Muji Xiaoji* (An On-the-Scene Report of the Labor Protest on July 16th)," July 28, 2003 (www.aisixiang.com/data/700.html).

Case No.5, "*Shi Yue Jiu Ri, Huoxi Women de Guoqi bei Mai Diao* (On Oct. 9th, I Got to Know that Our Factory was Sold)," Oct. 11, 2003 (www.mala.cn/thread-4358-1-1.html).

Case No.6, Three Thousands Workers of the No.3403 Military Factory, "Guoqi Siyouhua Zhong Jiang Jifa Geming: Zhi Zhonggong Shiliu Jie Si Zhong Quanhui de Gongkaixin (Privatization of SOEs would Finally Lead to Revolution: A Petition to the Central Committee of the Chinese Communist Party)," Sept. 17, 2004 (www.xinmiao.com.hk/0004/0100-0124S).

Case No.7, "*Chong Te Gongren: Women Yao Shengcun, Women Yao Pingdeng* (The Workers of the Chongqing Special Steel Co.: We Want to Survive, We Want Justice)," New York, *The Epoch Times (Dajiyuan shibao)*, Oct. 5, 2005, and the China Labor Bulletin, "Speaking out: The Workers' Movement in China (2005-2006)", Hong Kong, *CLB Research Reports*, No.5, Dec. 2007, 15-35 (www.clb.org.hk/en/files/File/research_reports/).

Case No.8, "*Ha'erbin Yama Jituan Gongren Jingzuo Shiwei, Guojia Diantai Jizhe Caifang Zao Wuduan Kouya* (Workers of a Flax Factory in Ha'erbin Involved in Demonstration, and a Reporter of the official China National Radio was Detained by Police, when the Journalist Interviewed the Workers)," Aug. 28, 2006 (www.xinmiao.com.hk/0002/chifu1158.htm).

Case No.9, "*Zai Guanliao he Ziben Zhihou: Sichuan Shuangma Gongren Kangzheng Shijian Shuping* (Behind the Bureaucrats and Capital: The Labor Protest at the Twin-Horse Factory)," Aug. 5, 2007 (www.xinmiao.com.hk/0004/0100-0168S.htm).

Case No.10, "*Xiri He Gongye Gongcheng, Jinri You Bei You Can* (The Misery of the People who have Rendered Great Services for China's Nuclear Weapon)," New York, *The Epoch Times*, Dec. 12, 2007.

Case No.11, "*Sichuan Mianma Zhigong Da Guimo Bagong, Jinri Di Ba Tian* (The Eighth Day of the Strike of the Workers of the Cotton and Flax Textile Factory)," New York, *The Epoch Times*, Feb. 25, 2008.

Case No.12, "*Hebei Shijiazhuang Changshan Fangzhi Shu Qian Gongren Lianxu Liu Tian Da Bagong* (The Strike of Textile Workers of the Changshan Co. Has Lasted for Six Days)," Mar. 17, 2008 (www.aboluowang.com/news/data/2008/0317/article_43899.html).

Case No.13, "*Yuan Guoqi Lingdao Juankuan Tao, Liang Qian Yuangong Chixu Du Lu Kangyi* (Former CEO absconded with the funds of the enterprise, Two Thousand Workers Blocked Traffic to Protest)," Washington, DC, *Radio Free Asia*, Nov. 12, 2008.

Case No.14, "*Hebei Baoding Yi Mian Jituan Baofa Daguimo Gongren Bagong Kangyi Shijian* (The Workers of the Baoding Yi-Cotton Co. Involved in Strike and Protest)," Apr. 8, 2009 (http://meetboss.com/space.php?uid=7876&do=blog&id=19501).

Case No.15, "*Wuhan Guolu Chang Gongren de Weiquan Douzheng* (The Struggle of Workers of the Wuhan Boiler Factory)," Aug. 9, 2009 (www.wyzxsx.com/Article/Class22/200908/98779.html).

Case No.16, Wang Jianjun, "*Tong Gang Beiju de Luoji* (The Logic behind the Tragedy at the Tonghua Steel)," Beijing, *The Outlook Weekly*, Aug. 10, 2009.

Case No.17, "*Henan Puyang Lin Gang Gaizhi Yinfa 400 Ren Juji Weidu Ganbu Shijian* (After the Restructuring Scheme of the Linzhou Steel Exposed, Four Hundred Workers Protested and Detained an Official)," Aug. 17, 2009 (http://biz.xinmin.cn/company/2009/08/17/2388474.html).

Case No.18, "*Xiang Mei Jituan Gaizhi Siyouhua, Gongren Kangyi, Jianchi Bagong Shi Yi Tian* (The Hunan Coal Mine Group was Restructuring for Privatization, and Workers Protested for Eleven Days)," Sept. 2, 2009 (http://hbgrw.net/read.php?tid=1148).

Case No.19, "*Chongqing Jialing Jituan Gongren Da Bagong Jinru Di San Tian* (Workers' Strike in the Jialing Machinery Factory Has Lasted for Three Days)," New York, *The Epochtimes*, Nov. 7, 2009.

Case No.20, "*Luzhou Gongren Dao Shi Zhengfu Kangyi Gaizhi Liyi bei Boduo* (The Workers in Luzhou City Protested at the City Government against the Restructuring that Exploited their Interests)," Washington DC, *Radio Free Asia*, Nov. 10, 2009.

Case No. 21, "*Datong Xinhuo Zhiyaochang Shu Qian Zhigong Kangyi Gaizhi, Daitou Zhigong Zao Juliu* (Workers of the Datong Xinhuo Medicine Factory Protested against the Restructuring Scheme, and Three Worker Leaders were Detained)," May 26, 2010 (http://blog.sina.com.cn/s/blog_53e717050100j2bo).

Case No.22, "*Bagong! Nantong Jianghai Gongsi Yuangong Bagong Kangyi Gaoguan Jie Gaizhi zhi Ji Qintuo Jiti Zichan* (Strike! Workers of the Jianghai Capacitor Co. Protested against Managers' Assets Stripping through Restructuring Scheme)," June 10, 2010 (http://www.xici.net/d121906619.htm).

Case No.23, "*Guang Gang 3000 Gongren Du Lu Shiwei, Kangyi Qigai Moshi Jiceng Quanyi* (Three Thousand Workers of the Guangzhou Steel Factory Blocked Traffic for Demonstration, Protested against the Restructuring Process that Ignored Workers' Interests)," Hong Kong, *The Apple Daily (Pingguo ribao)*, Aug. 24, 2010.

Case No.24, "*Shan Guoqi Pochan, Gongren Kou Lingdao, Jingfang Qiangren Bao Da Chongtu* (A SOE Fell Bankruptcy, Workers Detained Managers, Large Conflict Broke out between the Workers and Police who wanted to Free the Managers)," Dec. 21, 2010 (http://bbs123.blog.china.com/201012/7458717.html).

Case No.25, "*Shandong Qingdao Huanghai Xiangjiao Chang Gongren Bagong Kangyi, Jiaotong Tanhuan* (The Workers of the Huanghai Rubber Factory Involved in Strike, Protest and Blocking Traffic)," Washington DC, *Radio Free Asia*, Jan. 12, 2012.

Case No.26, "*Changan Pai Dao Changhe Qiche de Zongjingli Li Li bei Yuangong Bao Da* (The CEO of the Changhe Automobile was Beaten by Workers)," Jan. 14, 2012 (http://auto.enorth.com.cn/system/2012/01/18/008517932.shtml).

Chapter 10

How Managers are Empowered as the New Masters?

A Comparative Study of Privatization in Russia and China

Privatization in Russia and China has provided rich material for research about the transition from state socialism. The paths of the two privatizations are quite different, but they have seemingly reached the same destination: in most privatized enterprises, the SOE managers who personally invested only a little money, or nothing, have finally empowered themselves to be the new masters of the firms. How they succeed is an unexplored topic, and this thesis has made efforts to find answers. Contrasting the privatization in Russia with that in China, this final chapter will analyze the sociopolitical and economic preconditions, guidelines, policy making ramifications, and processes and outcomes of the two privatizations. All this promises a fresh understanding, both empirically and theoretically.

1. Privatization in Russia and China:

Background, Guidelines and Policy Making

Before privatization was initiated, political developments in Russia and China moved in opposite directions. The political liberalization in the Soviet Union under Gorbachev's leadership not only mobilized intellectuals and opened a limited space for

freedom of the press, but also empowered Russian workers to actively participate in independent labor movements. Almost at the same time in China, reform with a "soft hand" under the leadership of Zhao Ziyang ended after the crackdown on the 1989 democratic movement. Shocked by the Beijing massacre, the Chinese people immediately realized that the thaw that had begun in 1978 was over, and they had to compliantly and quietly live under political repression. Consequently, while the *nomenklatura* in government and SOEs in the two countries seized on the opportunity of economic liberalization to enrich themselves, they encountered different social responses. In the Soviet Union/Russia, the social forces opposing the *nomenklatura* were activated to pursue a just distribution of income and to prevent public property from being unlawfully appropriated. However, in China, "getting rich" was endorsed by the government, while the approach to be used was not questioned. With few worries about social resistance, an increasing number of members of the *nomenklatura* lent on their accumulated political power and social capital, and got involved in business. The difference between the sociopolitical atmosphere in Russia and that of China implies that, while social mobilization against the *nomenklatura* in Russia may have led the imminent privatization in a direction favoring the workers of SOEs, the business fever in China would pave the road for managers' spontaneous privatization.

Scholars of Russia and China often attribute the different paths of transition in the two countries to the influences of traditional culture. But such an explanation may

underestimate the influence of the communist ideology that deeply shaped workers' worldviews in both countries. Although pre-revolution Russia had been strongly influenced by the culture of Western Europe, and pre-revolution China maintained a legacy of Confucianism, in these cradles of communist revolution the official ideology of the regime took deeper root than it did in Eastern European societies. A key factor of the ideological influence, crucial to privatization, is the idea of workplace democracy based on the dogma that workers are the masters of production, or masters of enterprise. This idea greatly shaped workers' attitudes towards privatization and management-worker relations both in Russia and China. As a part of SOE reform measures under the communist regimes, new enterprise laws were issued in 1988 in both countries. The laws were not fully implemented; but in the minds of workers they reaffirmed the idea of workplace democracy. A large portion of SOE employees in Russia and China did believe that they ought to own their enterprises and select their managers. The idea of workplace democracy also implies that social justice and moral principles would be taken into consideration by SOE employees when their enterprises were privatized. Therefore, the pre-privatization social perceptions regarding SOE transformation in Russia and China were quite different from those in some Eastern European societies, such as the Czech Republic, where privatization was linked to the founding of a post-communist national identity, and institutionalized and informal manifestations of anti-communism discredited the demands of workers and managers,

and attenuated the two groups' ability to shape the process of privatization.[1] The author would thus suggest that evaluations of privatization in Russia and China should be based on an understanding of the influence of the idea of workplace democracy and of the anti-*nomenklatura* sentiment among workers.

While Russian and Chinese workers shared the idea of workplace democracy, SOE managers in the two countries pursued the same goal in privatization, i.e. to retain their power and acquire the assets of the enterprises. However, as the pre-privatization sociopolitical development in Russia and China was different, the balance of power at the workplace in the two countries was reconfigured in different ways. Russian managers realized that the fragile Soviet state might no longer be reliable, and their control over enterprises was under threat. When a straightforward claim of managers' rights to public property was politically isolating, the technocratic faction of the Russian *nomenklatura* could only get better off if they at least appeared to stand on the side of workers, because such a position matched the demands of workers for democracy and justice, and helped managers to obtain a portion of the shares when their enterprises were privatized. Unlike their Russian counterparts, Chinese SOE managers had much more freedom to select the approaches of privatization in their enterprises, as long as they had the tacit approval of the government. On one hand, China's economic liberalization initiated in the 1980s offered

[1] Hilary Appel, "The Role of Ideology in Privatization Programs: Reconsidering the Determinants of Liberal Economic Reform, Lessons from Privatization," the speech at Woodrow Wilson Center, Oct. 25, 1999 (www.wilsoncenter.org/index.cfm?event_id=3813&fuseaction=events.event_summary).

them an increasing level of autonomy and freedom in decision making; on the other hand, managers, appointed and backed up by the government, were given power to further tighten political control over workers. Before privatization was pushed forward in China, Chinese workers had been silenced, even though they observed corruption and maladministration at the workplace.

Privatization in Russia and China encountered two economic problems. First, who would be able to buy more than 20,000 industrial SOEs within one or two years? The privatization approach advocated by economists in the West suggests that SOEs should be sold to anyone who wants to buy the asset, at market price. If SOEs are put up for auction, SOE insiders, individuals outside SOEs (including wage earners who do not work in SOEs, and private entrepreneurs), institutional investors such as mutual funds or investment funds, and foreign investors, are among possible buyers. However, both in Russia and China, available financial resources for such investment were quite small. Hyperinflation in Russia rapidly diminished household savings and impoverished the population.[2] The total amount of savings of Chinese households was only equal to half of the assets of industrial SOEs,[3] and most families needed the savings to get by. Therefore, the majority of people in the two countries were unable to buy shares of the privatized

[2] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, London, Routledge, 2003, 32.

[3] The total amount of household savings in 1998 was 600 million yuan, and the total amount of fixed assets of industrial SOEs in the year was 1.09 billion yuan. See *Zhongguo Tongji Nianjian 2009* (China Statistics Yearbook, 2009), compiled by China's State Bureau of Statistics of China, Beijing, China, China Statistics Publishing House, 2009, 317, 494.

enterprises with cash, even at a discounted price. In both countries, small entrepreneurs do their business primarily in retail or other service industries, lack large amounts of capital, and mostly lack the knowledge and experience needed to manage industrial firms. As the emerging stock market in the two countries was full of short-sighted speculators and far from mature, and mutual funds had yet to be developed during the period of privatization, it is unrealistic to hope that domestic mutual funds could play an important role in privatization as institutional investors. Only financial oligarchs that come up from private banks had participated Russia's second-stage privatization of large- and medium-sized SOEs, through a "loans for shares" deal with the Yeltsin regime. It involved large-scale asset stripping.

China has successfully absorbed a large amount of foreign direct investment (FDI). From 1979 to 2008 the total amount of FDI that poured into China was $853 billion.[4] But, in China's FDI, the portion for merges and acquisitions which directly privatize industrial SOEs was very small, and greenfield investments in joint-venture projects that have a partial privatization effect only accounted for one-fourth of FDI in 1999, and 13 percent in 2008 (see chapter eight). Many of the foreign investors in China are based in Hong Kong and Taiwan; they are usually interested in investing in small- or medium-sized SOEs, for which real financial information can be obtained through personal networks with managers and local officials. Often such deals involved asset stripping behind the closed doors.

[4] The State Statistics Bureau of China, *Zhongguo Tongji Nianjian 2009* (China Statistical Yearbook 2009), 745.

Obviously, in neither country would there be sufficient investment from outsiders to complete the large-scale privatization; if the government decides to carry out privatization, very likely insider privatization is inevitable and would be the most feasible solution both for Russia and China, supplemented by a certain amount of domestic individual investors and foreign investors. The ideal model of privatization discussed by Western economists does not apply to these scenarios.

Second, workers' worried about losing their jobs were a primary concern during and after privatization in both countries. When over-employment in SOEs was a common phenomenon in Russia and China, the threat of large scale lay-offs during and after privatization would lead workers to tie individual survival to job security at the current workplace. Such attitudes greatly influenced their options in privatization and their evaluation of the results of privatization.

Another economic problem China encountered before privatization was the absence of a social security system. Since the 1930s the former Soviet Union began to establish a state-sponsored nationwide social security system which covered pension, medical expenditures and subsidies to low-income families; and, by the end of the 1970s, the Soviet social security system covered the entire population. But in China the state-sponsored pension and medical care system was only available for employees of government offices and government-sponsored institutions such as colleges, mass media, hospitals and schools; the pensions and medical expenditures of SOE employees were paid by each enterprise.

Once SOEs were privatized and SOE employees were laid off, the state was obligated to set up a nationwide social security system to provide pension, medical insurance, unemployment benefits, and low-income family subsidies for the employees of the bankrupted or privatized SOEs. Yet the Chinese government declined to acknowledge its responsibility to SOE employees. Instead, it left the expenditures for social benefits on the shoulders of the privatized enterprises. Then a unique problem arose, which was hardly understood by Western observers: the laid-off workers were often tied to their former work units by the government, and their former employers were asked to pay unemployment subsidies, and contribute to pension insurance and medical expenses. Many managers of privatized SOEs were reluctant, or simply did not have the financial resources, to pay the social benefits of their current and former employees; thus, quite often medical expenses were not reimbursed, and laid-off workers lost the financial support they needed for survival. Only after understanding the remaining ties between laid-off workers and their former work units can one explain why a lot of laid-off workers in China often see their interests connected with the privatization of their previous workplace.

Although economic conditions were not ripe for privatization, both the Russian and Chinese governments could no longer wait. In Russia, the nationwide pro-democracy labor movements in opposition to the spontaneous privatization activities of the *nomenklatura* of the branch ministries put great pressure on the Yeltsin regime. Immediate privatization thus became an urgent task for the Russian government, as it had to break

up the power of the state apparatus as soon as possible by building a foundation for democratization and an independent enterprise system. The Chinese government could no longer afford the increasing losses made by SOEs and was worried about the safety of its banking system, which was under the threat of a dangerous amount of bad loans to SOEs. Moreover, it was eager to join the World Trade Organization (WTO), so China's trade conditions could be improved, and the government could avoid tough negotiations with the U.S. government for Most Favored Nation Status. In order to be accepted by the WTO as a member country, the Chinese government had to privatize SOEs to meet the preconditions regulated by WTO rules.

In both countries, privatization programs by the governments have strategic goals and pragmatic concerns. First of all, the voucher privatization in Russia and the spontaneous privatization in China were part of the goal to establish a market economy to replace the planned one. In Russia, the voucher privatization was also a vehicle to undermine the Soviet state apparatus, and to consolidate the democratizing institutions, as well as the Yeltsin administration. The privatization in China helped the government unburden itself of the irresolvable SOE troubles, so the communist regime could get rid of the threat of bankruptcy of the state-run banking systems. At the same time, the privatization of large SOEs in Russia aimed at collecting some revenues through selling the shares of large SOEs to reduce the budget deficit; and the partial privatization of large SOEs in China by transforming them into LLSCs and listing them on the stock market

raised a large amount of capital to improve the financial situation of the companies. No matter what goals and pragmatic purposes it serves, such a large-scale nationwide privatization encompasses fundamental institutional changes and has produced various socioeconomic consequences.

When explaining differences in organizational behavior, economists of the property rights school emphasize the individual incentives created by the structure of property rights.[5] For them, the guideline in privatization is quite simple, i.e. transferring public properties into private hands. However, from a sociological point of view, privatization is a social process and is much more complicated than many economists posit. As Starr points out, privatization not only refers to public assets and individual involvement; privatizing enterprises means a privatization of wealth, employment relations, and social functions. The potential private owners of public assets represent specific interests and groups; governments that are in a hurry to sell state-owned enterprises may make concessions to current managers, and privatization then becomes an occasion for managerial enrichment and entrenchment. Privatization is unlikely to be carried out without concern for these social issues.[6] Viewing it from this perspective, the author seeks to emphasize that a responsible government should not implement a large-scale privatization program arbitrarily. Basic guidelines must be followed, including notions of

[5] Paul Starr, "The Meaning of Privatization," *Yale Law and Policy Review* Vol. 6, 1988, 6-41. This article also appears in Alfred Kahn and Sheila Kamerman, eds., *Privatization and the Welfare State*, Princeton, NJ, Princeton University Press, 1989.

[6] Ibid.

justice,[7] participation, and transparency. Whether and how the guidelines are taken into consideration by the governments is an important criterion when evaluating the privatization process and its consequences. Sometimes, devious actions by government can take place and unintended consequences of policies occur; however, if a government simply ignores the guidelines, it escapes accountability.[8]

The guideline of justice mainly refers to state policies regarding privatization and its socioeconomic consequences. In Russia and China, this guideline actually touches on an issue that has rarely been mentioned in the existing literature: who ought to benefit and who should pay the costs? In Russia's voucher privatization, the government assumed that all Russian people had participated in the creation of national wealth in the communist era, thus all citizens should have rights to lay claim to the public properties of SOEs. The voucher privatization scheme thus distributed vouchers to all Russian citizens. It also tried to prevent SOE managers from gaining a core stake without the approval of their workers.[9] But, in Russia's privatization of large SOEs, the guidelines were ignored.

In China, the situation was supposed to be the same as in Russia's voucher privatization, because all SOEs were officially defined as "owned by all the people" (*quanmin suoyou zhi*) for decades. However, in China's privatization, only SOE managers, and sometimes SOE employees, were offered the privilege of obtaining public

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[7] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, 76.

[8] Samuel P. Huntington, *The Third Wave: Democratization in the Late Twentieth Century*, Norman and London, University of Oklahoma Press, 1991, 213-214.

[9] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, 78.

assets, whereas all other citizens were excluded. Among managers and workers, managers were allowed to use the financial resources or guaranty of their enterprises to obtain the public properties for themselves, rather than paying with their personal funds, whereas workers had to pay cash if they wanted shares; on other occasions they were forced to buy shares even if they didn't want to.

The decision to privatize in the two countries suggests that the SOE system under state socialism and the reformed socialist institutions has failed. Someone had to pay the costs of failure. In Russia, the political responsibility of the failure of the SOE system was left to the Soviet regime, and the economic responsibility of the failure was shared by individual owners of the privatized enterprises. When Russian citizens used privatization vouchers to obtain shares of privatized enterprises, they took both opportunities and risks, although the opportunities were often minimized by the managers of the privatized enterprises. If the privatized enterprises fall into economic difficulties, their new owners become losers.

In China the communist regime refuses to take the political responsibility for the failure of the SOE system; at the same time, it asks SOE workers to pay the socioeconomic costs caused by the failure, but allows SOE managers to benefit from privatization. When the Chinese government gave managers the power to manipulate the privatization of their enterprises to benefit themselves, many SOE workers realized that such privatization arrangements could make workers sacrificial lambs for the failure of

state socialism. Moreover, from the point of view of workers, many SOE managers were responsible for the poor performance of their enterprises and had been involved in corruption before privatization, but they were still entrusted by the government with privatization, and benefited from it.

A possible cost workers may pay during privatization is lay-off. In Russia, "[T]he absence of mass unemployment is one of the most striking features of the Russian transition, which distinguishes it from the countries of Eastern Europe."[10] In all transition societies, only the Chinese government declared that, in order to achieve *gaizhi* (restructuring), about half of the SOE workers must be dismissed in a short period, even though a social security system had yet to be established. Under the official slogan of "escaping SOE difficulties within three years," Chinese SOE managers were authorized and encouraged to lay off their workers, but workers did not have any right to protect themselves. Ultimately, the Chinese government and SOE managers did "escape the difficulties," but millions of former SOE workers fell into misery that lasted years.

The privatization of Russia and China implies that, when assets of SOEs are privatized, the social function of SOEs is privatized as well. In both countries the privatization of SOEs' social functions meant a reduction of paternalistic practices and workers' structured dependence on enterprises;[11] at the same time, workers had to count on

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[10] Simon Clarke, "The Enterprise in the Era of Transition," in Simon Clarke, ed. *The Russian Enterprise in Transition: Case Studies*, Cheltenham, UK, Edward Edgar, 1996, 44.

[11] Andrew Walder, *Communist Neo-Traditionalism, Work and Authority in Chinese Industry*, Berkeley, CA, University of California Press, 1986, 81-84.

the state-sponsored social security system for benefits. In Russia this system had already been built up in the Soviet era, and remains functioning after the Soviet regime collapsed, though financial support was at quite a low level. But in China, privatization began before the social security system was established; it was only after privatization had almost been completed that China's government-sponsored social security system was gradually constructed in cities. Therefore, during privatization, workers, whether hired or laid off, have to rely on their current or previous work units to provide basic benefits. If managers refuse to do it, workers won't get help anywhere else. Many Russian pensioners experienced a tough time during the early 1990s, but they still had medical benefits from the state-sponsored social medical system. In China, a large portion of laid-off workers not only lived very poorly—either because unemployment benefits, or the lump-sum lay-off compensation, were too small or not available at all—but also suffered from absence of medical benefits. In privatized firms, about one-fifth of workers had no medical benefits in 2002; if they got sick, they had to personally pay all medical expenses.

The privatization of industrial enterprises in Russia and China proceeded in two stages: the first for small- and medium-sized enterprises, and the second for larger enterprises. Both governments chose a basic approach, i.e. grasping the large and let go the small. However, policy formations in the privatizations were different. The guidelines of participation and transparency in privatization can be analyzed at two levels: the national level and the enterprise level. At the national level of privatization policy formation in

Russia, the two guidelines can be seen in its voucher privatization scheme; but, in its privatization of large-scale SOEs, the guidelines were not followed. In the voucher privatization, various sociopolitical forces openly lobbied and negotiated at the Russian parliament to influence policy making, and SOE workers were offered choices about the way to privatize their enterprises; thus, social participation was widespread, and the formation of privatization policy at the national level was transparent. However, at the enterprise level, after workers supported managers to select insider privatization, schemes of privatization at each enterprise and worker participation at the workplace were often manipulated by managers, and not transparent to insider workers and outsider buyers.

Of transitional societies, China might be the only country where an authoritarian communist regime has carried out a large-scale privatization. Such a regime is in a position to intervene heavily in the privatization process. But, the Chinese central government declines to discuss privatization openly, and China's parliament has never passed any law to regulate it.[12] Even after large scale privatization had been done for years, there were never any formal discussions about the matter in parliament; nor is discussion about the process allowed in the media. The central government simply opened the door of privatization for SOE managers and local government officials without clear-cut guidelines.

[12] Wang Junchao, "*Zhongguo Guoyou Qiye Gaige de Xianzhuang yu Qianjing* (The Current Status and Perspectives of SOE Reform in China)," in Ru Xin, Lu Xueyi, Li Peilin, Huang Ping and Lu Jianhua, eds. *2003: Zhongguo Shehui Xingshi Fenxi yu Yuce* (The Blue Book of Analysis and Forecasting of the Chinese Social Situation, 2003), Beijing, China, The Social Sciences Documentation Publishing House, 2003, 185.

China's privatization was actually not done according to a designed program, nor was it properly regulated by the government. It was promoted with an unclear direction, while rules and procedures necessary to regulate the process were absent. During the privatization process, China's central government preferred an *ex post facto* response rather than to set up clear rules in advance. It stepped aside and mildly responded only when significant corruption or labor disputes occurred and were reported to the central government. When it came to regulating privatization, the hands of the central Chinese authorities were apparently quite feeble--but when it came to dismissing millions of SOE workers, they were tough.

In the most important years of China's privatization process, the only government office responsible for supervising state-owned assets, the Bureau of State Assets Administration, was abolished. On the other hand, the Russian federal government established the State Property Committee and the Russian Federal Property Fund, with local offices, to appraise and approve the privatization plan of each SOE and to organize tenders and auctions of shares of SOEs. China initiated its large-scale privatization after Russia had completed this task, so it is hard to imagine that the Chinese government would forget the importance of the government offices necessary for the operation of privatization. Very possibly the Chinese central government realized that a spontaneous privatization would conveniently release it from a lot of sociopolitical and economic obligations it did not want to have; thus, it granted local government offices and SOE managers discretionary

powers to decide how each SOE was privatized, and the local governments and SOE managers could try many approaches, in a legal vacuum, with no clear boundaries about what could not be done.

Chinese SOE workers were often excluded from the policy making of privatization of their enterprises by managers and local government officials. Although China's central government regulates that the *gaizhi* program of each SOE should be approved by the congress of workers and staff, the request was often ignored by managers and local government officials; and quite often, managers and local officials simply manipulated the approval by arranging a meeting of selected representatives of workers and staff and forcing them to accept the arrangement. Overall, the privatization schemes at each SOE were manipulated by managers and officials behind closed doors, without worker participation.

It is worth noting that, after the spontaneous privatization of small- and medium-sized SOEs was almost done in China, the Chinese government established the State Assets Supervision and Administration Commission (SASAC) with local branches across the country charged with overseeing the partial privatization of large SOEs. Therefore, the partial privatization of large SOEs in China has been closely monitored and better regulated by central and local governments. In the process, although workers were still excluded, privatization schemes were transparent to government offices—no longer a scheme known only to the managers. But, managers of partially privatized companies in

China still tried various ways to conduct MBOs to benefit themselves with the support of local officials (see chapter eight).

A significant difference between the spontaneous privatization in China and the voucher privatization in Russia is that in Russia, local governments were not much directly involved in the voucher privatization process, while an alliance of SOE managers and workers against outside investors was formed to make the process more favorable to insiders; but in China, local governments and SOE managers formed an alliance to manipulate the spontaneous privatization against workers' interests and demands. An important incentive that motivated Chinese government officials to support or protect the spontaneous privatization was the chance that they would benefit personally.

2. Outcome and Evaluation:

Comparative Analysis of Privatization in Russia and China

Although the sociopolitical conditions and policymaking of privatization are different in Russia and China, most industrial SOEs have been privatized in the two countries. Evaluating it from this angle, one may conclude that the privatizations in the two countries reached their goals. In 2001, the privatized nonagricultural enterprises in Russia held more than 60 percent of productive capital in manufacturing, produced 75 percent of GDP, and employed about 80 percent of national labor force; about 40 million Russian citizens

became shareholders in the privatized enterprises.[13] The privatized enterprises have become the pillar of the Russian economy. In China, the privatized industrial enterprises possessed about 47 percent of the productive capital in manufacturing, produced 49 percent of industrial output, and employed about 49 percent of the industrial labor force in 2008.[14] China began economic liberalization before privatization and has created a business environment for privately funded small enterprises, and for enterprises in which foreigners and people from Hong Kong and Taiwan have invested. So the large-scale privatization of industrial SOEs in China only involved about half of China's manufacturers.

In the media, and in the field of Russia and China studies, China has widely been praised for its economic achievements reached through economic reform, whereas Russia is often depicted as a poor student. In China, many people believe that China's economic success can be attributed to its gradualist economic reform strategy, and the economic problems in Russia are caused by its shock therapy.[15] This point of view can easily be challenged by two basic facts discussed in previous chapters. Rapid price liberalization and

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[13] Victor Supyan, "Privatization in Russia: Preliminary Results and Socioeconomic Implications," Moscow, *Demokratizatsiya* (Democratization), Winter, 2001. The percentages of output and labor may include privatized enterprises in the service industry.

[14] There is no well defined category for privatized enterprises in China's official statistics, and privatized enterprises were separately listed under different categories. The author includes the following types of industrial enterprises as privatized enterprises: cooperative enterprises, other LLCs (exclude state sole funded corporation from all LLCs), all LLSCs, private LLCs, and private shareholding corporations Ltd. See *Zhongguo tongji nianjian 2009* (China Statistics Yearbook 2009), complied by the China State Statistics Bureau, Beijing, China, China Statistics Press, 2009, 487.

[15] Hu Shuli, Xu Chenggang, and Yang Zheyu, "*Sulian Jieti Ershi Nian Ji: Duihua Xu Chenggang* (After the Collapse of the Soviet Union: A Dialogue with Xu Chenggang)," Beijing, China, *Zhongguo Gaige* (Reform in China), No. 12, 2010.

SOE privatization are two basic shock therapy programs for reform of a planned economy. As analyzed in chapter four, China quietly did its price liberalization from 1993 and 1994, right after Russia completed its own. In both Russia and China, price liberalization was implemented within two years. In terms of large-scale privatization, Russia implemented a voucher privatization from 1992 to 1994, and China carried out a nationwide privatization of small- and medium-sized SOEs from 1998 to 2001, under the name of *gaizhi*. In order to push privatization forward, China had laid off about half of the employees of industrial SOEs in a couple of years; but "the unemployment rate in Russia was not particularly responsive to the shock of the transitional period."[16] In Russia, "privatization occurred with relatively little social conflict;"[17] however, China's privatization caused nationwide labor protests. If Russia's voucher privatization is perceived a shock therapy,[18] China's privatization is indeed no different: when comparing the price liberalization and privatization in the two countries, one finds that shock therapy was employed in both countries, and a key difference between them is that the privatization of small- and medium-sized SOEs in China was more spontaneous than Russia' voucher privatization.

Privatization not only yields economic outcomes; it also results in social and political consequences that deserve evaluation. Using the mentioned three guidelines, the author contrasts the privatization in Russia with that of China and finds five features. First, at the

[16] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," in Robert McGee ed. *Corporate Governance in Transition Economies,* New York, Springer, 2008, 227.
[17] Ibid, 221.
[18] Ibid, 223; Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, 66-67.

national policy formation level, the Russian government did much better in its voucher privatization than the Chinese government. Second, at the enterprise level, Russian workers could participate more in the voucher privatization process than their Chinese counterparts, and information about privatization schemes was more transparent in Russian workplaces than in Chinese workplaces, because, bound by the state privatization policy, Russian managers needed workers' support against potential outside takeovers. Chinese managers were authorized to act as they wished. Third, still at the enterprise level, in Russia, during and particularly after the voucher privatization, a large portion of managers played the same game as their Chinese counterparts did with MBOs, in order to obtain more shares; while doing so, managers in both countries excluded workers, and MBO schemes were not transparent. Fourth, upon comparison, similarities are apparent between Russia's privatization of large SOEs and China's privatization of small- and medium-sized SOEs: as both processes were spontaneously manipulated by government officials, outside buyers and managers, and in the process obvious asset stripping took place. Fifth, the partial privatization of China's large SOEs was better regulated by the government than the privatization of large SOEs in Russia; but, once MBOs were carried out in the Chinese large firms, such privatization looks the same as the spontaneous privatization of Chinese small- and medium-sized SOEs and Russian large SOEs; perhaps the only difference is the amount of assets grabbed by managers. The spontaneous privatization of large SOEs produced billionaires in Russia but only millionaires in China.

This is a simplified picture of the respective privatizations for readers, and has left many aspects of the process unexplored. Analyzing the impact of the privatizations on corporate governance, social relations at the workplace, and politics, the author finds that, while ownership structures, particularly the composition of insider ownership, in privatized firms of the two countries are different, corporate governance, manager behavior, and management-worker relations in both countries are quite similar; but there have been many more instances of labor conflicts in China than in Russia.

2.1 The Privatization Process Revisited

Both in Russia and China, privatization was initiated by the central government; however, the government cannot control the process of large-scale, nationwide privatization, because a lot of decisions and arrangements have to be negotiated at the enterprise level. Indeed, during the privatization process in the two countries, some developments have gone beyond the expectations of the governments. The Russian privatization administration once believed that, among three options of voucher privatization, workers and managers would most likely select Option 1, which offered workers 25 percent of the free allocation of non-voting shares, allowed managers to purchase 5 percent of the shares, and planned to have 60 percent of the shares sold to potential outside investors. This option was designed to satisfy the demands of managers and workers, and, at the same time, to maintain outsider-dominated ownership. Actually, in about 80 percent of the privatized enterprises,

managers and workers selected Option 2, a scheme in which workers and managers might purchase 51 percent of the shares but have to pay a price 70 percent above the book value of enterprise assets. Unlike what the Russian government predicted, most Russian managers and workers chose to pay the higher price in order to turn the privatization into an insider-dominated one. The Chinese government did not really have the concern that the privatization process would deviate from an assigned track, as it did not have any designated privatization schemes; but it was bothered by the rapidly increasing number of labor disputes during and after privatization, which have caused social tension and conflict.

The unexpected results of the privatizations suggest that we should not only analyze how sociopolitical conditions and processes of policymaking differ in Russia and China, but also try to understand how the actions of managers, investors and workers at the enterprise level are affected by these sociopolitical conditions and privatization policies. Moreover, at the enterprise level, privatization is not simply economic decision making and legal arrangements; it is also a social process shaped by participants pursuing self-interested goals, potentially in conflict with the public interest.[19] As privatization in Russia and China was dominated by insiders, how managers and workers interacted during the privatization process and how their social relations are reconfigured after privatization inevitably becomes a central concern of our analysis. Without an understanding of the

[19] Gordon C. Rausser, and Leo K. Simon, "The Political Economy of Transition in Eastern Europe: Packaging Enterprises for Privatization," in Christopher Clague, and Gordon C. Rausser, eds. *The Emergence of Market Economies in Eastern Europe*, Cambridge, MA, Basil Blackwell, 1992, 252.

interactions between the two parties, one can hardly arrive at a proper evaluation of the outcome of privatization.

In Russia, the voucher privatization process was greatly shaped by the interactions between managers and workers at the workplace, whereas in China the paths of privatization were manipulated by managers and local officials. How do managers and workers in the two countries perceive their new positions in the privatization process and how do they identify their interests? Workers' attitudes towards privatization in Russia and China were quite similar. The majority of SOE workers in the two countries did not really embrace privatization enthusiastically; they worried about unemployment, and their top concern was survival and job security. On the other hand, if privatization turned out to be inevitable, the idea of master of the enterprise deeply rooted in their values would lead them to support employee privatization. At the same time, many workers did not think their managers were qualified entrepreneurs who could solve the problems of their enterprises after privatization. But they did care about their rights in privatization, and were particularly sensitive to managers' behavior involving in corruption or conspicuous consumption during and after privatization.

SOE managers as part of the *nomenklatura* would certainly play a very active role in privatization. However, at the early stage of privatization, the attitudes of Russian managers and that of Chinese managers were opposite. As discussed in chapter five, the majority of Russian managers worried very much about losing their jobs during

privatization—they were sometimes more fearful than workers. They also worried about their shaken authority and the legal vacuum in which they operated at the workplace. At the same time, they dared not openly claim that they wanted to obtain the assets of their enterprise. Therefore, when a privatization program was prepared by the Russian government, about two thirds of Russian managers did not want the privatization to take place. The attitudes of Chinese SOE managers towards privatization were completely different. They realized that, since the Chinese government did not restrict them to any privatization approach and workers under strict political control could not claim rights, the privatization in China was indeed a rare opportunity for managers to become millionaires within mere months, or days. The differing attitudes of managers towards privatization in the two countries indicate that they are likely to behave differently at the beginning of privatization.

The sociopolitical changes prior to privatization in the two countries decisively reconfigured workers' social status, and the privatization policies of the two governments determined whether they would be able to impose their own choices. Russia's voucher privatization program was designed to meet the interests of all members of society and to create millions of individual owners, and offered SOE workers some rights to prevent managers from declaring themselves the new bosses of their enterprise. Although at the beginning of the voucher privatization many Russian managers were opposed to privatization, their administrative positions and social capital would unavoidably offer the

elite group opportunities and advantages that workers do not have. When the voucher privatization started, most Russian managers found a way to become better off by seeking support from their employees. The Russian privatization administration actually failed to read the minds of most workers and managers. Both Russian manages and workers did not want outside investors to get control over their enterprises, and workers' mistrust of outsiders was much stronger than the mistrust of their own managers; therefore, insider privatization became the common choice of managers and worker at the workplace. In Russia, most workers and managers worked together in an alliance against outside investors who might lay off workers and managers; thus about 80 percent of the privatized enterprises selected Option 2 of the voucher privatization program, in order to keep the firms under the control of insiders. They used their vouchers and cash to gain ownership of their enterprise.

However, once Russian managers consolidated the alliance with employees, and found that insider privatization would successfully prevent their enterprises from being taken over by outsiders, they began to expand their ownership. Like the Chinese managers, a lot of Russian managers also wanted to obtain a controlling share of their enterprises. Many used various tactics to buy shares from workers and outside owners, in order to consolidate their position and power. From 1993 to 1996, the number of companies with big concentrated stakes (20 to 40 percent) by managers grew substantially in Russia. So, in a lot of privatized enterprises the insider privatization was further

transformed into *de facto* managerial privatization. The practices of MBO in Russia might also involve asset stripping, as managers may use the funds or loans of their enterprises to buy shares for themselves.

The author compared the ownership structure of small- and medium-sized privatized enterprises of the two countries, and found that in Russia insiders held 53 percent of the shares in 2000, of which managers held eighteen percent and workers held 35 percent;[20] and in China insiders held 57 percent of the shares in 2006, of which managers held 47 percent and workers held ten percent.[21] Since Russia stated privatization in 1992 and China started it in 1997, after eight or nine years the percentages of insiders' shares in privatized firms of the two countries were not significantly different; however, Chinese managers held many more shares than their Russian counterparts, and Russian workers held much more than their Chinese counterparts. The contrast seems to suggest that in Russia, even though managers did try to obtain more shares, they were unable to obtain as many as Chinese managers. Kozarzewski suggests that, when managers can control employee-shareholders with administrative methods, they do not have to buy-out the shares of employees.[22] This interpretation is challenged by China's manager privatization. In China, managers have

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[20] Carsten Sprenger, "Ownership and Corporate Governance in Russian Industry: A Survey," London, UK, *European Bank for Reconstruction and Development, Working Paper*, No.70, Jan. 2002, 4.

[21] Gan Jie, "Privatization in China: Experiences and Lessons," in James R. Barth, John A. Tatom, and Glenn Yago, eds. *China's Emerging Financial Markets: Challenges and Opportunities*, Berlin, Germany, and New York, NY, Springer, The Milken Institute Series on Financial Innovation and Economic Growth 8, 2008, 584.

[22] Piotr Kozarzewski, "Corporate Governance Formation in Poland, Kyrgyzstan, Russia, and Ukraine," in Robert W. McGee, ed. *Corporate Governance in Transition Economies*, 272.

even greater control over employees than their Russian counterparts, because they not only have administrative methods, but also power backed up by an authoritarian government; and, actually, about half of Chinese managers chose MBO. In the Russian case studies conducted by the author, it was also found that some Russian managers indeed did MBO and obtained 100 percent of the shares of their enterprise. The author would like to argue that it might be the social relations at the Russian workplace that made MBO more difficult in Russia than in China. Russian workers were allowed to participate in the early stage of the voucher privatization, and this has somewhat shaped the relations between managers and employee owners, and restrained managers' wishes or efforts to obtain the shares of their enterprises from employee shareholders. Unlike in Russia where employee shareholding was more or less a choice by workers, Chinese workers were asked, and sometimes were forced, by managers to buy the shares of their enterprises, and they have many fewer shareholder rights than their Russian counterparts; thus, Chinese managers were able to arrange MBOs with the support of government officials and against the resistance of workers. When obtaining controlling shares of their enterprises, quite often Chinese managers acted much more freely than their Russian counterparts at the workplace. More details about the management-worker relations in the two countries will be discussed and compared in this chapter.

2.2 The Corporate Governance under Managers' Dominance

After privatization was done, have ownership changes improved management of privatized firms in Russian and China? When analyzing corporate governance, economists often pay attention to large and listed companies where corporate governance is supposed to be better relative to that in smaller, non-listed companies, because listed companies must release board composition and financial information to the public to fulfill the disclosure requirements of stock market regulators. These practices of corporate governance may affect the stock price and the value of the firms. Ownership structures of listed companies in Russia and China are very different, but in the realm of corporate governance companies in the two countries have many of the same problems.

More than two thirds of the shares of Russian listed companies are held by large outside blockholders, managers, and minority shareholders,[23] whereas China's listed companies are mainly owned by the state, rather than private owners. From 1992 to 2004, more than 60 percent of the shares of Chinese listed companies were held by government organs; it went down to 55 percent in 2005[24] and has been relatively stable since then. It has been found that state-concentrated ownership has significant negative effects on market valuation of listed companies.[25] In Russia, on average, large outsider blockholders hold

[23] Olga Lazareva, Andrei Rachinsty, and Sergey Stepanov, "A Survey of Corporate Governance in Russia," in Robert W. McGee, ed. *Corporate Governance in Transition Economies*, New York, Springer, 2008, 318.

[24] Ma Shu-yun, "China's Privatization: From Gradualism to Shock Therapy?" *Asian Studies*, Vol.48, No.2, 201.

[25] Bai Chong-En, Liu Qiao, Lu Joe, Frank M. Song, and Zhang Junxi, "Corporate Governance and

about 35 percent of the shares and managers hold twenty percent,[26] employee shareholders are generally on the incumbent management side.[27] Therefore, Russian managers could act on behalf of employee shareholders who hold about twenty percent of the shares.[28]

Although primary owners are different in the two countries, both in Russia and China managers often dominate the board of directors of the listed companies. In China, about 80 percent of directors of the board of listed companies are either appointed by government offices or arranged by governmental agencies,[29] and more than half of the directors are current management team members.[30] In Russia, about 60 percent of the directors of the board are insiders.[31] In both countries, corporate law requires that listed companies must have independent board members; but, in Russia, as of 2009, about one third of the companies had not met that requirement.[32] When the board of directors does include independent board members, in the two countries, the independent directors of the board are either paid by CEOs (like the situation in China), or have close ties with the

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Market Valuation in China," *Journal of Comparative Economics*, Vol.32, 2004, 612.

[26] Olga Lazareva, et al, "A Survey of Corporate Governance in Russia," 318.

[27] Ibid, 318, 328-330.

[28] Ibid, 318.

[29] Liu Qiao, "Corporate Governance in China: Current Practices, Economic Effects, and Institutional Determinants," *CESifo Economic Studies*, Vol.52, No.2, 2006.

[30] Bai Chong-En, et al, "Corporate Governance and Market Valuation in China," 610.

[31] Olga Lazareva, et al, "A Survey of Corporate Governance in Russia," 329.

[32] Russian Economic School, "Corporate Governance Practices in Russia: 2004-2009 Comparative Study, New Trends in 2009," Moscow, Russia, 2010, p.27 (http://www.nes.ru/dataupload/files/events/news/CG_2004-2009_Eng.pdf).

management or the controlling shareholders.[33] China's company law does not restrict CEO from holding the position of the chairman of the board of directors; therefore, CEOs can play the double role, despite the obvious conflict of interest. In 2000, more than one third of CEOs were also the chairman of the board of directors;[34] in 2003 the ratio dropped to eleven percent.[35] "Russian federal legislation has made it illegal since 1996 for the same person to serve as both CEO and board chair at the same time." However, many CEOs in Russia continued to be chairman of the board of directors, and a 2002 survey found a negative correlation between this particular personnel arrangement and firm performance.[36]

The portion of insider board members in Russia and China is significantly higher than that in the U.S., where insider board members are usually no more than one third.[37] This implies that Russian and Chinese managers are highly interested in dominating the board of directors, and primary outside owners, whether private or government representatives, often do not see proper corporate governance through an effective board as a priority. Consequently, market mechanisms play a diminished role in CEO selection. Analysis of the

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[33] Olga Lazareva, et al, "A Survey of Corporate Governance in Russia," 330.

[34] Bai Chong-En, et al, "Corporate Governance and Market Valuation in China," 610.

[35] Huang Zhangkai, Xu Xinzhong, and Yue Yunxia, "*Zhongguo Shangshi Gongsi Dongshihui Jiegou Fenxi* (Analysis of the Composition of the Board of Directors of the Listed Companies in China)," Oct. 23, 2007.

[36] Robert McGee, "Corporate Governance in Transition Economies," in Robert W. McGee, ed. *Corporate Governance in Transition Economies*, New York, Springer, 2008, 6.

[37] Michael Useem, "Corporations and the Corporate Elite," *Annual Review of Sociology*, Vol.6, 1980, 54.

quality and social background of industrial managers in the two countries presented in chapters six and nine suggests that most managers are from the former communist managerial elite, and secured their positions despite the absence of either motivation or capability to improve their managerial skills. In both Russia and China CEOs and the chairmen of the board of directors often do not really understand what kind of role they are supposed to play from the perspective of modern corporate governance, and sometimes do not mind if they play multiple role at once.[38] Very often, the boards of directors in the listed companies of Russia and China are more like a managerial council, and spend too much time on tactical issues, which should usually be performed by management, [39] rather than acting as a body overseeing the CEO on behalf of shareholders. Thus, a lot of CEOs could enjoy exclusive authority and power in the companies.

Large companies in Russia and China are gradually improving their corporate governance; however, overall, corporate governance remains at a rather low level.[40] As of 2006, introducing efficient practices of corporate governance still depended upon the good will of CEOs in Russia. [41] In 2010, a survey found that only six percent of the

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[38] The Chinese Entrepreneur Survey System (CESS), "*Zhongguo Qiye Jingyingzhe Jiazhi Quxiang: Xianzhuang yu Tezheng-2004, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Characteristics of Value Orientation of Chinese Entrepreneurs: 2004, Special Report about Growth and Development of China's Entrepreneurship)," April 2004 (www.ceoinchina.com/Item/789.aspx).

[39] Olga Lazareva, et al, "A Survey of Corporate Governance in Russia," 330.

[40] Ibid, 341.

[41] Piotr Kozarzewski, "Corporate Governance Formation in Poland, Kyrgyzstan, Russia, and Ukraine," 276-277, 281.

interviewed CEOs of China's listed companies considered international standards of corporate governance a necessary reference, twelve percent admitted that they did not really follow China's rules regarding corporate governance, and reported that they did not feel real competition for their positions.[42]

Russia's stock market is quite small, and only 327 companies (including non-industrial companies) were listed at the end of 2011.[43] These companies comprise only about one percent of privatized industrial firms. China's stock market is much larger; but, at the end of 2011, only eight percent of large- and medium-sized industrial enterprises (1,329) were listed on stock market.[44] Obviously, the listed companies are only a very small portion in privatized firms, and the majority of the privatized firms, small- and medium-sized, are not listed.

When the small- and medium-sized non-listed firms are owned by a few owners and registered as LLCs, the conventional perception of corporate governance might not be applicable. According to China's company law, if a company only has a few owners or

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[42] Deloitte Accounting Firm, "*Gongsi Zhili, Ren Zhong Dao Yuan: 2010 Nian Zhongguo Shangshi Gongsi Zhili Diaocha Baogao* (Corporate Governance, A Heavy Task and a Long Way to Move: Survey Report about Corporate Governance of China's Listed Companies in 2010)," 2010 (www.deloitte.com/view/zh_CN/cn/services/corgov/6b5d1fa364f18210VgnVCM100000ba42f00aRCRD).

[43] World Bank, "Listed Domestic Companies, Total," visited on Sept. 11, 2012 (http://data.worldbank.org/indicator/CM.MKT.LDOM.NO).

[44] China's Association of Listed Companies, "*Zhongguo Shangshi Gongsi de Fazhan* (The Development of China's Listed Companies)," Beijing, China, the Website of China's Association of Listed Companies, visited on July 7, 2012 (http://www.capco.org.cn/zhuanti/cjz/xi_hylt.html).

the company is small, the establishment of the board of directors is not required.[45] In China, MBOs were widely adopted and about half of privatized firms are owned by managers; at the same time, at least ten percent of China's privatized firms are taken over by outside individuals. In such firms, manager-owners may feel it not necessary to establish a board of directors. Indeed, in 2002 about 40 percent of privatized small enterprises in China actually did not have a board of directors.[46]

In the West, employee-owned firms are common in the service sectors but relatively rare in industrial sectors, because industrial workers lack managerial skills and corporate governance experience.[47] In Russia and China, employee ownership turns out to be one of the most feasible privatization methods for industrial enterprises. After Russia completed its voucher privatization, insiders of industrial enterprises held quite a large portion of the shares; most Russian non-listed firms have many employee shareholders and are registered as LLSC. In China, about ten percent of small- and medium-sized privatized firms are owned by managers and workers. The author would like to emphasize that, besides the corporate governance of the listed companies, the study of corporate governance in Russia and China should also focus on the corporate governance of the non-listed firms which are jointly owned by employee shareholders and managers.

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[45] "*Zhonghua Renmin Gongheguo Gongsi Fa* (Company Law of the People's Republic of China)," Beijing, China, *Renmin Ribao* (People's Daily), Dec. 31, 1993, p.2.

[46] "*Zhongguo Siying Qiye Yanjiu Keti Zu* (the Research Group for Study of China's Private Enterprises)," "*Zhongguo Siying Qiye Diaocha Baogao* (Survey Report of Private Firms in China)," Beijing, China, *Caijing* (Finance and Economy Magazine), No.4, Feb. 20, 2003.

[47] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," 225-226.

However, previous studies of corporate governance in the two countries have not paid much attention to the issue.

Since both in Russia and China many managers and workers have become insider shareholders, might they work together for their own interests? Theoretically, they may have a greater incentive to improve performance, because they share in the benefits of improvement. However, if the shareholder rights of workers are not regarded by managers, employee shareholders may feel alienated.

According to Kryvoi, a typical voucher privatization outcome in Russia resulted in 60 to 65 percent of the shares going to managers and employees and about 20 percent to individuals and investment funds; the subsequent redistribution of corporate ownership led to a decline of employee shares.[48] Nevertheless, workers still hold about 35 percent of the shares, a quite large proportion, much more than that of managers.[49] Although workers may have voted the rank-and-file members into the board, in most privatized firms, the board of directors is dominated by managers; managers have retained their positions, and become the sole decision makers, whereas employee shareholders remain passive observers and wage earners, rather than co-owners. Managers also refuse to implement cumulative voting procedures mandated by law, which in effect disenfranchised employee shareholders.[50] The author found from his interviews in the

[48] Ibid, 226-227.

[49] Carsten Sprenger, "Ownership and Corporate Governance in Russian Industry: A Survey," 4.

[50] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," 222, 228, 233.

Moscow area that some outsider large-block shareholders did not have any seats on the board of directors or had some seats but did not exercise their governance power; employee ownership in a lot of enterprises did not offer the employee owners opportunities of oversight; and CEOs in a lot of enterprises gained full dominance over their employee owners with a smaller portion of shares. In Russia, the overall influence of employee shareholders on decision-making has been low and independent from their ownership, [51] and employee participation in enterprise management has been minimal. [52]

As analyzed in chapters eight and nine, in firms where the board of directors exists, managers' dominance in the boards of China's small- and medium-sized privatized firms is as same as in Russia, and the rights of employee shareholders have rarely been regarded. Chinese managers of privatized firms usually hold many more shares than their Russian counterparts, either through a partial MBO or by the "stock option" learned from the United States, which allows top managers to buy company shares at prices far below market value. [53] Managerial team members appointed by CEOs usually occupy most seats in the board of directors. Such a board composition offers CEOs exclusive authority and power on the board, and CEOs are often self-appointed or

[51] Derek Johns, "The Economic Effects of Privatization: Evidence from a Russian Panel," *Comparative Economic Studies*, Vol.40, No.2, 1998, 75-102; quoted from Garsten Sprenger, "Ownership and Corporate Governance in Russian Industry: A Survey," 8.

[52] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," 228.

[53] Michael Useem, "Corporations and the Corporate Elite," *Annual Review of Sociology*, No.6, 1980, 48.

nominally elected by the board of directors. Moreover, the board members often oppose selecting CEOs through market mechanisms, although it is possible to find better CEOs from foreign companies that operate in China.

The dominance of managers in the board of directors in the two countries implies that managers have successfully prevented selecting or changing CEOs by market mechanism. When conducting interviews in privatized enterprises in the Moscow area, the author found that, if some CEOs were replaced, candidates would very likely have been selected from within the companies. At the same time, the interests and rights of employee shareholders were very likely to be ignored.

2.3 How Do Management-Worker Relationships Differ?

The recent research in the sociology of organizations in advanced economies assumes that "most of the use rights and benefit rights that arise from corporate property have already been captured by managers," so the focus of research on corporate governance has moved from ownership to variables affecting organizational outcomes.[54] Kryvoi points out that the success of enterprises in transition depends largely upon the ability of managers to perpetuate a climate of common goals between workers and managers.[55] How have managers of the two countries reconfigured management-worker relationship?

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[54] David L. Kang, and Aage B. Sorensen, "Ownership Organization and Firm Performance," *Annual Review of Sociology*, Vol.25, 1999, 134.

[55] Yaraslau Kryvoi, "Employee Ownership and Corporate Governance in Russia," 227.

In order to understand their behavior, we need to know their background and value orientations. After privatization, most of the managerial elite in the two countries are former *nomenklatura* members. Although they can now be called entrepreneurs, whether they are good swimmers in a market economy is questionable. Having analyzed the characteristics of managers in Russia and China, the author finds that both Russian and Chinese managers encounter the same problem: socialization of many managers was completed during the Brezhnev or Mao era, and their managerial skills were usually accumulated through working experiences at the socialist workplace, rather than through systematic training in modern management practices. Moreover, many lack the abilities necessary to improve a firms' performance, and do not have strong motivation or pressure to improve their management skills. On the other hand, a lot of them are quite sophisticated in pursuing their personal interests, such as high salaries and conspicuous accommodations, at the cost of the companies.

Chinese SOE managers had experienced marketization for about two decades before privatization, and had accumulated experience in a market-oriented economy.[56] Indeed, in contrast to their Russian counterparts, the new Chinese entrepreneurs have obvious advantages, as the business environment in China did not change after the privatization, and the Chinese new entrepreneurs did not have to adapt to their new roles in a completely unfamiliar market environment, as Russian new entrepreneurs had to. Before

[56] Huang Yasheng, *Selling China: Foreign Direct Investment during the Reform Era*, New York, NY, 2003, 343.

privatization, Chinese SOE managers already enjoyed autonomous decision-making on matters of production, sales, pricing, purchases, investment, profit distribution, wages and bonuses, internal enterprise organization, and personnel. Right after the privatization, however, the percentage of Chinese managers who spent most of their time looking for new opportunities for enterprise development dropped significantly, while the percentage of those who devoted most of their time to maintaining relations with government offices increased. Several years later, those behavioral patterns had changed only slightly.

Pre-reform management-worker relations in the Soviet Union and China were characterized as paternalistic. After privatization, paternalist practices in Russia diminished, and were destroyed in China by the government and managers. From interviews the author finds that Russian workers believed that they should be protected by their workplaces, and their motivation was influenced by managers' promises of protecting workers; many managers recognized that they had to take the issue into consideration. But nationwide opinion surveys in Russia showed that, during and after the privatization process, about 25 percent of workers reported massive cutbacks in labor benefits; about 60 percent of them did not receive any fringe benefits, and only 40 percent received some goods and food at reduced prices, or financial assistance. Compared with Soviet paternalistic practices, the range of social protection for workers at the workplace significantly shrank in Russia; in many privatized enterprises paternalist practices were no longer a solid pillar of the management-worker relationship, though the ideological legacy kept

influence for years. The large-scale lay-off policy of the Chinese government before and during privatization actually denied the institutions based on which the previous dependence of SOE workers was built.[57] In the process of privatization and in the post-privatization practices, Chinese managers of small- and medium-sized privatized enterprises no longer provided workers reliable job opportunities or necessary benefits. In at least 60 percent of privatized enterprises, the employment status of workers became fragile, wages were kept low, and benefits were cut or cancelled.

In Russia and China, before privatization workers long believed that they were the masters of enterprise; after privatization, most Russian workers and a proportion of Chinese workers became shareholders in their enterprises. Do they now stand in a better position to defend their interests than before? With little consciousness and knowledge of how to act as shareholders, and discouraged by managers, employee owners in Russia and China often do not actively pursue their ownership rights; consequently, the boards of directors of privatized firms are usually dominated by managers, and employee shareholder participation is low. On the other hand, in both countries, labor unions are either under the control of managers or inactive, and workers are often not organized at the workplace. Therefore, after privatization, although workers hoped to be respected by managers, and had a strong desire to participate in the decision-making surrounding their interests, whether their voices were taken into consideration largely relied upon the

[57] Andrew Walder, *Communist Neo-Traditionalism: Work and Authority in Chinese Industry*, Berkeley, CA, University of California Press, 1986, 14-17.

willingness of managers, rather than proper corporate governance or negotiations between workers and managers.

Analyzing managers' attitudes towards political and workplace democracy and their own behavior, the author finds that in China about 60 percent of entrepreneurs supported the communist regime, and only a minority supported democratic values and institutions;[58] at the same time, about 60 percent of managers did not support workplace democracy,[59] and 73 percent declined to negotiate with workers.[60] The surveys of the China Entrepreneur Survey System (CESS) also found that many Chinese managers were reluctant to disseminate information to employees, and the majority of them lacked abilities in learning, expression and public relations, and were not good in appraising and placing personnel. In Russia, from the survey in the Moscow area, the author found that, among senior managers of eleven privatized firms, only two supported the workplace

[58] Chen Jie, and Bruce J. Dickson, "Allies of the State: Democratic Support and Regime Support among China's Private Entrepreneurs," *China Quarterly*, No.196, Dec. 2008, 792-793, 802.

[59] The Research Dept. of the All-China Federation of Trade Union (ACFTU), ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), Beijing, Chinese Workers' Press, 2006, p.1142. The question is "At your workplace, do you practise the meeting for earnest talk?" The meeting for earnest talk between workers and managers was an institution recommended by the official ACFTU in the late 1990s to promote workplace democracy. The percentage included answers of the CEO respondents who answered "No" or "Don't Know." The sample size is 260, including CEOs of LLCs, LLSCs and SOEs.

[60] Ibid, 1139. The question is "At your workplace, has the regular meeting for negotiation between managers and workers been practised?" The meeting for negotiation between workers and managers was another institution recommended by the official ACFTU in the late 1990s to promote workplace democracy. The percentage included answers of the CEO respondents who answered "No" or "Don't Know." The sample size is 261, including CEOs of LLCs, LLSCs and SOEs.

democracy policy and allowed representatives of employee shareholders to have seats in the board of directors; however, in other enterprises where managers negatively evaluated the workplace democracy policy, representatives of employee shareholders were excluded from the board of directors, even though from 10 to 98 percent of shares of those enterprises were held by employees. The attitudes of the managers in the two countries suggest that many of them may very likely choose an authoritarian-style management.

The value orientations of managers do shape management-worker relations at the workplace. In Russia, according to interviews conducted in the Moscow area, the author noticed that when managers negatively evaluated the idea of workplace democracy and disregarded the rights of employee shareholders, they maintained an authoritarian management-worker relationship, and employee shareholders had little influence. In these firms, although employee shareholders had a strong desire to play an active role as employee owners, their rights were not considered by managers; management in the enterprises was rough, not based on rules, regulations and records; the role of the labor union was reduced, and in some enterprises even dissolved after privatization; managers usually kept workers at a distance and often did not care about what they thought and felt; managers declined to share information with workers, and interactions and communication between managers and workers diminished after privatization. Workers felt that their situation was either not improved or had worsened after they became

shareholders in their enterprises, and after privatization their motivation declined. Moreover, after privatization a majority of workers were not satisfied with their CEOs, or their satisfaction had decreased.

The Chinese managers of privatized enterprises share a lot in common with their Russian counterparts in value orientations regarding the management-worker relationship. The most favorable pattern of management-worker relations among Chinese managers is the authoritarian pattern in which managers make decisions without listening to anybody else; the least favorable is the participation pattern, which encourages workers to participate in decision making and to share risks, and provides incentives for innovative work. An official survey in China on manager abilities reveals that the sharpest difference between Chinese managers and American managers lies in the attitude toward interpersonal relations at the workplace: American managers care more about understanding others, disseminating information, and participating in employee discussions, whereas many Chinese managers decline to disseminate information and participate in discussions with employees.[61] Chinese managers also lack the willingness to learn and take criticism from subordinates; instead, they are more used to an authoritarian leadership.

Much data from opinion surveys in China show that, being ruthless to their workers, many Chinese managers see their enterprises as a personal kingdom, while employment

[61] The CESS, "*Zhongguo Qiyejia Duiwu Chengzhang Xianzhuang yu Huanjing Pingjia: 2003, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Status and Environment of the Development of Entrepreneurship in China: A 2003 Survey)", June 2003 (www.ceoinchina.com/Item/646.aspx).

is often not protected by labor contracts, wages are cut, employee benefits diminished, working hours extended without extra pay, working hour limitations and much else are often violated, and dialogue between managers and workers is reduced after privatization. Only official labor unions can exist, and they work for managers to control workers and prevent them from organizing independently. Under authoritarian management, manager control is probably bureaucratic, but incentive structures might not be merit-based (wages are often not linked to education, professional capability, and tasks performed, and career development opportunities are absent), so workers' emotional ties to their work place are crippled, and their commitment is weakened. Such a management-worker relationship may serve industrial development for labor-intensive products that do not require highly-educated workers and much R&D. In other words, the management-worker relationship may not be supportive of technological innovation, but instead of a production process that takes relatively little skill and does not provide room for initiative. When such firms compete in the international market, their key advantages are only low labor costs and cheap prices. According to Jin, Lu and Deng, although China's exports have grown very rapidly, Chinese companies that produce the products have not much improved their own technologies; on the contrary, they rely heavily on the design, components, and equipment provided by their foreign partners, and make only a small amount of money in labor-intensive assembling.[62] From a long-run perspective the

[62] Jin Pei, Lu Tie, and Deng Zhou, *Zhongguo Gongye Jiegou Zhuanxing Shengji: Jinzhan, Wenti yu Qushi* (Transformation and Upgrading of China's Industrial Structure: Progresses, Problems and

weakness of the firms is obvious: if foreign companies find cheaper labor elsewhere and decide to move orders to other countries, Chinese firms will be hard-pressed to develop their own brands, designs, or reliable components and technologies for international market.

Both in Russia and China, the authoritarian management-worker relationship is widely to be found at the workplace, whether or not employee shareholders hold a large portion of the shares. Privatization in the two countries made managers the new master of the firms, but did not help in improving long-term competitiveness, because the retrograde management style restrains innovation and undermines any *esprit de corps* among the workforce.

A unique pattern of management-worker relations in China is worth nothing: the despotic, militarized, or paramilitarized management pattern is seen in some privatized enterprises. It has been discussed for years in China and is becoming popular recently in energy industries, such as coal mining and power supply, and in some firms in other industrial sectors as well. Militarized or paramilitarized management introduces the organizational forms, behavior standards, strict control, and discipline of military organizations into industrial enterprise management, so workers are guided to behave like soldiers, and managers' orders are implemented completely and unconditionally.[63] Some

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Trends), *Zhongguo Gongye Jingji* (China Industrial Economies), No.2, 2011.

[63] Bai Xiaoguang, and Fan Anxin, "*Shixing Zhun Junshihua Guanli, Cujin Meitan Qiye Fazhan* (Carrying out Paramilitarized Management, and Promote Development of Coal Mines)," *Cangsang* (Vicissitudes), Taiyuan, China, No.4, 2007.

interviewed workers complained that under militarized management they always felt nervous, and their personality and self-respect were injured;[64] but when the unemployment rate is high, they are in a weak position and cannot but obey. While emphasizing the efficiency of executing an order, militarized management treats workers as slaves, or a working machine without self-esteem, even though many of the employees are shareholders in their company. It is controversial in China, as the militarized management may foster hatred against managers, and is very unlikely to inspire enthusiasm, innovation, or loyalty. For workers, the privatization followed by the despotic management is not simply an ownership change: it is a culture shock that they dislike. The despotic militarized or paramilitarized management reinforces tensions between workers and managers; but workers can hardly challenge it, not only because they are now in a weaker position at the workplace than ever before, but also because the militarized management approaches are supported by the authoritarian government.

If the militarized or paramilitarized management-worker relationship is perceived as an extreme in China, one should not come to conclude that other privatized firms in Russia and China would all follow the authoritarian model when reconfiguring post-privatization management-worker relations. It is interesting that, in the case studies of eleven privatized enterprises in Russia, the author finds a unique enterprise, the Moscow Wallpaper Company, where management-worker relations could be characterized as

[64] Ye Tieqiao, "*'Zhun Junshihua Guanli' Jianwen* (Report about 'Paramilitarized Management')," Feb. 12, 2007, Beijing, *Zhongguo Qingnian Bao* (Daily for Chinese Youth).

cooperative. In that enterprise, which is fully owned by insiders, managers support the idea of workplace democracy and employee ownership; employee-shareholders have seats in the board of directors and can in some ways conduct oversight; and, while implementing formalized control over the workplace, managers have made efforts to improve interactions and communication between management and workers. As a result, employee-owners at the workplace are quite satisfied with their managers and perceive the management-worker relationship as better than ever. Under such a cooperative management-worker relationship, the performance of the enterprise has been quite successful. The case suggests that a cooperative management-worker relationship could grow in a privatized firm, if the value orientation of managers leads them to respect employees' co-ownership rights. It might not be an isolated case in Russia, because among the eleven interviewed enterprises, some characteristics of the management-worker relationship of the Moscow Wallpaper Company have been found in another enterprise. It is also possible that such management-worker relationship might be found in China, as there are some Chinese managers supporting the idea of workplace democracy, and some firms in China proclaim that they have practised various institutions to implement workplace democracy. [65]

[65] For instance, the labor union of the Hualing Xiangtan Iron and Steel Company has introduced practices for workplace democracy in the firm. See the Hualing Xiangtan Iron and Steel Company, "*Gonghui Gongzuo* (The Work of Labor Union), visited on Sept. 15, 2012 (http://www.hnxg.com.cn/xgfc/ghqt_mingzhu.asp). No responses from workers of the company are found.

The existence of the cooperative, authoritarian and despotic management-worker relationships implies that, after privatization, workplace relations in Russia and China are not identical. Management choice might be a key variable that determines what kind of management-worker relationship is built. On the other hand, under different sociopolitical conditions, privatization approaches and insider ownership structures, many managers of the two countries prefer the authoritarian style, and workers' legal rights as owners are restrained, if not ignored. If one compares the authoritarian management-worker relationship discussed in chapter six with the Chinese pattern described in chapter nine, he may find that the Chinese version of the authoritarian management-worker relationship is quite similar to its counterpart in Russia's privatized enterprises.

The authoritarian management is not fresh to scholars of industrial relations. From the late nineteenth century to the early twentieth century, American firm owners often employed informal or hierarchical control over their workshops: "The work tasks were organized and controlled by the continuous, direct, ad hoc, and arbitrary instructions," and workers "were enforced by positive rewards, by physical force, and/or by… dismissal;" using arbitrary commands, managers and foremen "became company despots encumbered by few restrictions on their power over workers;" the work motivation inherent in such control was simple: perform your task correctly or be docked in pay,

fired, or, on occasion, beaten.[66] The American workforce has been split into factions with different interests and has pursued separate interests in the political arena since the 1940s,[67] and management-worker relations in the United States have changed a lot. In the 1980s, managers were often expected to show their intelligence, ability, enthusiasm, honesty and fairness, as well as their willingness to learn from subordinates and ability to take criticism and acknowledge mistakes.[68] However, violations of employment and labor laws are still found today in cities like Chicago, Los Angeles, and New York, largely because workers there lack bargaining power.[69] After the communist managerial elite became entrepreneurs after privatization, it seems that many of them adopted an authoritarian style, and their attitudes towards former worker comrades become ruthless. Moreover, the despotic, militarized management observed in China has never been observed in a modern capitalist system, and is probably the product of an economic transition under a communist regime. The next section will compare workers' responses to authoritarian management in the two countries.

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[66] Richard Edwards, *Contested Terrain: The Transformation of the Workplace in the Twentieth Century*, New York, NY, Basic Books, Inc. 1979, 25-34.

[67] Ibid, 203.

[68] Charles Perrow, *Complex Organization: A Critical Essay*, New York, McGraw-Hill, Inc., 1986, 59.

[69] Annette Bernhardt, Michael W. Spiller, and Nilk Theodore, "Employers Gone Rogue: Explaining Industry Variation in Violations of Workplace Laws," June 22, 2012 (http://ssrn.com/abstract=2013376).

2.4 Labor conflicts and Protests in Russia and China

Under authoritarian or militarized management, confrontation between managers and workers at the workplace may lead to labor disputes and conflicts. Workers' responses to the changing management-worker relationships are diverse in Russia and China. One may reasonably assume that more labor conflicts and protests can be observed in Russia than in China, because in China strikes are banned and only pro-government demonstrations would be approved by the government, whereas in Russia protests and demonstrations are not prohibited, although the Russian government has become more and more authoritarian during the past decade.

Indeed, if one compares the percentage of labor conflicts or disputes at the workplace in Russia and China, he may find that during privatization process labor conflicts or disputes more frequently occurred in Russia than in China; but, after privatization labor conflicts decreased in Russia, but increased in China. When privatization just began in Russia, about 45 percent of the respondents to VCIOM opinion surveys reported conflicts between management and workers at their workplaces; as the privatization was completed in mid-1994, the percentage decreased: to 31 percent in September 1994 and 28 percent in March 1995. It then further fell to thirteen percent in 2001.[70] In contrast to the total number of Russian

[70] Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.3, 1993, 44, No.2, 1994, 75; No.4, 1994, 63; No.6, 1994, 70; No.3, 1995, 88; No.6, 2001.

industrial enterprises, the percentages mean that, on average, at least 9,000 conflicts occurred in 1993, 5,700 in 1994, and 2,500 in 2001. In China, the official All-China Federation of Trade Unions (ACFTU) found from its 2002 survey that, from 1998 to 2002 when the large-scale privatization was carried out, in about 13 to 14 percent of privatized enterprises, labor disputes took place, mainly caused by workers' grievance against privatization practices and employment and wage issues.[71] It is worth noting that the post-privatization dynamics of labor conflicts in China presents a growing trend, opposite to that of Russia. The total number of labor disputes taking place in *gaizhi* firms rapidly increased from 19,000 in 1996 right before the large-scale privatization was initiated,[72] to 63,000 in 2005 when the privatization had been done for years.[73] The data suggests that Chinese workers were more compliant than their Russian counterparts during privatization, but became more and more active in fighting for their demands after privatization.

In Russia, during and right after the voucher privatization (from 1993 to 1995), the main causes of labor conflicts were poor wages, poor working conditions or lack of work,

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[71] The Research Dept. of the All-China Federation of Trade Union (ACFTU), ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 2006, 1186, 1190.

[72] Wang Zhenqi, "*Woguo Laodong Zhengyi Chuli Zhidu Huifu Shi Zhounian Jiankuang* (Brief Review of Labor Dispute Arbitration in the Past Ten Years)," Beijing, *Zhongguo Laodong Kexue* (Labor Relation Studies in China), No.10, 1997.

[73] Zhang Yanning, and Chen Lantong, eds. *2006 Zhongguo Qiye Laodong Guanxi Zhuangkuang Baogao* (The Status of Labor Relations in China's Enterprises: A 2006 Report), Beijing, The Press for Enterprise Management, 2006, 83, 87.

managers' privatization practices, and their poor attitudes toward workers. It is notable that only about fifteen to twenty percent of labor conflicts in Russia were caused by managers' privatization practices.[74] In contrast to the situation in China, where 34 percent of labor conflicts in LLCs and 23 percent in LLSCs were caused by managers' privatization practices,[75] the voucher privatization in Russia has seemingly caused less labor conflicts than the spontaneous privatization in China. Moreover, the dissatisfaction of Russian workers with their managers regarding the issues above often did not lead workers to organize collective action. In the peak years of labor conflicts, although worker's economic conditions were very poor and their job security was under threat, strikes in Russia were fairly short and limited in scale, and appeared to be directed against the government rather than managers.[76] For instance, in the VCIOM surveys, about 20 to 25 percent of employee respondents reported that massive layoffs occurred during the period from 1994 to 1997,[77] and about twenty percent

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[74] Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.3, 1993, 44, No.2, 1994, 75, No.3, 1995, 88.

[75] The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 1190.

[76] Penny Morvant, and Peter Rutland, "Russian Workers Face the Market", *Transition*, June 28, 1996, 6-11.

[77] Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No. 2, 1993, 63; No.3, 1993, 71, No.6, 1993, 49; No.3, 1994, 54; No.4, 1994, 70; No.6, 1994, 71; No.3, 1995, 79; No.2, 1996, 89; No.6, 1997, 85; No.6, 2001, 87.

mentioned that the threat of redundancy caused labor conflicts at the workplace, but only about three percent said that workers organized collective action against dismissals.[78] In the circumstances of the transitional economic recession, from 1993 to 1995 about 30 percent of the respondents reported that alienation among workers arose from the competition to keep one's current job, and would reduce their willingness to unite for collective action; on the other hand, under the threat of lay-offs, many Russian workers chose individual actions, such as looking for other jobs (about 30 to 40 percent) or trying to ingratiate themselves with managers to gain their help (about twelve to twenty percent), rather than struggling against managers.[79] Such actions could explain why the worsened management-worker relationship did not lead to more collective actions at the workplace in Russia.

After privatization, why do not Chinese workers behave as their Russian counterparts do? At least in three aspects, Chinese workers encountered different circumstances from that of their Russian counterparts. First, instructed by the state policy for a nationwide lay-offs, dismissal occurred at almost every workplace in China, whereas in Russia it occurred only in about 20 to 25 percent of workplaces; and the scale of dismissal in China was much larger that that in Russia, as about half of SOE workers were laid off in a short period in China. Obviously, Chinese workers would have many more difficulties in finding jobs than their Russian counterparts if

[78] Ibid, No.2, 1993, 55, No.6, 1994, 76-77, No.3, 1995, 79, No.2, 1996, 89, No.2, 1997, 87.
[79] Ibid.

they were fired. Second, the privatization practices, such as MBO, that could trigger workers' resistance, were more widely adopted in China than in Russia; thus, Chinese workers are more likely dissatisfied with the privatization practices that benefit managers at the cost of workers than their Russian counterparts are, and the privatization practices may cause more conflict between management and workers in China than in Russia. Third, Chinese managers of privatized firms still have political authority backed up by the authoritarian communist government, and could be more ruthless than their Russian counterparts who now do not have the political power at the workplace; therefore, workers' voices and demands are more likely to be ignored in China than in Russia. It is thus understandable that, although Chinese workers, under the communist authoritarian rule, were more compliant than their Russian counterparts during privatization, the lower percentage of labor conflicts at Chinese workplaces by no means implies that there was less tension in privatized firms in China than in Russia.

When workers' grievances and discontent accumulate, labor disputes can arise rapidly, including even street protests. After privatization, the widely adopted style of authoritarian management reinforced tensions between workers and managers. Political risks for Chinese workers who protest are much higher than for their Russian counterparts. But if Chinese workers with grievances have no choice, they may well bring pressure to bear on their managers through street protests. In 2002, when labor disputes took place, Chinese workers either negotiated with managers or looked to

government offices to help; in about 30 to 40 percent of labor disputes, workers could not find any channel for resolution, either because managers refused to negotiate, or because the government declined to intervene; and, among all the labor disputes, about 60 to 70 percent were not resolved at all.[80] In 2007, of all labor disputes, 32 percent were not resolved, and 43 percent were only partly resolved.[81] The 2007 survey by the ACFTU found that, if there were labor dispute at their workplaces, 61 percent of worker respondents wanted to participate in protests.[82] According to a recent report by the China Labor Bulletin (CLB), from 2001 to 2011 the main protest approach was to strike. Although the ACFTU encourages workers to take an alternative approach through collectively negotiating with managers, in 553 cases of collective action the CLB found none where collective negotiation helped resolve the problems that caused the protests.[83]

In China, most worker protests were suppressed, activists in the strikes or protests were arrested, and in some cases sentenced to prison for years. Analyzing 26 cases of labor protests that took place from 2002 to January 2012, the author found that grievances were all rooted in the schemes or consequences of privatization: lay-offs, asset stripping,

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[80] The Research Dept. of the ACFTU, ed. *Zhongguo Zhigong Zhuangkuang Diaocha, Di Liu Pian, Diaocha Shuju Ziliao* (Survey of the Status of Chinese Staff and Workers in 2002: Vol.6, Survey Data), 2006, 1196, 1177.

[81] The Research Dept. of the ACFTU, "*Woguo Zhigong Sixiang Daode Zhuangkuang Yanjiu* (Study about the Thought and Moral Views of Staff and Workers in China)," Beijing, *Gongyun Yanjiu* (Labor Movement Studies), No.16&17, Sept. 2008.

[82] Ibid.

[83] The China Labor Bulletin, *Gongren Jiti Xingdong Shiyi Nian: Jiyu 533 ge Ge'an de Fenxi* (Workers' Collective Actions in the Past Eleven Years: Analysis Based on 553 Cases), Dec. 2011 (www.clb.org.hk).

delayed or unpaid redundancy compensation, MBO, and income disparities between managers and workers. Even though the protests were not well organized, half of the protests involved more than 1,000 participants. Managers were often rude to workers and refused to negotiate; nine protests were violently suppressed by police; and in only four cases did the managers and local governments compromise and the workers gain some concessions, while in other cases the protests met with no success (see chapter nine).

2.5 Performance of Privatized Enterprises

Right after the voucher privatization was done in Russia and the privatization of small- and medium-sized SOEs was completed in China, some scholars did surveys to evaluate performance of privatized enterprises, and concluded that the immediate effects of privatization in the two countries were not positive. In Russia, Perevalov, Gimadii and Dobrodei found that the voucher privatization did not produce performance improvements, except for costs per unit of revenue and to some extent for productivity of labor, and, on average, did not have any influence on employment. [84] Earle and Esrtrin suggested that the voucher privatization in Russia seemed to have a clear and substantial effect on productivity, but its effect on the restructuring of product lines and employment (layoffs) was much less clear. [85] Reviewing the

[84] Yurii Perevalov, Ilya Gimadii, and Vladimir Dobrodei, "Does Privatization Improve Performance of Industrial Enterprises? Empirical Evidence from Russia," *Post-Communism Economies*, Vol.12, No.3, 2000, 351, 356.

[85] John S. Earle, and Saul Estrin, "Privatization versus Competition: Changing Enterprise Behavior

research about the post-privatization enterprise performance in Russia, Moers concluded in 1999 that privatization per se did not bring the better performance that many thought it would.[86] In China, Yusuf, Nabeshima and Perkins found that the restructuring effort of privatization in China did not improve the efficiency of the privatized firms and the actual impact of restructuring was quite limited.[87] Garnaut, Song, Tenev and Yao observed a fluctuation pattern of the profitability of privatized enterprises, as it dropped before privatization, went up right after privatization, then declined again.[88]

After privatization in the two countries had been carried out for more than four or five years, research into performance of privatized enterprises began to show some positive signs. In Russia, Estrin and Bevan found in 2001 that ownership and performance were not yet well correlated, and there was no evidence of outsider-owner firms outperforming insider-owned ones, but 75 percent of the firms in their sample were able to generate profits.[89] Examining the productivity data of privatized firms from 1985

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in Russia," International Institute for Applied Systems Analysis, *Working Paper*, No. 96-049, May 1996.

[86] Luc Moers, "What Determines Enterprise Performance in Russia? A Survey of the Evidence," Tinbergen Institute, Amsterdam, the Netherland, *Tinbergen Institute Discussion Papers*, No.99-077/2, Sept. 22, 1999, 15.

[87] Shahid Yusuf, Kaoru Nabeshima, and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, Washington, DC, the International Bank for Reconstruction and Development/ the World Bank, 2006, p.151-155, 208.

[88] Ross Garnaut, Song Ligang, Tenev, Stoyan, and Yao Yang, *China's Ownership Transformation: Process, Outcomes, Prospects*, Washington, DC, the International Finance Corporation and the International Bank for Reconstruction and Development/ the World Bank, 2005, 159, 161.

[89] Saul Estrin, and Alan Bevan, "Determinants of Russian Enterprise Performance," *Comparative Economic Studies*, Vol.45, No.2, June 2003.

to 2002, Brown, Earle and Telegdy concluded that the impact of privatization in Russia remained negative until the fifth year after privatization. From five to fourteen percent of the productivity improvements were observed in Russia in 2002, though the privatization effect was obviously poorer than that in Romania and Hungary.[90] In China, Guo, Gan and Xu conducted a nationwide survey in 2006 and reported that there appeared a significant improvement in performance in firms that were privatized.[91]

Evaluating the performance of privatized enterprises in Russia and China is in fact a difficult and controversial task: it requires both reliable data and the appropriate methodology. For instance, in China, it was found that prior to privatization managers of SOEs reduced profitability and productivity in order to obtain the enterprises through MBOs easily and at a cheaper price; after the privatization the profitability returned to the level it was at before it declined. The U-shape movement of profitability may mislead scholars.[92] In Russia, during the economic crisis in the first half of the 1990s and in the financial collapse of August 1998, barter in industrial sales became popular, and

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[90] J. David Brown, John S. Earle, and Álmos Telegdy, "The Productivity Effects of Privatization: Longitudinal Estimates from Hungary, Romania, Russia, and Ukraine," *Journal of Political Economy*, Vol. 114, No. 1, February 2006, 61-99.

[91] Guo Yan, Gan Jie, and Xu Chenggang, "A Nationwide Survey of Privatized Firms in China," *Seoul Journal of Economics*, 2008, Vol.21, No.21, 18-20.

[92] Susan F. Lu, and David Dranove, "Profiting from *Gaizhi*: Management Buyouts during China's Privatization," Dec. 2009 (http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1348277); Liu Xiaoxuan, and Liu Shaojia, *Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (A Research Report on SOE Gaizhi), May 2005 (www.sachina.edu.cn/download.php?optype=channel&channelid).

managers often tried to keep their profits at very low level, if not zero.[93] The estimates researchers made, used to reinforce their conclusions, did not take this socioeconomic background into proper consideration. This includes research findings about the performance of privatized enterprises in both Russia and China. On the other hand, methodologically, while analyzing profit rates, how one can identify real improvement in performance from within the results of economic fluctuations remains a topic that was not discussed by the scholars. In Russia, the economic recovery since 2000 would certainly raise the profit rates of privatized enterprises. But so far we still do not know if the reported increase in profit rates is caused by improvement in performance, or by the expansion of demand and increases in product prices. The same is true in China. In the latter half of the first decade of the 21st century, China experienced an economic boom sustained by growing exports, a huge amount of government investment projects, and a real estate bubble; but in 2012, China has begun to fall into a recession, and the profit rates of most enterprises dropped rapidly.[94] If one compared the profit rates of enterprises prior to privatization with those from 2006, and 2012, he might get contradictory conclusions regarding the post-privatization performance of the firms. Readers of the reports on the performance of privatized enterprises in Russia and China should carefully assess the

[93] Clifford Gaddy, and Barry Ickes, "Russia's Virtual Economy," *Foreign Affairs*, Vol. 77, No. 5, September/October 1998; "The Virtual Economy and Economic Recovery in Russia," May 1, 2001 (http://www.brookings.edu/research/articles/2001/05/russia-gaddy).

[94] Pei Minxin, "Everything You Think You Know About China Is Wrong," *Foreign Policy*, Aug. 29, 2012.

conclusions drawn from the annual profit rates of the firms, and consider the extent to which those numbers reflect performance improvements.

As privatizations in the two countries failed to produce immediate improvements in the performance of the firms, and evaluations of their later improvements are questionable, one may want to know why the privatizations did not work as expected. Analysis so far has suggested that Russia and China encountered the same problems.

The lack of ability of Russian and Chinese managers is one important reason. Right after China's privatization of small- and medium-sized SOEs, in an entrepreneur survey more than 40 percent of managers admitted that their quality was low, while another 50 percent considered their quality fair.[95] Explaining the performance of privatized firms, Yusuf et al. pointed out in 2006 that, although China had experienced a marketization process since the 1980s, domestic competition had no real impact on firm productivity.[96] Three years later, Chinese managers of privatized enterprises were reporting that only 30 percent of their time was spent on investment and marketing, and about fifteen percent was spent on dealing with government offices, whereas R&D and looking for new opportunities for enterprise development occupied only a very small portion of their time.[97] In Russia,

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[95] The CESS, "*Zhongguo Qiyejia Duiwu Chengzhang Xianzhuang yu Huanjing Pingjia: 2003, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Current Status and Environment of the Development of Entrepreneurship in China: 2003, Special Report about Growth and Development of China's Entrepreneurship)."

[96] Shahid Yusuf, Kaoru Nabeshima and Dwight H. Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises*, 193.

[97] The CESS, "*Zhongguo Qiye Zhanlue, Xianzhuang, Wenti, ji Jianyi: 2010, Zhongguo Qiye Jingyingzhe Chengzhang yu Fazhan Zhuanti Diaocha Baogao* (Enterprise Strategy in China, Current

from 1993 to 2000, only about ten to sixteen percent of employee respondents reported that their managers did actively search for new supplies and sales markets; and until June 2001, seven years after the voucher privatization was completed, it was only 29 percent; only after 2000 did a small portion of enterprises begin to develop new products for market.[98] In 2001, a nationwide opinion survey in Russia showed that only five to seven percent of workers, and thirteen percent of technician, perceived that the efforts of their managers had yielded positive results for their enterprises.[99]

Secondly, manager-owners of privatized enterprises do not necessarily see maximizing profits as the priority. After gaining control of their enterprises, they are apt to use firm resources to meet their personal needs, even though the enterprises are not making much profit to begin with. When the author conducted interviews in the Moscow area in 1997, some worker interviewees said that their managers spent a lot of money in building new offices or traveling abroad. Perevalov et al. pointed out in 2000 that Russian managers "could be interested only in quick enrichment." As new owners who received ex-state equity very cheaply, they may have strong incentives not to

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Status, Problems and Proposals: 2010, Special Report about Growth and Development of China's Entrepreneurship," April 2010 (http://www.ceoinchina.com/Item/16713.aspx).

[98] Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.2, 1993, No.4, 1994, 70; No.6, 1994, 72; No.3, 1995, 79; No.2, 1996, 89-90; No.2, 1997, 87; No.2, 2000, 71; No.6, 2001, 87.

[99] Ibid, No.6, 2001, 86.

maximize profit, but to make their equity liquid by privatizing it completely—transferring it to foreign bank accounts or by some other means.[100] In a 2001 nationwide opinion survey, 16 to 22 percent of Russian employee respondents thought that their managers were not really interested in improving their enterprises, as their personal interests did not necessarily depend on the performance of the company.[101] In China, Garnaut et al. also found that management shares had negative and significant impact on labor productivity;[102] and Liu and Liu reported that, in contrast to other privatized enterprises, the firms that were privatized into the hands of managers made the least investments after the privatization, even less than companies owned by employees.[103]

The third, but not the least important, factor that may have a negative impact on enterprise performance is the management-worker relationship. The ruthless treatment of workers under an authoritarian management system can trigger tension and undermine morale. How the performance of privatized enterprises in Russia and China correlates with how managers treat workers remains an unexplored research topic. It would require a large-scale survey looking at both financial information and opinions at the workplace.

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[100] Yurii Perevalov, Ilya Gimadii and Vladimir Dobrodei, "Does Privatization Improve Performance of Industrial Enterprises? Empirical Evidence from Russia," *Post-Communism Economies*, Vol.12, No.3, 2000, 339.

[101] Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), No.6, 2001, 86.

[102] Ross Garnaut, Song Ligang, Stoyan Tenev, and Yao Yang, *China's Ownership Transformation: Process, Outcomes, Prospects*, 168.

[103] Liu Xiaoxuan, and Liu Shaojia, "*Guoyou Qiye Gaizhi Chongzu Diaocha Yanjiu Baogao* (Research Report on SOE *Gaizhi*)," May 2005.

Such research would not be easy in either country, and so far no one has conducted it.

3. What Do We Learn from Privatization in Russia and China?

This research on privatization in Russia and China has explored how the state, managers, and workers shape the privatization, what motivates them, and how they interact. Under different political conditions, Russia and China initiated their privatization. While Russia promoted a voucher program, China pushed forward a nationwide spontaneous privatization of small- and medium-sized SOEs. In both countries employee shareholding was practised, and many workers are now shareholders and hold a large portion of shares; but they still lack negotiation power. Most Russian and Chinese managers are able to dominate, rather than being overseen by, the board of directors, if the board exists; and an authoritarian management-worker relationship has been established in many privatized firms in the two countries. Although the dogma of state socialism, that workers were the masters of enterprise, shaped worker attitudes, and policies of workplace democracy were carried out before and during the privatizations in the two countries, ultimately, both in Russia and China, most SOE managers arrogated to themselves the role of the new “masters of enterprise,” whether they held controlling stakes in the shares or not. The new masters of privatized enterprises do not necessarily see profit maximization as their priority. Asset stripping during and after privatization has

been widely observed in China and Russia, but in neither country have the laws and regulations necessary to prevent asset stripping been made, and in most situations such activities have not been penalized. In many privatized enterprises the new manager-owners established an authoritarian management-worker relationship, and many workers in the two countries felt worse off after privatization, because workers' social status was lowered, their working conditions became poorer, and benefits were reduced. While Russian workers are often not organized at the workplace, the occasional unorganized collective actions of Chinese workers failed to improve their conditions.

How should the developments in privatized enterprises in Russia and China be interpreted? The explanatory power of corporate governance and labor relations theories seems to be limited at this juncture: the former emphasizes questions of ownership, corporate structure, and institutions of oversight, while the latter focuses on the united struggles of workers under democratic institutions. Following from the empirical investigations undertaken from chapters four to nine, the author would like to further analyze three issues of theoretical interest in economic sociology, political science and political sociology.

3.1 Interpreting Consequences of Privatization from Perspective of Economic Sociology

The changing social relations at the workplace during and after privatization should be a core concern of scholars in the field of transitions from state socialism to capitalism. Ownership change of public property in transitional societies is not simply a series of economic transactions or a legal issue; it is embedded in social relations. Interests are always socially defined, and they can only be realized through social relations.[104] The factors that shape the perceptions of managers and workers on issues like property rights, managerial power, and the position of workers, and what the relationship is between their perceptions on these issues and the choices they make during the privatization process, have not been fully taken into consideration in privatization policymaking or explored in the literature.

The author has discussed the value orientations of managers and workers, and the interactions between the two groups in Russia and China during privatization. It was found that outcomes in privatization are shaped by social relations at the workplace, and also by social relations among bureaucrats, SOE managers, and private businessmen.

First, the existing social relations in the enterprises that link managers and workers may help the two parties form an alliance against outsider owners through manipulating the

[104] Richard Swedberg, "The Economic Sociology of Capitalism: An Introduction and Agenda," in Victor Nee and Richard Swedberg, eds. *The Economic Sociology of Capitalism*. Princeton, NJ: Princeton University Press, 2005, 5.

ownership structure and corporate governance, as seen in the first stage of Russia's voucher privatization. Western literature on employee ownership usually appraises its strength and weakness according to conventional efficiency standards.[105] But the lessons of Russia's voucher privatization suggest that managers and workers select employee ownership not because of concerns over efficiency; instead, their actions are based on a temporary mutual dependence.

Second, privatization is a process of redistributing wealth and power. If SOE managers get tacit approval or support from governments, as seen in China's spontaneous privatization, they may manipulate the wealth redistribution to benefit themselves at the cost to workers. If government officials or former *nomenklatura* cooperate with private businessmen or SOE managers, wealth redistribution may become a free banquet for these attendees. Many of the practices in the privatization of Russian large SOEs and in China's spontaneous privatization have well shown that. In either situation, privatization can be manipulated into a "piratization."[106]

Third, in the power structure that has dominated the socialist workplace for decades, workers are usually in a weak position. Managers' role in institution building during and after privatization had been poorly understood before privatization was initiated in Russia

[105] John S. Earle, and Saul Estrin, "Employee Ownership in Transition", in Frydman, Roman, Cheryl W. Gray, and Andrzej Rapaczynski, eds. *Corporate Governance in Central Europe and Russia, Volume 2: Insiders and the State*. Budapest: Central European University Press, 1996, 17.

[106] Marshall Goldman, *The Piratization of Russia: Russian Reform Goes Awry*, London, Routledge, 2003, 32.

and China. Such a power structure may weaken the role of corporate governance or employee ownership, as found in the second stage of Russia's voucher privatization, and could pave the way for manager-led spontaneous privatization as observed in China. Fourth, the relations among workers after privatization are often driven by individual tendencies to retain jobs. The changing social relations among workers within their work organization militate against the possibility of collective action, and undermine the resistance of Russian workers to management privatization after voucher privatization.

Privatization has produced a new structure of ownership and power at the workplace, and reshapes social relations at the workplace as well. The author has identified three new management-worker relationships at the workplace, drawn from observations in Russia and China. The cooperative management-worker relationship found in a Russian firm shows the possibility that social relations at the workplace in a former communist country can evolve to something close to the expected pattern in the United States,[107] and, some managers, although they were socialized in the cradle of communist revolution, may adopt such practices if they embrace the idea of democracy. However, such managers are apparently a minority. The most striking phenomenon in terms of management-worker relations in the two countries is the organizational isomorphism under authoritarian management. Such an isomorphism is not the result of

[107] Charles Perrow, *Complex Organization: A Critical Essay*, 59.

outside pressure, nor is it related to technological or environmental uncertainty.[108] The author has not found any evidence that Russian and Chinese managers learnt from each other in adopting the authoritarian pattern. My findings about their similar value orientations and working habits suggest that an isomorphism of manager characteristics may lead to organizational isomorphism. From the point of view of the sociology of production,[109] patterns of management-worker relations can have a large influence on production processes in firms.

3.2 The Role of the State in Privatization

A communist authoritarian state, like the one in China, is often assumed to be strong, whereas the Russian state is weaker, at least during the years after the collapse of the Soviet communist regime, with much less capacity for the state to assert its power. Is the privatization under a weaker state more spontaneous than that under a stronger state? When problems of Russian privatization have attracted attention, scholars have often accused the regime of a low capacity to intervene. For example, some Russian scholars call the privatization in the country a *nomenklatura* privatization and think the government is responsible for the consequences. Also, others believe that without democratization,

[108] Paul J. DiMaggio, and Walter W. Powell, "The Iron Cage Revisited: Institional Isomorphism and Collective Rationality in Organizational Fields," in Walter W. Powell and Paul J. DiMaggio, eds. *The New Institionalism in Organizational Analysis*, Chicago, IL, The University of Chicago Press, 1991, 63-82.

[109] Richard Swedberg, "The Economic Sociology of Capitalism: An Introduction and Agenda," 13-20.

the Russian managers would not have had the chance to operate in a legal vacuum. But the arguments ignore that in the Chinese case, *nomenklatura* privatization in a legal vacuum did take place under an authoritarian regime. The Chinese authoritarian government played a much weaker role in the privatization of small- and medium-sized SOEs than its Russian counterpart did in voucher privatization, although the hand of the former is obviously stronger, particularly when it comes to suppressing worker protests and promoting economic growth. Rather than actively intervening in the process to minimize asset stripping by SOE managers, the Chinese government chose inaction, and postponed the setting of rules, creating a vacuum where a legal framework for privatization should have been.

Most Eastern European countries did privatization earlier than China, and their rich experiences and lessons could have helped the Chinese government prepare a better privatization program. Obviously, lacking capability or experience is not the reason the Chinese government took a hands-off approach during the privatization process. The real problem is that the Chinese central government did not have motivation to prevent spontaneous privatization from taking place; instead, it minimized its fiscal burden to subsidize the restructuring SOEs and establish a social security system for privatization. Therefore, it removed the load on local governments and SOE managers, and, in exchange, allowed them to act in whatever ways they liked. Such a role of the state in privatization seems similar to a corporate actor, possessing its own interests, but not representing the

interests of most social groups.[110] For the same reason, the Chinese government carried out a large-scale lay-off policy in SOEs. In contrast, during voucher privatization, the Yeltsin regime did respond to requests from different social groups, and the goals of the Russian government for the voucher privatization were largely shaped by political forces with various interests. However, it is undeniable that the same Russian regime later adopted the spontaneous privatization of large SOEs for its fiscal needs.

The vacuum of a legal framework is not a unique problem in Russia. China has the same problem. Both the Russian government and the Chinese communist regime are weak in enforcement of civil laws. Unlike Western countries where the rule of law has taken deep root in society and politics, in Russia and China the legal framework for privatization—company law, labor law, and financial market regulations—often has only a weak regulating role. Under the communist leadership, the communist party and its government possesses a superior position, above the law. The communist tradition, that the elite manipulate law enforcement for their own interests and without sanction, still has strong influence in the two countries. Many of the practices during and after privatization in both countries are questionable from the point of view of criminal and civil laws of the West, but both the Chinese and Russian government tacitly approved them. Without a deeper understanding of the imperfect legal environment in the two

[110] Dietrich Rueschemeyer, and Peter B. Evans, "The State and Economic Transformation: Toward an Analysis of the Conditions Underlying Effective Intervention," in Peter B. Evans, Dietrich Rueschemeyer, and Theda Skocpol, eds. *Binging the State Back In*, Cambridge, UK, and New York, NY, Cambridge University Press, 1985, 47.

countries, one can hardly apprehend why laws often do not work properly there.

3.3 How Does Social Reconstruction Affect Economic Transition?

This issue refers to the impact of sociopolitical transformation on economic transition. The growth of markets depends upon the environment in which they are planted. In a communist or former communist country, capitalism can not flourish by decrees issued by the President or a central government, while the institutional soil in which a market economy must take root is ignored.[111] The Central European post-communism societies experienced a reconstruction characterized by anti-communism, which greatly helped the economic transition. This was missing in Russia, and is completely impossible in China.

Why did *nomenklatura* privatization prevail in Russia and China? Is this a phenomenon common to all transitional societies? Actually, *nomenklatura* privatization is not new for transitional societies. In the early 1990s, many scholars pointed out precisely this possibility,[112] and, according to Burawoy, one of the major points of the World Bank's shock therapy was how to prevent it from occurring.[113] Analyzing the transition processes in Central Europe and Russia, Eyal, Szelenyi and Townsley found that there was relatively little evidence of this sort of development in Central Europe, but they suggested that the

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[111] Michael Burawoy, "From Sovietology to Comparative Political Economy," in Daniel Orlovsky, ed. *Beyond Soviet Studies*, Washington DC, the Woodrow Wilson Center Press, 1995, 89.

[112] For example, Elemer Hankiss, *East European Alternatives*, Oxford, UK, Clarendon Press, 1990; Jadwiga Staniszkis, *The Dynamics of the Breakthrough in Eastern Europe: Polish Experience*, trans. Chester A. Kisiel, Berkeley, CA, University of California Press, 1991.

[113] Michael Burawoy, "From Sovietology to Comparative Political Economy," 86.

nomenklatura privatization was more likely to occur in Russia and China.[114]

Before China completed its nationwide privatization, in world history only the democratic and democratizing regimes, or authoritarian regimes which did not oppose capitalism, had carried out the task. Now a new and different case has been added to the historical record. China's privatization suggests that such a task can also be done in a country ruled by a communist party, but it turns out to be a *nomenklatura* privatization. It could be argued that under the communist leadership this is an unavoidable consequence of building capitalism, because the *nomenklatura* members are not restrained from manipulating privatization for their personal interests, and are actually acting under institutionalized support and protection. If this is the case, what about Russia? Russia already began its initial stage of democratization twenty years ago, why was privatization in Russia significantly different from that in the democratized Czech Republic, Hungary, Slovakia and Poland, but similar to the China model?

Using the case of Poland, Goldman suggests that if the implementation of privatization in Russia had been postponed, there would have been less asset stripping.[115] The author would argue that the key factor that caused *nomenklatura* privatization and asset stripping was not the timing of privatization, or whether shock therapy was adopted; instead, it is the political context, or the linkages between politics and socioeconomic

[114] Gil Eyal, Ivan Szelenyi, and Eleanor Townsley, *Making Capitalism without Capitalists: The New Ruling Elites in Eastern Europe*, London and New York, Verso, 1998, 4-5.
[115] Marshall Goldman, The Piratization of Russia: Russian Reform Goes Awry, 207-208.

transformation, that matters. The economic preconditions of privatization in Poland and China were similar: while a private economy existed widely for years, farmers or peasants worked on their land (privately owned or leased), and memories of market activities remained in people's minds in both countries. A key difference between Poland's privatization and China's is that in the latter's the *nomenklatura* was unrestrained. In Russia, the managerial *nomenklatura* enjoyed some of the same privileges as their Chinese counterparts.

Contrasting the sociopolitical conditions and approaches of the policy makers of privatization in the Czech Republic and Russia, Appel explains why the path of privatization in the two states was very different. In the Czech case, she notes, both institutionalized and informal manifestations of anti-communism had a great impact on society; in Russia, however, anti-communism was less prevalent in political discourse.[116] She did not further analyze how anti-communist manifestations influenced sociopolitical transformation in the Czech Republic, but Eyal, Szelenyi and Townsley have explored the topic.

Analyzing the ideology and practices of the post-communist power elite of the Central European counties, Eyal, Szelenyi and Townsley state that the monetarist ideology of the technocratic portion of the elite, based on the Chicago school of

[116] Hilary Appel, "The Role of Ideology in Privatization Programs: Reconsidering the Determinants of Liberal Economic Reform, Lessons from Privatization," the speech at Woodrow Wilson Center, Oct. 25, 1999 (http://www.wilsoncenter.org/index.cfm?event_id=3813&fuseaction=events.event_summary).

economics—i.e. a vision of how society, markets, firms and individuals can be led, coordinated and monitored—is shared by all parts of the post-communist elite; on the other hand, the ideology of dissident intellectuals, the ideas of civil society in pursuing a life beyond socialism, also had dominant influence in the Central European societies. The latter not only discredits the authoritarian and aggressive nature of state socialism against human rights, but also indicts communist rulers as the henchmen of the Russian empire.[117] Moreover, the dissident intelligentsia conducted three social practices, or three rituals of post-communist life, that helped along sociopolitical transformation in Central European societies: sacrifice (requiring every social member to live beyond their means under socialism, and to sacrifice for the sake of the future of a free society), purification (denouncing that in the communist period both individual and collective consciousness were polluted and deficient, and asking all former socialist citizens to be purified through new civic education), and confession (recalling all the crimes against human nature under communist rule, impressing on the public that virtually everybody either engaged in crimes or failed to resist the system, and that, if one confesses, forgiveness is granted).[118] In these countries such ideologies and practices won wide social support, partly because of their link with patriotic-religious traditions.

[117] Gil Eyal, Ivan Szelenyi, and Eleanor Townsley, *Making Capitalism without Capitalists: The New Ruling Elites in Eastern Europe*, 86-94.

[118] Ibid, 102-112.

In Russia, although several technocrats in the Gaidar administration under the Yeltsin regime held to at least a sort of monetarist ideology, and much of the Russian intelligentsia sought genuine civil society, such ideas were challenged by the communist discourse maintained by *nomenklatura* members, and encountered the resistance of emotions or complicated psychological defense mechanisms[119] of many Russian people. Beyond that, the ideologies of monetarism and civil society have often been discredited by proponents of Russian nationalism and patriotism. The challenges and resistance can best be observed in the conservative Russian parliament, the Russian Congress of People's Deputies, where most seats were occupied by former *nomenklatura* members in the 1990s.[120] Under such a political environment, it is hard to image that Russian dissident intellectuals would be able to initiate a successful campaign to eliminate the communist legacy as their Central European counterparts had.

Therefore, sociopolitical development in Central Europe and Russia moved ahead in different directions. In Central Europe, economic transition and democratization were accompanied by a rapid social transformation that reshaped people's minds and values away from the communist legacy. But in Russia, the anti-*nomenklatura* sentiment during the last years of the Soviet Union and in the early years of the post-Soviet era did not

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[119] Moshe Lewin, "Society, Past and Present, in Interpreting Russia," in Daniel Orlovsky, ed. *Beyond Soviet Studies*, Washington D.C., the Woodrow Wilson Center Press, 1995, 59.

[120] Mervyn Matthews, "Elitism in Post-Communist Russia: Some Interim Comments," in James R. Millar, and Sharon L. Wolchik, eds, *The Social Legacies of Communism*, New York, Woodrow Wilson Center Press and Cambridge University Press, 1994, 314-316.

completely deny communist rule and ideology, and privatization and the initial democratization were pushed forward with only feeble and slow attempts to reduce the influence of communist discourse. In the sphere of political culture, the necessary reconstruction of society for democracy and free economy was never properly conducted.

Consequently, post-communism social consciousness and values of Central European societies significantly differ from that of the majority of Russian population. For example, public opinion surveys done from November 1991 to November 1992 in Poland, the Czech Republic, Slovakia, and Hungary showed that only 18 to 26 percent of respondents in the four countries supported the idea that "a government should guarantee the basic economic needs of its people;"[121] but, in Russia, when asked "do you agree with the statement that the state is to provide every citizen with the minimal subsistence," 85 percent of respondents said yes.[122] Before the collapse of the Soviet Union, an opinion survey done in February 1991 found that only 18 percent of Russian respondents thought "socialism in the USSR was flawed from the beginning and could never meet the people's needs," whereas 31 percent thought "there were possibilities in Soviet socialism but these are already exhausted," and 37 percent believed that

[121] James R. Millar, and Sharon L. Wolchik, "Introduction: The Social Legacies and the Aftermath of Communism," in James R. Millar, and Sharon L. Wolchik, eds, *The Social Legacies of Communism*, 14-15.

[122] The Intercenter and VCIOM, *Ekonomicheskiie i Sotsial'nae Peremenay: Monitoring Obshchestvennego Mneniia, Informatsionnay Bulletin* (Economic and Social Change: Monitoring the Pubic Opinions, an Information Bulletin), Moscow, Russia, Aspect Press, No.1, 1994, 64. The survey was done in October 1993, and its sample size was 2,018.

"socialism in the USSR is sound and has a future;" and the percentages to the answers from age cohorts 18-29 were respectively 25, 45 and 21.[123] After the demise of the Soviet Union, a survey done in January 1992 revealed that 54 percent of Russian respondents thought that "it is a great misfortune that the Soviet Union no longer exists," while in the 18-29 age cohort the percentage was 42, and in the cohort of 50 years old and above it was 66 percent.[124]

The efforts of the Central European intelligentsia for a more or less thorough social transformation had a great impact on economic transition and, as Appel points out, discredited the demands of labor and made managers reticent, thus preventing the two groups from shaping the design of privatization.[125] For instance, Czech reformers linked the creation of the new property regime to the founding of a post-communist national identity.[126] Moreover, in Central European countries economic measures were often attributed with different meanings from that in Russia and China. In the Czech Republic, Hungary and Poland, budget cuts and budget-balancing acts often did not serve primarily economic purposes, but represented a ritual calling for sacrifice as exercises in civic education; cutting welfare budgets was a call for sacrifice from people, and an attempt to purify the population of welfare dependency. Beneficiaries of socialist paternalism were

[123] Richard B. Dobson, "Communism's Legacy and Russian Youth," in James R. Millar, and Sharon L. Wolchik, eds, *The Social Legacies of Communism*, 240-241.
[124] Ibid, 246-247.
[125] Hilary Appel, "The Role of Ideology in Privatization Programs: Reconsidering the Determinants of Liberal Economic Reform, Lessons from Privatization."
[126] Ibid.

called upon to confess; and downsizing and lay-offs were not merely technical steps required to restore the economy to health, also ritual sacrifices meant to purify society and individuals, so that the laid-off workers would have to atone for their sins in state socialism by becoming more efficient, flexible, responsible, and skilled.[127] During the transition period, in Central European countries about a third of the former economic elite became downwardly mobile, shifting from elite economic positions, and about half of them ended up in early retirement; some former socialist managers did maintain their decision-making power in enterprises, and in most situations they used their social capital and managerial experience to keep their positions and exercise power, but owned little property of their firms. MBO was not the major form of privatization in these countries, and only about a fifth of those who were members of the *nomenklatura* before the collapse of communist rule held ownership of businesses; most were very small firms.[128]

The author would like to argue that the broad social reconstruction observed in the Central European countries, once ruled by communist regimes that were externally imposed, could hardly take place in the transition of Russia and China that were cradles of communist revolution. In Russia, there were no strong social forces to support the reconstruction, and it was certainly not an option found acceptable by the Chinese

[127] Gil Eyal, Ivan Szelenyi, and Eleanor Townsley, *Making Capitalism without Capitalists: The New Ruling Elites in Eastern Europe*, 115-157.
[128] Ibid, 115-142.

communist regime. While social capital of managerial factions of the Russian *nomenklatura*, which was highly institutionalized in the Soviet era, has remained predominant in the post-Soviet Russia,[129] the political capital of managerial factions in the Chinese *nomenklatura* guarantees their superior positions at the workplace. Russian privatization policies reflected a strong reliance on material incentives, but ideological legitimacy was absent; on the other hand, Russian liberal technocrats granted certain privileges to SOE managers and workers, in order to buy support and ensure compliance with the new ownership regime. As a result, the legitimacy and power of many groups who benefited from the Soviet regime was strengthened (or at least not weakened), which affected their ability to advance their claims to public assets during the reformulation of the ownership regime.[130] In China, the communist regime actually protected the *nomenklatura* privatization through strict political control over the media, workers, and liberal intellectuals. It can also be found that, defending their interests, Russian and Chinese workers share a feeble "weapon of the weak,"[131] the idea of workplace democracy endorsed by communist ideology. Actually, the "weapon" implies that the workers still accept the values proclaimed by communist ideology, though in China workers do not really have any other choice. The use of such a "weapon" could simultaneously reinforce

[129] Ibid, 21.

[130] Hilary Appel, "The Role of Ideology in Privatization Programs: Reconsidering the Determinants of Liberal Economic Reform, Lessons from Privatization."

[131] The term of weapons of the weak was introduced by James Scott in his *Weapons of the Weak: Everyday Forms of Peasant Resistance* (New Haven, CT, Yale University Press, 1985).

the ideological legitimacy of the *nomenklatura* members, and has often turned out to be ineffective to improve workers' status.

As a concluding remark, the author wishes to state that in the past two decades many Western observers, and Russian and Chinese people also, believe that Russia and China have moved along two different tracks: Russia has carried out privatization and marketization under a post-communist regime, while China has promoted marketization without political change. There is no doubt that their progress on the two tracks has not been, and will not be, identical. But the finding of the author's research suggests that, in fact, in both countries *nomenklatura* privatization has greatly shaped marketization and produced similar modes of management-worker relations. The similarities reflected in the *nomenklatura* privatization process remind us that, in many aspects, Russia and China encounter the same problems.

Unlike in Central European countries, where the transition from state socialism led to democracy, a free economy, and civil society within a rather short period, the journeys of transition in Russia and China may both be much longer— perhaps lasting several more decades. Without the real social reconstruction that occurred in Central Europe, Russia's economic transition has moved ahead with the result of a backsliding into a capitalist *nomenklatura*-authoritarian rule. China's economic transition has produced a unique

communist capitalism,[132] a new capitalism manipulated by the communist party, a first to be observed in world history. The rich lessons of Russia and China have left many unexplored questions for scholars of transitology.

[132] Michael Burawoy, "From Sovietology to Comparative Political Economy," in Daniel Orlovsky, ed. *Beyond Soviet Studies*, 93.

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