1 The advance of the state in China: the power of ideas

Two combinations of four characters have much to reveal about change in the Chinese economy. In 2004, Hong Kong economist Larry Lang raised the alarm about corrupt management buyouts (MBOs) of state-owned enterprises (SOEs) and applied the phrase 'retreat of the state, advance of the private sector' (*guotui minjin* 国退民进) to the ills of SOE privatization. Lang's public skewering of refrigerator tycoon Gu Chujun for acquiring state assets at below market value stirred controversy on the mainland, leading ultimately to Gu's arrest and an end to officially sanctioned MBOs. A few years later, the same characters arranged in slightly different order described a very different trend. In the wake of the 2008 Global Financial Crisis, a series of high-profile takeovers of private enterprises by China's central-level SOEs gave rise to a new, and quickly ubiquitous, phrase: 'advance of the state, retreat of the private sector' (*guojin mintui* 国进民退). In the span of less than a decade, in other words, hand-wringing about the Chinese economy has come full circle. Whereas concern once focused on curtailing private entrepreneurs' predations in the weakened state sector, policy debate now centres on how to shield private enterprises from the unwanted advances of massive and centrally backed SOEs (*yangqi* 央企). What has happened?

The analysis offered here finds that the advance of the state in China is a longer-term and slower process than the above vignette would suggest. Commentators have sometimes characterized central SOE assertiveness since 2008 as marking a turning point in Chinese economic development – as a decision for state capitalism and against slow but steady marketization (e.g. Wines 2010). A closer look at the evidence shows that the state's advance reaches much farther back in time. To be sure, the Chinese government's US $586 billion post-crisis fiscal stimulus plan, which heavily favoured the state sector, did play to the advantage of large SOEs and hastened the 'retreat' of private enterprises from several industries including steel, real estate and airlines. But this was a moment of culmination more than inception. Today's muscular *yangqi* are, in some measure, the product of twenty years of sustained effort to mould state-owned national champions in key industries. While previous work has focused on the contribution of institutions and interests to the advance of the state, this study demonstrates the formative role played by ideas, stressing the economic *and* political significance of state-controlled large enterprise groups.

The advance of the state: events, debate

The phrase 'advance of the state, retreat of the private sector' entered common parlance along with events linked to the Global Financial Crisis of 2008–9. While SOEs have long enjoyed privileged access to financial resources as compared to non-state enterprises, the government's 2008 fiscal stimulus plan was interpreted by some as having substantially boosted the competitive advantages of SOEs, above all SOEs under the authority of the central government, as well as hastening the retreat of private enterprises from certain industries. Unveiled in November 2008, the US $586 billion stimulus plan was subsequently tied to the implementation of the 'Ten Industries Revitalization Plan' (2009) which aimed to promote industrial consolidation via mergers and acquisition as well as technological upgrading in the steel, auto, shipbuilding, textiles, light industry, non-ferrous metals, equipment manufacturing, IT and logistics industries. Since industrial SOEs in these industries tend to be much larger than private enterprises, industrial consolidation often squeezed non-state enterprises into state-owned enterprise business groups (Economist Intelligence Unit 2009: 23). Perhaps the most audacious example of consolidation by administrative fiat took place in Shandong Province where the Rizhao Company, a thriving private steel enterprise, was heavily pressured by the provincial government into accepting a takeover by struggling state-owned Shandong Steel in September 2009. In the wake of the financial crisis, *guojin mintui* was also seen to be taking place in a number of other key industries. Chapter 3 examines the phenomenon of *guojin mintui* in the airline industry more closely.

As some domestic commentators have pointed out, China was hardly alone in marrying fiscal stimulus to industrial policy in the immediate post-crisis period. But the deep resonance, if also the fuzziness, of continuing debate about *guojin mintui* in China is distinctive. In late 2012, a little more than four years after the collapse of Lehman Brothers, at a time when public discussion had moved well past arguments for and against bank bailouts and nationalization of industry in other crisis-afflicted countries, *guojin mintui* was said to be the single most important matter of economic policy at the Eighteenth Party Congress, the occasion for Xi Jinping and Li Keqiang to take over national leadership from Hu Jintao and Wen Jiabao. Indeed, in his opening remarks to the Congress, outgoing General Secretary Hu Jintao strived to appease both camps. In one breath he called for 'enhancing the vitality of the state-owned sector of the economy and its capacity to leverage and influence the economy' before declaring that the government ought to 'unswervingly encourage, support, and guide the development of the non-public sector' (quoted in Rabinovitch 2012).

In the fray, it is not always clear just what, or whom, is being indicted. As Li Zheng points out, the phrase *guojin mintui* is very much open to interpretation:

> The 'state' (*guo*) and 'private' (*min*) in 'advance of the state, retreat of the private sector' are all unclear, making it easy to have misunderstandings. To be specific, *guo* can refer to the country, to the state economy or to SOEs. *Min* can indicate the public, the private economy or private enterprises. And 'advance' (*jin*) and 'retreat' (*tui*) could each refer to long term or short term, qualitative or quantitative, active or passive forms of advance or retreat. (Li 2010)

Indeed, defined as an aggregate ownership trend, a number of prominent economists have argued that *guojin mintui* does not in fact exist, since, economy-wide, the proportion of state ownership in industry continues to decline while the share of non-state forms of ownership marches ever upwards (Hu 2012; Ma 2010; Wei and Zhang 2010; Li 2010). Nicholas Lardy points out that, by 2011, SOEs produced just 26 per cent of industrial output with non-state firms accounting for nearly all the rest (Lardy 2014: 20).

Others contend that the aggregate trends do not do away with arguments for the existence of an advancing state. In a detailed analysis of *guojin mintui*, economists from the Unirule Institute, a think-tank known for advancing views at right angles to the official line, concede to *guojin mintui* sceptics that, while the share of SOEs contribution to gross industrial output continues to fall, 'in certain resource-based and basic industries, the role of state-owned capital has increased' (Sheng and Zhao 2012: 155). They also find that the degree of industrial concentration in several industries increased between 2002 and 2007, including elements of the non-ferrous metal, tobacco and oil industries (ibid. 132). The analysis concludes, too, that industries with the highest levels of concentration were those home to the largest proportion of SOEs.

Others understand *guojin mintui* as nothing less than an about-face in China's approach to economic development, one that, while difficult to pinpoint in the official statistics, nevertheless represents a profound break with the past. Wang Hongqie writes:

> Some scholars think that the current *guojin mintui* is not a few isolated events but has become a general trend; it is not the behaviour of a few individual enterprises, but is quite common among SOEs, especially central SOEs; it is not a few industries, but is widespread in many important industries; it is not limited to a few upstream, so-called related-to-people's-livelihood-and-state-security-natural-monopolies but touches on many other industries. (Wang 2010: 16)

As discussed below, to some participants in China's 'theory world' (*lilunjie* 理论界), *guojin mintui* has contributed to a reform stall.

What is beyond debate in this empirically murky and often emotionally charged discussion is that central SOEs are a force to be reckoned with. This is itself a remarkable turn of events and, to some observers, the growing economic clout, size and political influence of central SOEs constitutes the primary evidence for an advancing state and a retreating private sector, even if the aggregate numbers might suggest a different conclusion. Yasheng Huang (2008), for example, offers the controversial conclusion that the apotheosis of private sector development actually took place in the 1980s after which point the tide began to turn, slowly but surely, against rural private enterprises in particular, as government at all levels placed steadily greater emphasis on building up large, state-owned enterprises in urban areas. In recent years, the central government has stressed the importance of the hundred-odd central SOEs under the State Council 'going big and going strong' (*zuo da zuo qiang* 做大做强), by which is meant expanding the scale of SOE business groups via mergers and acquisitions while improving their competitiveness. One study finds that, in accordance with this policy, the largest state-owned business groups have rapidly scaled up in recent years. In 2000, 538 parent company SOEs controlled a total of 6,805 subsidiaries and had an average of 12.6 subsidiaries each; in 2007, a smaller number of parent company SOEs – 301 – held fewer total subsidiaries (5,002) but the average number of subsidiaries per SOE had risen to 16.6 (Lee and Kang 2010: 221). Within this group, the 131 business groups under the watch of either the State Council or central government are particularly dominant. Of China's 2,926 business groups, these central groups, which account for just 4.5 per cent of the total number of registered groups, held 48 per cent of total assets and contributed 42 per cent of total revenue in 2007 (ibid. 220). This, too, has generated controversy. In recent years, some have characterized the expanding scale of central SOEs as predatory: 'More than a few scholars as well a segment of public opinion see the efforts of central enterprises to get bigger and stronger as 'central ferocity' (Wang 2010: 16). Central SOEs are not only growing, they are also suddenly awash in cash.

Since China's debt-ridden SOEs were once albatrosses around the necks of Chinese leaders, the surging profitability of state-owned, large enterprise groups in the so-called 'monopoly sectors' (*longduan hangye* 垄断行业) is perhaps the most significant, and certainly the least anticipated, change in the Chinese economy since the turn of the century. In 1998 just 31 per cent of all SOEs were reported to be profitable, as compared to 57 per cent of SOEs in 2007 (Zhongguo Caizheng Nianjian 2008: 429). Yet these official figures largely reflect strong profitability among central SOEs. Many provinces with a large state sector continue to struggle even after the massive restructuring efforts of the late 1990s. Official figures record that between 2001 and 2009 central SOE net profits more than quadrupled. While there can be no doubt that state sector profitability has remarkably improved, there are good reasons to treat these numbers cautiously (Sheng and Zhao 2012: 51). First, despite notable improvements in data-gathering and measurement, official figures published by the National Bureau of Statistics are still seen as lacking reliability (Koch-Weser 2013). Second, economists caution that this surge in profitability (see Figure 1.1) should not be too easily interpreted as evidence of vastly improved economic performance. While today's SOEs tend to be better managed and shoulder lighter social obligations than they did prior to restructuring, state sector profits are padded by certain non-market benefits which are generally not extended to non-state enterprises. In particular, large SOEs often acquire resources at below market rates, enjoy lower financing costs than non-state enterprises and receive various forms of government subsidies (Sheng and Zhao 2012: 51–73).

The central SOEs advance is not taking place evenly across industry, however. They are the leading players in just a select few strategic industries, although their tendrils extend deep into many non-priority, 'competitive' industries. As defenders of the status quo have pointed out, this development is aligned with a government policy first outlined in the late 1990s. The Fifteenth Party Congress (1997) first established the guiding principle for pruning the once-universal state economy such that SOEs were to remain the 'commanding presence' in 'lifeline industries and key areas' but could begin to retreat from non-priority sectors in which non-state enterprises were expected to become the dominant force. Following years of clamorous internal debate about how exactly to define 'lifeline industries' and 'key areas' (cf. Eaton 2011: 86–93), the central government finally signalled, in late 2006, the industries from which SOEs would not retreat. Although the associated central government policy was actually more ambiguous and non-committal than many observers realized at the time, this was the first time a central bureaucracy had put a name to the 'lifeline industries' in which SOEs were to maintain absolute control, namely: defence, power grid, petroleum and petrochemicals, telecommunications, coal, civil aviation and shipping.[1]

[1] In December 2006, the State Council issued an important policy on SOE retreat and advance, which was widely interpreted as having clearly demarcated the industries from which SOEs should retreat and those in which they should advance. Indeed, in the official *Xinhua* media report of the press conference, the policy is made to sound crystal clear on the matter of which industries count as lifeline industries: 'the state sector should maintain absolute control in national security and lifeline industries including in the seven big industries: defence, the power grid, petroleum and petrochemicals, telecommunications, coal, civil aviation and shipping.' In fact, the actual text of the policy says only vaguely that the 'state's controlling force' should increase in 'important industries and key areas'. Interviewees suggested that the marked discrepancy between the *Xinhua* version of events and the actual text of the policy reflects a last-minute difference of opinion between SASAC and the State Council (10BJ0629; 10BJ0702). The press release version listing seven lifeline industries reportedly reflects the contents of a SASAC report

Central SOEs in these strategic industries – regarded as the stars of China's 'national team' (Sutherland 2001)[2] – are every bit a 'commanding presence' and, behind high administrative barriers to entry, they have contributed the most to the surge in SOE profits in recent years. In 2009, petrochemical enterprises industries that were relatively off limits to private capital accounted for 32 per cent of total SOE profits, and SOEs in telecommunications, another protected sector, contributed 20 per cent of the total (Sheng and Zhao 2012: 40).

And while the expanding market share of non-state enterprises in non-priority sectors explains why the overall proportion of state ownership continues to fall, the sprawling business groups under these national champion SOEs include lines of business well outside of their core domains. An internal report drafted by the bureaucracy charged with managing these behemoths, the State-Owned Assets Supervision and Administration Commission (SASAC), acknowledged that, in spite of a concerted effort to focus central SOE business on their designated core areas of business (*zhuye* 主业), national team subsidiaries remained 'too broadly' dispersed across Chinese industry and were found in fully eighty-six of China's ninety-five official industries (SASAC 2007: 166). The shadowy role of central SOEs in one such non-lifeline industry, China's booming urban real estate markets, has earned them public opprobrium as well as the epithet 'land kings' (*diwang* 地王). One study finds that a surge in real estate investment by central SOEs in connection with a flood of stimulus funds in the immediate post-crisis period fuelled a housing bubble in 2009, the effects of which are still being felt (Deng *et al.* 2011)

In the context of China's internationalizing economy, the so-called advance of the state has implications well beyond Beijing. The national team's increasingly bold 'going forth'（*zou chu qu* 走出去）into global markets has brought the phoenix-like rise of central SOEs to the world's attention. Anyone who has spent time in Beijing cannot fail to notice Sinopec's imposing headquarters opposite the Ministry of Foreign Affairs on Chaoyangmen Dajie, a potent reminder of the state-owned oil giant's record of multi-billion-dollar investments around the world. Besides the massive resource enterprises, China's

which had been submitted to the State Council and which was supposed to have accompanied the policy that was unexpectedly rejected by the higher level.

[2] There is some confusion about the precise origins of the term 'national team' in the literature on Chinese business groups. Dylan Sutherland (2001) was the first to use the phrase 'national team' in the English secondary literature to describe the so-called trial group enterprises under the central government's authority; however, it seems to have had some currency among Chinese policymakers and academics prior to that publication. For instance, a 1992 article by Sun Xiaoliang, a scholar and member of the State Commission for Restructuring of the Economy (SCRES), the organization with primary responsibility for the trial groups at the time, wrote of the importance of developing a 'national team' (*guojia dui* 国家队) to compete with global players (Sun 1992: 27).

Table 1.1: *Mainland enterprises on the Fortune Global 500 list (2003, 2014)**

	2014		2003	
	Number	**% of total (Global 500)**	**Number**	**% of total (Global 500)**
Total mainland enterprises	95	19	12	2.4
Total state-owned enterprises (SOEs)	71		10	
	Financial (Huijin)	**Non-financial (SASAC)**	**Financial**	**Non-financial**
Central-Level SOEs	5	46	4	6
Top five mainland enterprises (Fortune 500 rank)	1. Sinopec Group (3) 2. China National Petroleum (4) 3. State Grid (7) 4. Industrial and Commercial Bank of China (25) 5. China Construction Bank (38)		1. China Petrochemical Corp. (68) 2. State Power Corporation of China (77) 3. China National Petroleum Corporation (83) 4. Industrial and Commercial Bank of China (213) 5. China Telecommunications Corporation (228)	

Source: Fortune Global 500 annual ranking, available at: fortune.com/fortune 500.
*The year 2003 is chosen as a comparator since that was the first year that China's current state asset management system came into existence. With a few exceptions, China's central-level SOEs in non-financial sectors fall under the authority of SASAC. Responsibility for oversight of the largest central-level financial institutions lies with Central Huijin Investment Ltd.

service sector SOEs are also increasingly active in global mergers and acquisitions markets. And prior to the Global Financial Crisis, global capital markets were kept busy with a wave of big-ticket 'red chip' SOE initial public offerings (IPOs) that peaked with the world's biggest-ever listing: the Industrial and Commercial Bank of China's 2006 offering for US $19 billion. Yet these IPOs made the national team enterprises public companies in name only; foreign and non-state investors were sold minority stakes that did not entail a substantive transfer of corporate control away from the state (Walter and Howie 2010). The national teams' overseas listings have helped them quickly advance up the ranks of the Fortune Global 500, a closely watched list in Beijing which is often treated as a measure of central SOEs' success in 'going big and going strong'. In 2003, only twelve mainland enterprises were to be found on the Fortune 500 list, of which ten were SOEs. By 2014, the total number of Chinese companies had jumped to ninety-five, of which fifty-one are central-level SOEs.

The question now on people's minds is whether this 'advance' of central SOEs is a cause for celebration or despair. While the dramatic reversal of fortunes in China's state sector is understandably a source of pride for SASAC officials as well as senior SOE managers, the pages of a new corps of liberal-leaning mainland media outlets such as *The Economic Observer* and *Caixin*, as well as social media sites, are littered with complaints about profiteering and official corruption in the so-called 'monopoly sectors'. In a biting piece surveying the challenges and achievements of thirty years of economic reform, *éminence grise*, Wu Jinglian, described the state economy in perilous terms as evidence of a reform stall:

> In the beginning of reform, much of the initial resistance came from ideology but now it comes mainly from vested interests . . . state-owned monopolies and government departments have been enjoying the fruits of reform for a long time and further reforms will harm their interests. Pushing reform of the state-owned monopolies and that of the political system means that the government will have to reform itself. Consequently, reform has entered a more difficult battle and progress has slowed significantly. (Wu 2009)

Scholars critical of the state's advance argue, too, that the huge increase in government investment and the ever-expanding base of SOEs is gradually dragging down the efficiency of the entire economy (Zhan 2013). Tian Guoqiang (2011) argues that *guojin mintui* is indicative of a mistaken approach to economic development in China, which he see as predicated on a 'three heavies, three light' (*san zhong san qing* 三重三轻) principle: 'heavy on government, light on market; heavy on national wealth, light on people's wealth; heavy on development, light on service'. Reflecting on such criticisms, former head of SASAC, Li Rongrong, articulated what many SOE reform insiders see as something of a bitter irony: 'I don't understand it: why it is that when SOEs did poorly you swore (*ma* 骂) at them and now that they are doing well, you also swear at them?' (quoted in Wang 2010: 16).

Other influential economists contend that what we are seeing is not the betrayal of reform but rather its fruition. Influential Tsinghua professor, Hu Angang, argues that the hybrid economy now emerging in China offers both a sensible and a durable basis for a market economy with Chinese characteristics, one which brings into play the relative strengths of private and state-owned enterprises:

> In the socialist market economic system, state-owned enterprises and private enterprises play different roles. In market competition, state-owned enterprises are more like an elite field army. They are resource-intensive, capital-intensive, technology-intensive enterprises and their core mission is to engage in fierce competition with the world's top 500 companies and Global 2000 enterprises. Their aim is not only to take their place in this group, but also to rise rapidly to become industry leaders. Private enterprises are more like regional forces. They are job-creating, labour-intensive and employment-intensive

enterprises, which can effectively help local development, while at the same time making use of private enterprises' advantages in flexibility and innovation to gain prominence in international competition. (Hu 2012)

Others with similar views suggest that when Wu Jinglian and other liberal-minded economists characterize the increasing heft of central SOEs as contrary to the spirit of reform, they in fact misunderstand the very spirit they invoke. Whereas liberal economists have assumed, or perhaps hoped, that China's gradual reform would lead SOEs to the margins of the economy and eventually into oblivion, others argue that this was never the outcome envisioned by state leaders in the reform era. Two Renmin University economists suggest that SOE reform has always been a task of curing and strengthening rather than harm reduction and euthanasia: 'The basic aim of SOE reform has been to use institutional innovation to help SOEs adapt to the requirements of market competition so that they could become the main body of the market (*shichang jingji zhuti* 市场经济主体) and develop strength in market competition, in this way fruitfully combining the socialist system of public ownership with the market' (Lin and Zhang 2013: 12).

The debate outlined above has at its heart the question of what an advancing state could portend for the future of China's economic development. For social scientists and others drawn to trying to form an image of reform-era China in the long view, there remains the all-important, backward-looking *why* questions to dissect. The following pages turn, for clues about the deep causes of the advancing state, to three master concepts of social science inquiry: interests, institutions and ideas. While there have been a number of interesting and insightful studies of this topic, broadly conceived, in the institutionalist and interest traditions, there has as yet been comparatively little analysis from an ideational perspective, a void this study begins to fill.

Seeking the origins of the state's advance

China studies scholars have sometimes been accused of engaging too seldom and too listlessly with theoretical developments in the social science disciplines (cf. Reny 2011; Kennedy 2011). While that may be true, the field is in no way isolated from theoretical innovation in the social sciences. The following brief review of the scholarship examining the factors behind the precipitous advance of the state shows that China scholars have drawn very strongly from two pillars of late twentieth-century social science thought, institutions and interests. The basic, powerful insight of institutionalism is that social life is shaped strongly by myriad 'rules of the game'. Since these rules supply many of the constraints in which actors operate, so the argument goes, theory with a purchase on the real world cannot avoid reckoning with institutions. In the late twentieth century, this stream of institutionalism was blended into the work of many leading rational choice scholars, for whom interests and preferences comprise the core variables. The vision of social behaviour given by rational choice is of purposive, goal-oriented choice-making under constraint; institutions come in as 'scripts that constrain behavior' (Shepsle 2006). While institutions serve to channel behaviour, interests are the hard ground of action in a rational choice world, 'the stable foundations on which actors' preferences over policy shift as their situation and the policy vary' (Milner quoted in Schonhardt-Bailey 2006: 23). In recent years, both institutional and interest-based modes of analysis have been brought to the analysis of the advancing state in China.

While a later section of the chapter summarizes the key attributes of the ideational approach to political economy, it is worth here briefly differentiating the ideational approach from its closest relative, institutionalism. Of course, the choice of brevity means trading off against accuracy to some extent since there is considerable ambiguity within the social sciences about both the meaning of 'institutions' and 'ideas' as well as the relationship between the two (cf. Searle 2005; Schmidt 2011). This study follows an important recent work in conceiving of ideas as 'the foundations of institutions' which 'give rise to people's actions and as those actions form routines, the results are social institutions' (Béland and Cox 2011: 9). Ideational analysis is seen as a necessary corrective to institutional approaches that tend to treat institutions as social givens rather than products of social construction with a story of their own. Key ideational variables encountered in this literature include 'theories, conceptual models, norms, world views, frames, principled beliefs, and the like' (Campbell 2002: 21).[3] In the arena of politics, various species of idea that meet with the right circumstances are 'able to become a durable or *institutionalized* part of life' (Berman 2013: 229), while others less fortunate wind up in the dustbin of history. To date, a number of scholars have provided a thorough inventory of institutions shaping the advance of the state in China but we have, as yet, much less work examining the ideational provenance of institutions and the process through which they came into existence.

[3] Certain institutionalists would consider some of these variables as institutional rather than ideational. Indeed, Schmidt (2011: 54) writes that 'In the sociological tradition, one cannot talk about a move into ideas as such, since ideas have always been at the basis of this approach – as norms, cognitive frames and meaning systems.' Recent work in comparative politics on informal institutions also includes in its ambit some social phenomena that others would think of as ideas. For example, Gretchen Helmke and Steven Levitsky's widely cited work gathers norms under its definition of informal institutions as 'socially shared rules, usually unwritten, that are created, communicated, and enforced outside of officially sanctioned channels' (Helmke and Levitsky 2004: 727).