

Sheng Hong and Zhao Nong, *China's State-Owned Enterprises: Nature, Performance and Reform*, Singapore: World Scientific, 2012, 372 pp. ISBN 978-981-4383-84-4 (hardcover).

In their remarkable volume, Sheng Hong and Zhao Nong provide a detail-rich discussion of China's state-owned enterprises (SOEs), covering political, economic, and legal aspects. The book can be used as an introduction to SOEs and the political economy they are embedded in, but it also provides empirical data and analyses of interest to experts of the field. In ten chapters and four sub-reports, this English translation of the original Chinese 2011 report adds important insights to our still-limited knowledge of the SOE reform and development process, their political embeddedness and the economics behind their success. The chapters cover important aspects such as the 'theory and process' of SOE reform (chapter 1), classification of SOEs (2), performance in terms of efficiency (3) and distribution (4), the 'state advances and the privates retreat' phenomenon (5) and the political economy of SOE performance (7). The four sub-reports add further analytical material on the mission of SOEs, the conflicts between SOEs and the State-Owned Asset Supervision and Administration Commission (SASAC), the lack of rent on land and the evolution of SOE-related policy.

The wide range of data and topics treated in the book are impressive. In chapter 1, the authors provide an overview of important reforms after 1978 by introducing some of the main policies that drove the evolution of SOEs until the late 2000s, such as the 'contract responsibility system', attempts at 'separating control from ownership', and the recognition of the 'socialist market economy' in 1992. Alongside this brief but useful overview, the volume provide insights into the theoretical discussions and implications surrounding these developments. Chapters 3 and 4 continue with a detailed discussion of the performance of SOEs in terms of efficiency and distribution; some of the strongest arguments of the volume are based on these interesting but bleak results. These results are not entirely new in nature (i.e. relative inefficiency and unequal distribution of resources compared to private enterprise), but are staggering in quality. According to the authors, the rents and hidden subsidies that large SOEs receive by far exceed their profits, and most SOEs would actually be loss-making enterprises were they to pay market prices for land, energy, interest on loans, etc. Deducting all subsidies and rents from the nominal profit, the authors state that SOEs in 2009 in fact have operated at a loss of a staggering 362 billion RMB (p. 80)! Additionally,

SOEs pay their employees 67 per cent higher salaries than private companies (p. 100) and offer excessive 'position-related consumption' benefits for their managers (p. 109), while paying less in tax and dividends. If correct, these findings could serve as proof for the hitherto anecdotal evidence many observers have given on the very distorted character of SOEs in the Chinese economy.

The discussion extends to a macroeconomic and political economy perspective, giving the analysis a solid foundation on which to build its main arguments, showing political reasons for and implications of the rise of SOEs. Chapters 8 to 10 are a mix of assessments and discussions of what SOEs are and *should* be, along with suggestions on how to reform the economic system toward a more market-oriented and competitive economy. The book thus follows (roughly speaking) a sequence from analysis of SOEs in the Chinese economy, criticism of the system based on the flaws found, and a discussion of what is at the heart of the problems and what should be done.

The strengths of the book lie in the remarkable untangling of the disparities between nominal and real returns, the factors that boost the apparent profitability and efficiency of SOEs, and the political implications of this. It is an excursion of rare detail-richness into the economics behind the rise of SOEs, which have become a major force behind the Chinese economy. It also stands out (for an originally mainland Chinese publication) as an unusually critical examination of what the authors call a system where 'SOE managers and government officials...conspire', which has 'severe constitutional defects in the actual legislative procedure' (pp. 188-189), leading to 'revolving doors', 'in-house lobbying', and ultimately, 'bureaucratic capitalism or crony capitalism' (p. 217). Of main concern to the authors are the administrative monopolies that, coupled with vested interests in the top levels of the administration, lead to severe distortions in the economic system, unfair competition and rent seeking behaviour by SOEs, not only at the expense of private businesses, but society at large. And while these points of criticism have been part of the repetitive repertoire of critics before, this book stands out in showing systematic evidence for these issues. Remarkably, this is done by relying almost entirely on publicly available data and discussion of SOE-related policies.

There is a clear liberal baseline to the book, and the recommendations it gives make clear that transformation toward a liberal market economy is seen as the (perhaps only) solution for the diagnosed ills. In other words, the book calls for structural reforms that cut deep into

the political system and break the vested interests. The authors present these recommendations quite convincingly, and in many points they echo concerns aired by Chinese top officials themselves.

However, some minor points remain to be corrected in a (hopefully planned) updated second edition. The discussion generally presents SOEs as parasites, capitalizing on their political clout, skimming off capital nominally belonging to the general society, thereby catalyzing inequality and unfair treatment of private business. Even though the evidence speaks in favour of the authors' arguments, some important aspects of these dynamics remain unaddressed. For example, it is unclear whether the SOEs are the driving force, pushing bottom-up lobbying for beneficial treatment and thus impeding reforms, or if in fact the party-state is actively promoting this state capitalism, top-down. This would shed some light on the political integration, and therefore the degree of power, behind vested interests, and whether the rise of central SOEs is in fact by design. In other words, is it possible that the current setup is in fact a bold bet made by planners two decades ago, and SOEs will actually turn for the better, giving way to an alternative to (the ideal types of) plan and market? Moreover, important questions are not discussed about the role of the Chinese Communist Party as the integrative force permeating both the state and SOEs, even exercising direct control over top-level management of 53 of the largest SOEs. For example, questions about the political rather than commercial mission of SOEs in general, and by extension of that also of the incentives behind SOE managers' decision making are yet to be clarified. Although touched upon (i.e. pp. 181, 188), a deeper discussion of the incentive webs across party, state and SOEs would serve the arguments of the authors well.

The volume has some minor issues in terms of structure and methodology. The chapters are not structured uniformly, and although they work well as single chapters, the reader never has a feeling of a smooth flow throughout the entire book. There are some editing errors in some figures and tables, and at times it is unclear what the units are (fig. 7.2 - 7.4), while some others are rather unclear to the reader, since they are black and white versions of originally colored diagrams (fig. 3.2). At times, newspaper articles are used as material next to econometric studies, which is not a problem *per se*, but results in a somewhat unclear mix of various data. The sub-reports serve more as background material than as integrated parts of the book, but they fit in quite well with the subject and make a valuable appendix.

Sheng Hong and Zhao Nong have compiled and analyzed a tremendous amount of data, which surprisingly, to a large extent consists of publicly available material. This makes the volume a must-read for anyone interested in China's political economy, industrial development, and of course, SOEs and their development and reform. This book is unmistakably located on the liberal side of the political spectrum, calling for a break-up of SOE monopolies, a total split of political and commercial rights and general market-oriented reforms. The authors do not hide their convictions, pointing out the flaws of the existing system of weak control over SOEs, leading to harmful effects on the economy and society at large. All in all, the book stands out as a well-informed, critical analysis in rarely seen detail, and as such it is an important addition to our limited knowledge of SOEs, their performance and their political integration. And while there are some minor structuring and editing issues, it nevertheless constitutes one of the most valuable contributions to the topic yet.

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