

## The Private Sector in Public Office

This book addresses the long-standing puzzle of how China's private sector manages to grow without secure property rights, and proposes a new theory of selective property rights to explain this phenomenon. Drawing on rich empirical evidence including in-depth interviews, a unique national survey of private entrepreneurs, an original survey of bureaucrats, two original national audit experiments, and secondary sources, Yue Hou shows that private entrepreneurs in China actively seek opportunities within formal institutions to advance their business interests. By securing seats in the local legislatures, entrepreneurs use their political capital to deter local officials from demanding bribes, ad hoc taxes, and other types of informal payments. In doing so they create a system of selective, individualized, and predictable property rights. This system of selective property rights is key to understanding the private sector growth in the absence of the rule of law.

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# The Private Sector in Public Office

## *Selective Property Rights in China*

YUE HOU

*University of Pennsylvania*



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## Preface

This book addresses the long-standing puzzle of how China's private sector manages to grow without secure property rights. I propose a new theory of selective property rights to explain this phenomenon. I show that, instead of passively accepting the existing institutional arrangements, private entrepreneurs in China actively seek opportunities within formal institutions to advance their business interests. By securing seats in the local legislatures, entrepreneurs use their political capital to deter local officials from demanding bribes, ad hoc taxes, and other types of informal payments. In doing so, they create a system of selective, individualized, and predictable property rights. This system of selective property rights is key to understanding private sector growth in the absence of the rule of law.

Drawing on rich empirical evidence, including in-depth interviews, a unique national survey of private entrepreneurs, an original survey of bureaucrats, two original national audit experiments, and secondary sources, this book shows how private entrepreneurs use the status and connections associated with holding a legislative seat to protect their property. I find that, even though government predation is an endemic problem, entrepreneur-legislators are less likely to suffer its effects. I quantitatively show that entrepreneurs who have seats in the local legislatures spend, on average, substantially less on informal payments to local officials than those who do not. Experimental evidence further demonstrates that Chinese bureaucrats are significantly more responsive to business people with connections in formal institutions than to those with no political connections.

These findings challenge prominent theories of economic development and suggest that a selective property rights regime helps sustain economic growth and political stability. Adopting an “institution as resource” perspective, I show that, within authoritarian institutions, entrepreneurs can seek opportunities to advance their interests and improve their well-being, even when the powers of these formal institutions are relatively weak.

## Acknowledgments

On a summer afternoon in 2012, when I was working in my graduate student office in Cambridge, MA, I received an e-mail forwarded from a friend. The e-mail was from his high school friend, who was pleading for help to save her father Mr. Zeng, a private entrepreneur who was sentenced to death for illegally fundraising billions of yuan (1 USD = 6.23 yuan in 2012). I had no connection to the Chinese legal system and I did not reply, but I started to follow the case. That same summer, Zeng's lawyer announced that Zeng's company was valued at 2.3 billion yuan but was secretly and cheaply sold to a government-owned asset management firm for 330 million while Zeng was in jail.<sup>1</sup> Zeng therefore missed the opportunity to sell his company in time to repay his loans. Zeng's daughter was unable to save her father. In July 2013, she posted on her Chinese Twitter (Weibo) account that he had been executed without warning. I was deeply saddened by the story. There were many details I did not know about the case, but the fact that Zeng was executed only two years after his initial guilty verdict and was not permitted to say goodbye to his daughter shows how powerless individuals are when facing a strong state. The government's devaluation and blatant takeover of private assets suggests how insecure property rights still are in China. Stories such as Mr. Zeng's motivated me to write this book, which examines how Chinese private entrepreneurs defend themselves against heavy-handed government expropriation.

<sup>1</sup> Sina blog entry, August 6, 2013. "Letter from Zeng Chengjie's lawyer to the Central Commission for Discipline Inspection" (*Zeng Chengjie lvshi gei zhongjiwei de xinhan*). [http://blog.sina.com.cn/s/blog\\_d8689d1f010191rij.html](http://blog.sina.com.cn/s/blog_d8689d1f010191rij.html). Last accessed July 26, 2018.

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This book is dedicated to my family. My grandpa, who invited – or forced – me to watch the evening news while having dinner when I was a toddler, is the earliest influence on my interest in political and social issues. My parents have accomplished many achievements in their own careers while raising me. Their work has provided me with first-hand insights on the Chinese economy, and they are always interested in learning about what I study. Peichun has been cheering me on as I approach the finish line. He has made this a finer book and will continue to make me a better scholar.

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## Abbreviations

ACFIC	All China Industry and Commerce Federation
CCP	Chinese Communist Party
CPPCC	Chinese People's Political Consultative Conference
LPC	Local people's congress
MP	Member of Parliament
NPC	National People's Congress
NPCSC	National People's Congress Standing Committee
PC	people's congress
PLA	People's Liberation Army
PRC	People's Republic of China
PRI	The Institutional Revolutionary Party (Mexico)
SCIO	The State Council Information Office
SME	Small and Medium Enterprise
SOE	State-Owned Enterprise
TVE	Township and Village Enterprise
VCP	Vietnamese Communist Party (Vietnam)
VPI	Vertical Political Intergration

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