

# **DEVELOPMENT OF PRIVATE ENTREPRENEURSHIP IN CHINA: PROCESS, PROBLEMS AND COUNTERMEASURES**

**Yingqiu Liu**

If we consider the national economies of most countries in the world to be essentially enterprise or market economies in which individual economic activity is rewarded liberally and the role of the individual in the production process is central (Golay, 1960), we have to say that in the past, the Chinese economy<sup>1</sup> was essentially a government economy. In a government economy, economic activities are always controlled by the government, not by the enterprises themselves or by the market. In the early stages of the economic reform in China, there was an emphasis on the independence of operations and options for both enterprises and individuals. While the situation has changed a great deal, the government still intervenes in some microeconomic activities in a redundant fashion.

In this paper, I will analyze four issues. The first is the role of private entrepreneurship in China's national economic growth, while the second is the role of cultural/demographic factors on private entrepreneurial activities in China. The third concerns the business environment for private entrepreneurial activities in China in recent years, and the fourth is an analysis of government policies that support or hinder entrepreneurial activities in China. Finally, I will offer my conclusions and recommendations based on the whole analysis.

## **OVERVIEW OF PRIVATE ENTREPRENEURIAL ACTIVITIES IN CHINA**

### **THE RATE OF START-UPS IN THE PRIVATE SECTOR**

As many people know, in China the private sector became an important part of the economy after the economic reforms in 1978. Although in the early stage of establishing the People's Republic of China in 1949 there were about 9 million individual business units in China, they were one of the objects of the revolution during that time. After the socialist reconstruction from 1953-56, there was in practice almost no private and individual business. During "the three years adjustment period from 1963-65," some individual business households were established, but until the end of 1978, only about 150,000 existed in the whole country.

The first turning point of private sector development in China began in 1978. The Third Plenum of the Chinese Communist Party's (CCP's) 11th Central Committee, which convened in December 1978, was a milestone in Chinese socio-economic development. This Plenum distinguished itself by marking the beginning of the official revival of private business. Although the Plenum itself did not make any specific announcements concerning private business, it signified the official adoption of

---

<sup>1</sup> In this paper, the concepts of "Chinese economy" or "China" refer to the People's Republic of China or mainland China.

economic modernization and growth as the paramount concern of the CCP. It emphasized economic development and individual incentives, which gave impetus to the revival of private business. Before this Plenum, the mainstream society considered private and individual business activity to be the root of evil behavior—the so called “Capitalist tail”—which should be cut down by “revolutionary thought.” After this Plenum, the rapid development of individual and private activities had a strong experimental flavor since during that period this sector was still thought to play a marginal, stopgap role in the national economy as a supplement to the state and collective sectors. In practice, private businesses played the role of “filling in the gaps” in the national economy, particularly in the distribution of consumer goods and services and in employment. During that period, the main component of the private sector was individual household businesses (*getihu*).

The individual business (*getihu*) was a new business category in China during the early stages of economic reform. It was also called single industrial and commercial proprietor at that time. Until 1988, there were two types of individual or private businesses in China. The first was individual business, defined as a single unit that could hire no more than five employees, announced by a government document in July 1981.<sup>2</sup> If a private unit hired more than five employees, it was counted as a private enterprise. During that period, private enterprise was not a favored concept and hiring more than five employees was prohibited. But since this prohibition was not based on any economic reason, in June 1988, the central government issued a very important document, the Tentative Stipulations on Private Enterprises (TSPE). According to this document, if a unit with privately owned assets hired more than eight employees, it was regarded as a private enterprise (*saying qiye*). Private enterprise meant “a for-profit organization that is owned by individuals and employs more than eight people.”

According to the TSPE, there were three models of private firms: sole ownership, partnership and limited liability incorporation. These models of enterprise act as supplements to the socialist public-owned economy. Regarding other firms hiring eight or fewer employees, these are still registered as individual businesses (*getihu*)<sup>3</sup>. All of these can be called private sector businesses. We also refer to them as the “non-public economy” or “non-governmental economy.”<sup>4</sup>

From 1978 to 1988, the number of individual businesses and private enterprises grew rapidly. According to a 300-village survey conducted by a research institute under the State Council in 1987, more than 0.2 percent of farm households hired more than eight people in 1986. If we take this

---

<sup>2</sup> Bureau of Labor, Bureau of Urban Construction, Ministry of Public Security, and Bureau of Industry and Commerce Management, *Directives on Issues Related to Land Used by Urban Collective and Individual Economy*, 6 May 1981.

<sup>3</sup> This is a very funny and arbitrary definition. It is based on an example by Marx in his *Dos Kapital* in 1865. In his example, he seeks to illustrate the capitalist production and surplus producing process. Marx discusses the need for a certain number of people to be employed before the employer can get the surplus value and accumulate capital. So, he gives a purely hypothetical example in which the employer has to employ eight people in order to extract enough surplus value to make twice the employees' normal living standard, plus the same again to use as capital. In this example, his main presuppositions are that the surplus value rate is 33 percent and a half of the total surplus will be accumulated as capital, and that the employer wants to have a higher living standard, twice that of a normal employee. (Karl Marx, *Dos Kapital*, Chinese version, 1972, Vol. 1, 341-342). Obviously if the preconditions changed the conclusion should be changed, too. So, the definition given by China's government document is arbitrary and not based on any economic practice or theoretical reason.

<sup>4</sup> Please see also my paper, “On Necessities and Realities of China's Economic Non-governmentalization,” *Economic Research*, No. 6, (June 1994): 48-55.

survey result as a representative sample of the country at large, we estimate that by the end of 1988, there were 500,000 individual businesses in China that might be called private enterprises.

During this period, a series of central and local regulations on the licensing and controlling of individual and private businesses, taxation, product quality and hygiene, and free markets were introduced. As a result, the private sector developed rapidly in this phase.

But from 1989-91, the number of private and individual businesses declined, due not only to the “market rectification” during this period, but also due to the effect of leftist thinking from the traditionally dogmatic Marxist views. Of these two reasons for the decline, “market rectification” campaigns became an opportunity for the left to attack private business in practice. In this period, private and individual business activities were injured by the requirement that back taxes should be paid by these individual businesses and private firms. As a result, private sector businesses and enterprise activities declined significantly during this period (See Table 1).

**Table 1. Private Firm Development From 1989-2000**

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Number (1,000)	91	98	108	140	238	432	655	819	961	1,201	1,509	1,762
Growth (%)		8.4	9.9	29.5	70.4	81.7	51.4	25.2	17.3	25	25.6	16.8
Owners (1,000)	210	224	241	303	514	889	1,340	1,705	2,042	2,638	3,224	3,954
Growth (%)		6.7	7.6	25.7	69.6	73	50.7	27.2	19.8	29.2	22.2	21.5
Workforce (1000)	1,426	1,478	1,598	2,015	3,213	5,594	822	10,007	11,450	14,453	16,498	20,112
Growth (%)		3.7	8.1	26.1	59.5	74	46.9	21.7	14.4	26.2	17.6	18.4
Registered Assets (billion RMB)	8.45	9.5	12.3	22.1	68.1	144.8	262.2	375.2	514	719.8	1,028.7	1,330.69
Growth (%)		13.1	29.5	79.7	208.1	112.6	81.1	43.1	37	40	42.9	29.4
Gross Product (billion RMB)	9.7	12.2	14.7	20.5	42.2	114	229.5	322.7	392.3	585.3	768.6	1,073.98
Growth (%)		23.2	17.1	32.3	81.9	122	75.4	32.5	20.6	53.2	35.4	38.7
Taxation (billion RMB)	0.11	0.2	0.34	0.46	1.05	1.75	3.56	6.02	9.05	16.3	25.5	41.44
Growth (%)		78.6	69	34.6	129	67.5	103.1	69.2	50.2	80.1	56.4	62.5

*Source: Office of the State Bureau of Business Management, ed., Statistic Collection of Business Administrative Management (1989-2000) and Yearbook of Taxation in China (1993-2000).*

The new boom period of private sector development in China began after Deng Xiaoping’s “South Touring Talk” in April 1992. Under the guidance of Deng’s theory of “getting big forward and development is the first principle in China,” private and individual business activities flourished rapidly. In accordance with Deng’s theory, the governments, both central and local, started to implement expansionary policies for encouraging private business development. These policies included encouraging the movement of foreign capital into China and the expansion of investment of domestic private capital. As Table 1 shows, all private firm indices, including the number of firms, entrepreneurs and workforce as well as enrolled capital and taxation and growth rates, increased enormously.

If we take individual household businesses (*getihuo*) into account, until 2000 the total number of firms was more than 312.5 million, including 1.76 million private firms and 311 million individual

business units. More than 20 million workers were hired by private firms and more than 311 million of the workforce worked in individual business activities. In the development of the private sector, private enterprises, private entrepreneurs and entrepreneurship have been playing a very important role.

Except for the typical models of private enterprises that are defined as enterprises with privately owned assets and employment of more than eight people—sole ownership, partnership or limited liability incorporation—private enterprises have taken four other popular forms in the past two decades:

The first is the “red hat firm.” Normally, as private firms become established some take a “red hat” as an easy way to survive and grow successfully in China. The term “red hat” means that the firm can obtain a collective or state license for production and operations by paying certain administrative fees to the state or collective unit or local government organization. Normally the fee is about 1-2 percent of the firm’s output value or 5-10 percent of its turnover. After paying these fees, the private owner is able to evade government prohibitions on private firms and ideological harassment during the license period.

Township and village enterprises (TVEs), urban collective enterprises (UCEs) and even state-owned enterprises (SOEs) are the forms that “red hat” firms like to take. Among these forms, TVEs and UCEs are the main registered forms; however, they are actually privately owned. Until the mid-1990s, especially after the CCP’s 15th Congress in 1997, a number of the “red hat firms” started to take off the “red hat.” But most of them were not able to take off it completely, since the public organizations wanted to hold some “tail” in order to “control” them or to seek some “rents” from them. So, in practice the “red hat” phenomenon remains important in most areas of China.

The second form is the “rented collective.” There are many collective firms that have been rented out to private operators. These firms retain the collective form on the surface, but their inner operating mechanisms are private. According to a survey in 1984, such firms made up 19 percent of all collectives in Hebei, 30 percent in Tianjin, 40 percent in Liaoning and 50 percent in Ningxia. Under this form, by paying the collective only a fixed rent, a private entrepreneur is able to operate the firm as if it were his own and in many cases accumulate considerable capital assets. As a result, the share of the collective assets will eventually be diminished and the firm gradually transformed into a solely private-owned firm. According to my survey in Panyu County of Guangzhou, almost all of the private or shareholding companies evolved from this rented collective form.

The third form is the “shareholding firm.” This type of firm distributes the collective assets as shares to employees or profits as bonuses to employees for forming a private enterprise. Until now a few state-owned enterprise have been privatized through this form but many collectives, especially TVEs, have been changed in this way. Normally this form has applied to small collective-owned or state-owned units.

The fourth form is the “foreign investor joint enterprise.” Since foreign private enterprises were permitted as joint ventures with local collectives or SOEs, and obtained significant tax advantages, many domestic entrepreneurs invested through offshore companies so as to qualify as foreign investors. However, until recently, there have been few private enterprises operated jointly by

foreign investors. Nevertheless, foreign investor joint enterprises have been regarded by *domestic* entrepreneurs as a channel for increasing profits.

There are four main reasons why the private sector has developed rapidly during the past 24 years. First, there is an urgent need to establish these private businesses. In practice, the public sector is not able to employ enough people and to produce sufficient products to satisfy the diverse demands of the Chinese people. Second, the operational efficiency of the private sector is much higher than the public sector, including state-owned and collective enterprises. The private sector's operation depends on self-management and is charged with risk. There is no "free lunch" for this sector from either the central or local governments. The owner of the private firm has to work hard, manage effectively and to innovate ceaselessly everyday. Third, government policies have improved. Although there was a period of lagging growth for the private sector in China as we illustrated above, in most periods the growth rate of the private sector has been more rapid than the other sectors. The fourth reason is that during the past 24 years, the central and local governments have supplied the conditions and policies conducive for developing the private sector. For example, after the Third Plenum of the CCP's 11th Central Committee, the boom of non-agricultural individual economy and private enterprise took place first after the contact responsibility system evolved into practice, i.e. the arrival of the virtual privatization of agriculture. After the Third Plenum of the CCP's 15th Central Committee, the private sector flourished, and individual business activities and private entrepreneurial activities have been upgraded and elevated. Some large-scale private enterprises—as large as state-owned enterprises in terms of overall assets and gross product—have formed in China in recent years.

To sum up, we might consider the first historical turning point in private sector development as the period after the Third Plenum of the CCP's 11th Central Committee in December 1978, and the second important point of private sector development as the time after Deng Xiaoping's *South Touring Talk* in April 1992. If this is the case, we have to say—and dare to predict—that this sector has now entered its third important development period in which it is booming and flourishing. The policies for pushing private sector development forward will be more unambiguous and energetically accelerating this development will become a chief focus in the coming years.

## **THE IMPACT OF PRIVATE ENTREPRENEURIAL ACTIVITIES ON CHINA'S NATIONAL ECONOMIC GROWTH**

There are at least four positive effects of private entrepreneurial activities on China's national economy.

First, its development has rapidly and successfully pushed the entire national economy forward. As everyone knows, the private sector has become a dynamic component of China's domestic economy. During the period 1991 to 2000, the average annual growth rates of private firms, private sector employment and industrial output were 32.21 percent, 28.82 percent and 53.59 percent respectively (See Table 1). This explosive development is in sharp contrast to the decline of the public sector, including SOEs, state holding majority shares and collective-owned sectors as shown in Table 2. The entire public sector, including construction enterprises, declined dramatically by -0.7 percent from 1998 to 1999. The biggest decline was for collective-owned enterprises: -7.7 percent. In contrast, the private sector grew as shown in the Table 2. Since almost all of the rural construction teams are owned by private entrepreneurs, they should be considered private sector

enterprises. If this judgment is correct, the rate of increase for the private sector in 1999 was actually much higher than the 9 percent shown in the last line of Table 2. The decline of the public sector was accompanied by the continuing high growth rate of the GDP.<sup>5</sup> This means that the growth of the GDP was supported by the non-public sector's development, i.e. by the private sector's development, along with the higher growth rate itself.

**Table 2. Number of Enterprises in Various Ownership Sectors**

Sector	Grassroots Units		Rate of Increase 1998-99
	1998	1999	
Township Enterprises (10 000 units)	2003.9	2070.9	3.3
Industrial Enterprises (10 000 units)	797.46	792.99	-0.6
State-owned and State Holding Majority Shares	6.47	6.13	-5.3
Collective Owned	179.78	165.92	-7.7
Urban and Rural Private	603.38	612.68	1.5
Others	8.57	9.18	7.1
Construction Enterprises and Units (unit)	90926	96648	6.3
Construction Enterprises	9458	9394	-0.7
Affiliated Construction Units	26970	25443	-5.7
Rural Construction Teams	45292	49414	9.1

*Source: National Bureau of Statistics of PRC, China Statistical Yearbook, China Statistics Press 2000, p. 19.*

Second, the private sector's contribution to national economic growth has risen continuously, in contrast with the contribution of the public sector. From 1991 to 1999, the contribution rate of the public sector to China's total national industrial output declined steeply, from 79.64 percent to 9.11 percent, as column 5 of Table 3 shows. In contrast, the private sector's contribution rose rapidly and continuously, from 20.36 percent in 1991 to 90.89 percent in 1999. As shown in Figures 1 and 2, the share of public sector industrial output in the national total decreased significantly while private sector industrial output increased markedly.

<sup>5</sup> During 1991-2000, the GDP growth rate of China was 9.2, 14.2, 13.5, 12.6, 10.5, 9.6, 8.8, 7.8, 7.1 and 8.0 percent respectively (See also Statistics Department of the PRC, *The People's Bank of China Quarterly Statistical Bulletin*, (January 2002): 5.

**Table 3. Public and Private Industrial Values, 1990-99**  
(100 Million RMB yuan)

Year	Total Industry	Public Sector	Private Sector	Public Contribution Rate	Private Contribution Rate
1990	23,924	21,587	2,337		
1991	26,625	23,738	2,887	79.64	20.36
1992	34,599	29,959	4,640	78.02	21.98
1993	48,402	39,189	9,213	66.87	33.13
1994	70,176	52,673	17,503	61.93	38.07
1995	91,895	64,843	27,052	56.03	43.97
1996	107,407	75,405	32,002	68.09	31.91
1997	120,673	79,315	41,358	29.47	70.53
1998	126,993	79,351	47,642	0.57	99.43
1999	136,068	80,178	55,890	9.11	90.89

Notes: Data in this table are calculated at current prices.

Source: National Bureau of Statistics of PRC, *China Statistical Yearbook*, China Statistics Press 2000, p. 409.

**Figure 1. Share of Public Sector Industrial Outputs in the National Total (%)**

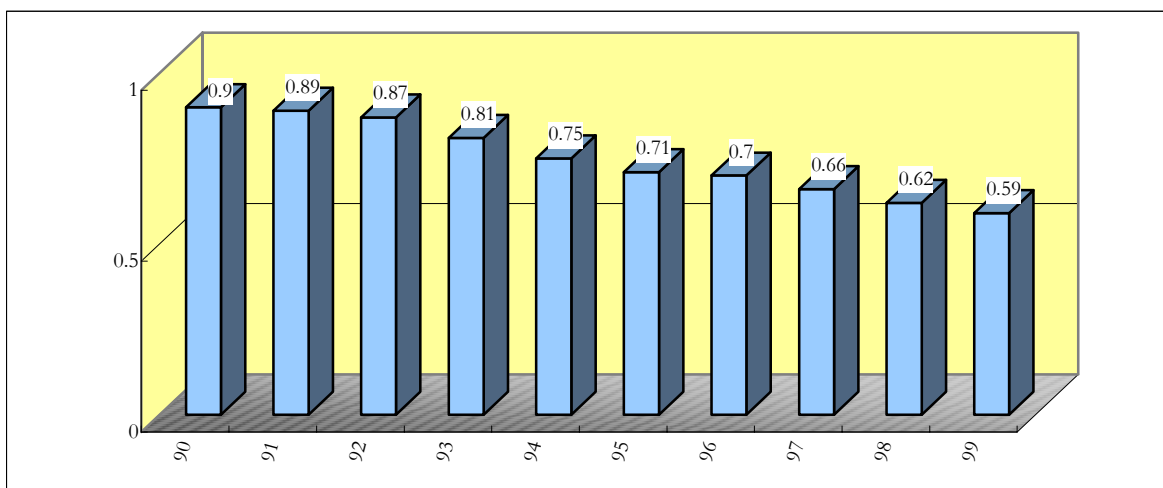
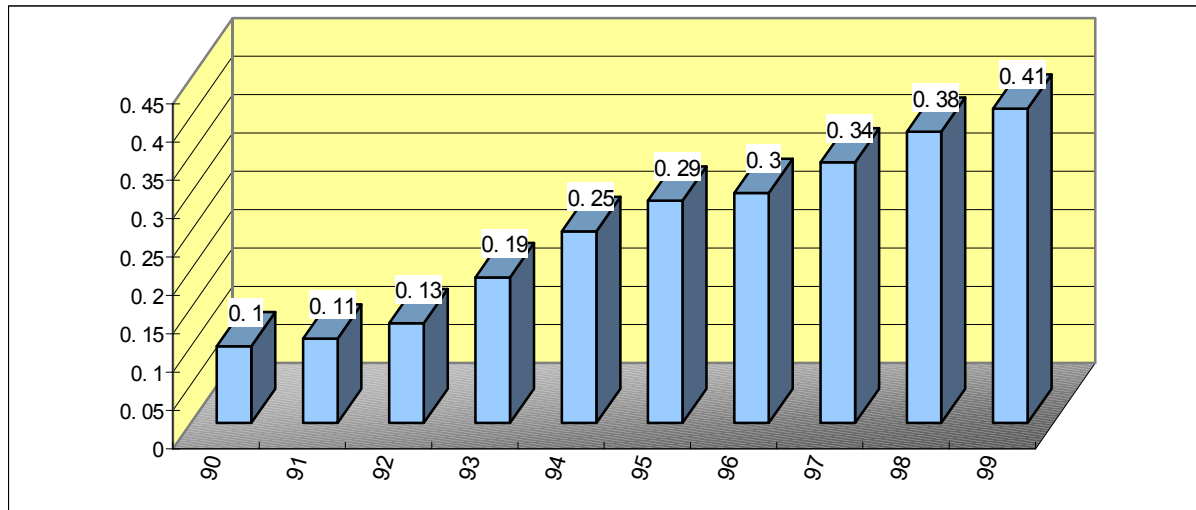


Figure 2. Share of Private Sector Industrial Outputs in the National Total (%)



Third, the private sector has offered more jobs than the public sector. If we look at Table 4 in detail, we find that the number of employed persons in urban state-owned and collective-owned units decreased rapidly from 1996. But in contrast, employment in the private sector rose each year. From 1996 to 1999, in the public sector, the number of employed persons declined more than 28.6 percent compared with the employment level in 1995, but in the meantime employment in the private sector increased more than 129.03 percent; the increase for private enterprises was more than 117.11 percent. In rural areas, the increase in employment in the private sector was not as high as in urban areas; however, it is important to note that most of the TVEs are actually “red hat enterprises.” When we take this fact into consideration, private sector employment in rural areas becomes higher than public sector employment. When we survey the columns of Table 5, we also find that in China the most rapid growth of employment is not in the public sector but rather in the private sector. More than 29.7 percent of jobs were supplied by the private sector in 1999 if we include TVEs in the private sector category. Obviously, if there were no private sector in China, workers laid off from public sector would become an unemployed workers’ army, overcrowding the entire country. Thousands of unemployed workers throughout the cities and countryside, acting like fainéants, could be a potential threat to society.



**Table 4. Number of Employed Persons by Sector in Urban and Rural Areas (10,000 persons)**

Item	1995	1996	1997	1998	1999
Total Number of Employed Persons (10,000 persons)	67,947	68,850	69,600	69,957	70,586
Urban Employed Persons	19,093	19,815	20,207	20,678	21,014
State-owned Units	11,261	11,244	11,044	9,058	8,572
Urban Collective Owned Units	3,147	3,016	2,883	1,963	1,712
Share Holding Units	-	-	-	136	144
Joint Owned Units	53	49	43	48	46
Limited Liability Corporations	-	-	-	484	603
Share-holding Corporations Ltd.	317	363	468	410	420
Subtotal for the above four items	370	412	511	1,004	1,213
Private Enterprises	485	620	750	973	1,053
Units Funded by Entrepreneurs from Hong Kong, Macao & Taiwan	272	265	281	294	306
Foreign Funded Units	241	275	300	293	306
Self-employed Individuals	1,560	1,709	1,919	2,259	2,414
Rural Employed Persons	48,854	49,035	49,393	49,279	49,572
Township and Village Enterprises	12,862	13,508	13,050	12,537	12,704
Private Enterprises	471	551	600	737	969
Self-employed Individuals	3,054	3,308	3,522	3,855	3,827
Number of Staff and Workers (10,000 persons)	14,908	14,845	14,668	12,337	11,773
State-owned Units	10,955	10,949	10,766	8,809	8,336
Urban Collective Owned Units	3,076	2,954	2,817	1,900	1,652
Units of Other Types of Ownership	877	942	1,085	1,628	1,785

Source: National Bureau of Statistics, PRC, *China Statistical Yearbook, China Statistics Press 2000*, p. 115.

Table 5. Employment in Private Sectors, Urban and Rural, 1978-99 (10,000 persons)

Year	Total of China	Sub-total Of Urban	Private and Individuals	Sub-total Of Rural	Township And Village Enterprises	Private Enterprises	Individuals
1978	40,152	9,514	15.0	30,638	2,827		
1980	4,2361	10,525	81.4	31,836	3,000		
1985	49,873	12,808	450.1	37,065	6,979		
1986	51,282		483.1				
1987	52,783	13,783	568.8	39,000	8,805		
1988	54,334	14,267	659.3	40,067	9,545		
1989	55,329	14,390	648.2	40,939	9,367		
1990	63,909	16,616	670.5	47,293	9,265	113	1,491
1991	64,799	16,977	759.5	47,822	9,609	116	1,616
1992	65,554	17,241	837.9	48,313	10,625	134	1,728
1993	66,373	17,589	1,115.7	48,784	12,345	187	2,010
1994	67,199	18,413	1,557.4	48,786	12,017	316	2,551
1995	67,947	19,093	2,045.0	48,854	12,862	471	3,054
1996	68,850	19,815	2,328.8	49,035	13,508	551	3,308
1997	69,600	20,207	2,669.0	49,393	13,050	600	3,522
1998	69,957	20,678	3,231.9	49,279	12,537	737	3,855
1999	70,586	21,014	3,466.9	49,572	12,704	969	3,827

Source: National Bureau of Statistics of PRC, *China Statistical Yearbook, China Statistics Press 2000*, pp. 118-119, 138.

Fourth, private sector development is conducive to enhancing the living standard of China's people. Looking at Table 6, we find that in recent decades the wages of staff and workers in the private sector have been increasing at a higher rate than for those in the public sector. With the exception of public sector reforms that changed the property right structure of firms and reduced the total wage level, the main reason for the dramatic and comparative decline of the public sector wage level has been the rapid development of the private sector. Another factor contributing to the increase in wages in the private sector has been the operational efficiency of the private sector. If private enterprises operate inefficiently, they cannot possibly pay more money to their staff and workers. Of course the rapid increase in total wages of private sector staff and workers is due not only to higher operating efficiency in the private sector but also to the fact that in this sector there are some foreign enterprises involved that facilitate making more money.

**Table 6. Increase in Total Wages for Staff and Workers in the Private Sector (%)**

Year	Total	State-owned Units	Urban Collective-owned Units	Units of Other Types of Ownership
1978	110.5	110.1	112.5	
1980	119.4	118.6	123.3	
1985	122.0	121.6	123.0	163.9
1986	120.0	121.0	116.2	142.4
1987	113.3	113.3	112.8	151.2
1988	123.1	123.8	119.2	169.3
1989	113.1	113.5	109.6	157.7
1990	112.7	113.4	108.7	135.7
1991	112.6	111.7	113.4	153.0
1992	118.5	119.1	112.8	150.0
1993	124.8	123.4	114.4	240.2
1994	135.4	135.8	120.4	179.7
1995	121.7	117.4	115.5	140.0
1996	112.1	111.7	105.0	119.4
1997	103.6	106.2	101.0	123.6
1998	100.2	95.8	83.1	156.9
1999	106.2	105.1	94.2	119.8

*Source: National Bureau of Statistics of PRC, China Statistical Yearbook, China Statistics Press 2000, p. 141.*

It is noteworthy that the private sector's share of output and employment and its contribution to the country have been achieved with much smaller resources. Statistics show that from 1991-97 the private sector's share of investment in the national total was in the range of 15-27 percent. According to Table 7, the share of investment in fixed assets by individuals plus "other ownership" is only 28.1 percent (since statistics for "other ownership" sector are available only from 1993, but among them there is some foreign investment), and the share of the individual sector itself in total national investment is only 13.4 percent. This means that the private sector is run more efficiently than the public sector. However, among these private firms, there are some enterprises that once used less advanced technologies and consumed more energy and materials in the production process. So beginning in 1997, China's central government decided to eliminate some small enterprises, such as small cement plants, paper mills, chemical plants and coal mines, etc.

Table 7. Total Investment in Fixed Assets by Ownership (100 million RMB yuan)

Investment	Total		State-owned Units		Collective-owned Units		Individuals		Other Ownership	
	Value	Growth Rate	Value	Growth Rate	Value	Growth Rate	Value	Growth Rate	Value	Growth Rate
1980	910.9		745.9		46.0		119.0			
1981	961.0	5.5	667.5	-10.5	115.2	150.4	178.3	49.8		
1982	1,230.4	28.0	845.3	26.6	174.3	51.3	210.8	18.2		
1983	1,430.1	16.2	952.0	12.6	156.3	-10.3	321.8	52.7		
1984	1,832.9	28.2	1,185.2	24.5	238.7	52.7	409.0	27.1		
1985	2,543.2	38.8	1,680.5	41.8	327.5	37.2	535.2	30.9		
1986	3,120.6	22.7	2,079.4	23.7	391.8	19.6	649.4	21.3		
1987	3,791.7	21.5	2,448.8	17.8	547.0	39.6	795.9	22.6		
1988	4,753.8	25.4	3,020.0	23.3	711.7	30.1	1,022.1	28.4		
1989	4,410.4	-7.2	2,808.2	-7.0	570.0	-19.9	1,032.2	1.0		
1990	4,517.0	2.4	2,986.3	6.3	529.5	-7.1	1,001.2	-3.0		
1991	5,594.5	23.9	3,713.8	24.4	697.8	31.7	1,182.9	18.1		
1992	8,080.1	44.4	5,498.7	48.1	1,359.4	94.8	1,222.0	3.3		
1993	13,072.3	61.8	7,925.9	44.1	2,317.3	70.5	1,476.2	20.8	1,352.9	
1994	17,042.1	30.4	9,615.0	21.3	2,758.9	19.1	1,970.6	33.5	2,697.6	99.4
1995	20,019.3	17.5	10,898.2	13.3	3,289.4	19.2	2,560.2	29.9	3,271.5	21.3
1996	22,974.0	14.8	12,056.2	10.6	3,660.6	11.3	3,211.2	25.4	4,046.0	23.7
1997	24,941.1	8.8	13,091.7	9.0	3,850.9	5.5	3,429.4	6.8	4,569.1	13.0
1998	28,406.2	13.9	15,369.3	17.4	4,192.2	8.9	3,744.4	9.2	5,100.3	11.6
1999	29,854.7	5.1	15,947.8	3.8	4,338.6	3.5	4,195.7	7.9	5,372.7	5.3

Notes: "Other ownership" refers to ownership other than state-owned units, collective-owned units and individuals, including joint-owned economic units, share holding economic units, foreign-funded economic units, economic units funded by the entrepreneurs from Hong Kong, Macao and Taiwan, etc. The data for total investment in fixed assets since 1990 have been adjusted in accordance with the data obtained from the 1994 fast survey on real estate.

Source: National Bureau of Statistics of PRC, *China Statistical Yearbook*, China Statistics Press 2000, p. 168.

## CULTURAL/DEMOGRAPHIC FACTORS AFFECTING PRIVATE ENTREPRENEURIAL ACTIVITIES IN CHINA

### ATTITUDES TOWARD ENTERPRISE CREATION

In the past 50 years, the attitudes of the government and the people towards a private economy have evolved from hostile to favorable. During the periods of the planned economy, collective economy and even the state-owned economy, the private economy was considered the source of exploitation and capitalism that needed to be eliminated. Accordingly, by the end of 1956, the main characteristics of private sector, including a capitalist economy and landlordism, become the object

of socialist revolution under the leadership of the CCP. After that, almost all private business activities were prohibited.

Since 1979, when the whole country turned its focus to reforming the economic system, opening China's gates, constructing a strong China and offering more job opportunities to the educated youth who returned to China's urban areas and "waited for a job at home," the government has encouraged the development of individual business activities (mainly self-employment). With the development of individual businesses, some individuals began to hire workers to enlarge their business, and thus, the private sector came into being. At the same time, the government's attitude changed to a certain extent by permitting private enterprises to develop. But during the 1980s, the government and some theorists claimed that private enterprises exploited workers, were contrary to the goal of socialism and had certain negative impacts on the national economy. So, in the early stages of the economic reform and openness, individual businesses were considered to be a beneficial complement to the national economy as a whole, but they were still considered bad form in China. As a result, private enterprises had to wear a "red hat" for their survival and growth, as mentioned earlier.

After Deng Xiaoping's *South Touring Talk*, more top leaders and people began to accept the new concept of the "socialist market economy." They started to understand that the key criterion for judging whether the economy is socialist or capitalist is not whether there is a central plan or planned economy, since planning and markets are only the instruments for building socialism. Deng's speech greatly emancipated people's thoughts and brought China into the golden age of private sector development, especially the development of private enterprises. At the end of 1992, the number of registered private enterprises reached 139,600—29.5 percent more than the previous year, and the number of employed persons reached 2,015,000—26.1 percent more than in 1991. Furthermore, more than 220,000 officials left their positions and jumped into the "business ocean."<sup>6</sup>

In September 1997, the 15th National Congress of the CCP admitted that the non-public economy is an important component of the Chinese Socialist Market Economy, and a coexistence of multi-ownership is also a key factor of the basic economic system in China. The CCP and China's governments, from the central to the local, began to take measures to protect the legal income of various enterprises, encourage the factors of production including capital and technology, participate in the distribution of revenue, protect the legal rights of all kinds enterprises and ensure fair competition among firms of different ownership types. The amendments to the Constitution in 1999 also affirmed that individual businesses and private enterprises are important components of the Socialist Market Economy. This confirmation of the active roles played by the private sector in China's national economy further cleared obstacles for the development of individual businesses and private enterprises.

Now, to create more job opportunities, hasten the reconstruction of the state-owned economy and boost domestic demand, the government is urgently encouraging the development of the private sector. Measures that have been taken include: encouraging private business activities to take over small and medium-sized SOEs; asking the state-owned bank to expand its loans to medium- and small-size business (including private enterprises); encouraging private enterprises to invest in the infrastructure fields; encouraging intellectuals to set up high-tech firms in high-tech industrial parks

---

<sup>6</sup> Chinese Reform and Development Institution, ed., *The Development of Chinese Private Economy*, (Hainan: Democracy and Construction Press, 1995): 324-325.

created by the governments; and even awarding to some big private enterprises the right to engage in import and export business.

The experience of the last two decades also shows that location and China's historical and cultural background have had an important influence on the development of the private sector. In southeastern coastal China (such as Wenzhou and Taizhou in Zhejiang Province and Shunde and Dongguan in Guangdong Province, etc.), a market economy had developed to some extent before and during economic reform in China. The people there got used to the operation of a market economy, formed the belief that "time is money" and became accustomed to free trade. The people knew how to make more money by operating their own businesses. In other words, the people who lived in these areas, Wenzhou, Taizhou and the delta of the Pearl River, had known for 20 years how to conduct their businesses even though a market economy was strictly prohibited. So, with the permission from the government and led by examples of enlightened businessmen from Hong Kong, Macao, Taiwan and Southeast Asia, the people in these areas admired successful entrepreneurs, and the culture encouraged people to set up their own businesses. To become a boss was every person's ambition and goal. As a result, the private sector has been growing rapidly there for many years. Now, private enterprises are the mainstay of the economy and the main source for income in these regions. On the other hand, the people who are confined by the opinion of autarky always despise the important roles played by trade, economic interest and so on. As result, the development of the private sector elsewhere in China has been slower and the income level of the people has also been lower compared with that of southeast China.

### ATTITUDES TOWARD FAILURE/SUCCESS

As everyone knows, many individuals in China have been successful in developing businesses because the government cannot offer enough job opportunities. Their primary goal is to earn money and sustain their basic living conditions. But from the middle of the 1990s, with the rising standard of living, increasing numbers of people set up new ventures not only to sustain their lives or to make more money but also for self-development. According to a survey of 201 private entrepreneurs in Hunan province, conducted by the Hunan Association of Business and Commerce and the Department of Hunan Unification, 41.79 percent of entrepreneurs there set up an enterprise to improve their living conditions, 16.91 percent to sustain their basic living standards, 18.41 percent to realize their self-value, 15.9 percent to contribute to society, 4.48 percent to apply their specialties and 2.49 percent for other purposes.<sup>7</sup> With more people engaged in business for purposes besides earning money, the criteria for judging whether an entrepreneur is successful or not depends not only on the money he/she has made, although money is the most important item. Employees hired by private enterprises are seeking not only a higher income but also to realize their self-value and have a free and fair working atmosphere, which is more common in high-tech private firms. But private enterprises cannot offer the same social security benefits as state-owned enterprises, including medical care, retirement pensions and even unemployment benefits (for the government denied the phenomenon of unemployment for a long time). Employees in private enterprises have higher mobility and a greater awareness of risk than employees in the state-owned units (including in the collective-owned units). Layoffs, resignations and a different kind of relationship between employers and employees are widely accepted. If dismissed, the employee is able to accept this result quietly and willing to try to find other opportunities by him/herself. On the other hand, the

---

<sup>7</sup> Jive Ran and Lin Lang, *Chinese Government and Private Economy*, (The China Federal of Industry and Commerce Press, 2000), 347.

entrepreneur also realizes that his firm, if poorly managed or if the product is rejected by the marketplace, will become bankrupt, and he is also able to accept the fact and to try to find another new way to salvage his business.

Regarding the attitudes of the people toward entrepreneurial failure, Chinese believe that it is natural and unavoidable since there are a great many storms in the “market ocean” and it is impossible to avoid drinking ocean water occasionally. So even when someone is a failure in the market ocean, while he/she does “go up the seaboard,” people look up to him/her, like to talk with him/her and hope that he/she will be able to re-launch the enterprise in the near future.

### ACCEPTANCE OF WOMEN IN THE WORKFORCE

Since the PRC was founded in 1949, the government and the whole society have supported women’s liberation, encouraging women to receive an education and join the work force. Women are also said to be “upholding half of the sky.” So, when private sector enterprises offer new positions, many women are likely to join them. At the end of 1999, the proportion of female staff in private units, with the exception of state-owned and urban collective-owned units, was 42.4 percent—4.4 percent higher than the rate in the total Chinese economy. Further, because of the varied requirements of different sectors and positions, more females entered sectors such as banking and insurance, wholesale and retail trade and catering services, the same as for state-owned and collective-owned sectors (See Table 8). Perhaps due to the traditional cultural norm that places the man as the head of the family, in the private economic arena, females are about 10 percent of private entrepreneurs.<sup>8</sup>

**Table 8. Proportion of Female Staff and Workers in Different Ownership and Sectors in 1999 (%)**

	Averaged	State-owned Units	Urban Collective Owned Units	Units of Other Types
Average in Whole China	38.0	36.5	41.1	42.4
Wholesale and Retail Trade & Catering Services	46.3	44.6	46.1	52.9
Health Care, Sporting and Social Welfare	56.9	57.7	51.4	49.0
Banking and Insurance	42.7	41.9	42.0	50.9
Manufacturing	43.4	39.5	49.3	45.6
Farming, Forestry, Animal Husbandry and Fishery	37.6	37.9	25.9	34.1
Mining and Quarrying	26.5	26.4	37.4	21.6
Construction	18.5	20.1	17.4	15.0

*Source: National Bureau of Statistics of PRC, China Statistical Yearbook, China Statistics Press 2000, p. 134.*

### EFFECTS OF AGING SOCIETY AND OTHER DEMOGRAPHIC TRENDS

In the last few years, because of the accelerated restructuring of the state-owned economy, tens of millions workers have been laid off. Employees (both management and workers) serving in state-

<sup>8</sup> *The Second Private Enterprises Survey in China* conducted by the Institute of Private Economy in 1994.

owned units declined from 112,610,000 in 1995 to 85,720,000 in 1999. On the other hand, the number of managerial staff and workers employed in private enterprises has increased from 4,850,000 in 1995 to 10,530,000 in 1999; the number of individuals hired as workers in the private sector has increased from 15,600,000 to 24,140,000, an increase of 8,450,000. Now, the private sector has become a main channel to absorb new workers. In past 10 years, large numbers of peasants have gone to the cities to take construction jobs, work in other fields, or become housekeepers in city homes. Normally these are young men and women. We predict that in the future, vast numbers of peasants will go to the cities to pursue higher incomes and better living conditions, and at the same time, with the restructuring of the Chinese economy, the state-owned economy will be unable to hire more workers, and also will lay off millions of workers. To alleviate the heavy pressure to create more job opportunities, the governments, including the central and local, have to take more efficient measures to encourage the development of the private sector in various fields. We predict that they will make greater progress than in the past and increasing numbers of people will be under the private sector flag.

## **THE BUSINESS ENVIRONMENT FOR PRIVATE ENTREPRENEURIAL ACTIVITIES IN CHINA**

### **STRENGTH OF FINANCIAL SYSTEMS**

Before economic reform in China, there were only four state-owned commercial banks: People's Bank of China, Bank of China, Construction Bank of China and Agricultural Bank of China. Unlike a commercial bank, these four banks behaved more like the accountant and cashier of the governments. So, in the early stage of private sector development after 1978, if individuals or private enterprises wanted to borrow money from these banks, they were not able to do so, even if they had the ability to obtain a mortgage loan. This meant that during that time, there were no places efficiently offering loans to the private sector.

Since the economic reforms, especially after the banking system reform, China has not only a central bank, the People's Bank of China, but also four state-owned commercial banks: Business and Commerce Bank of China, Bank of China, Construction Bank of China and Agricultural Bank of China. There are also several shareholding commercial banks at the national level, including the Chinese Communication Bank, Chinese GuanDa Bank, Chinese Zhongxin Bank, Chinese Huaxia Bank and Chinese Minsheng Banking Corporation, etc. In addition, there are some regional development banks, including the Shenzhen Development Bank, Fujian Xingye Bank and Hainan Development Bank. After 1997, in China all of the city credit unions were consolidated into a commercial bank and named the City Commerce Bank. In one year, more than 70 City Commerce Banks were established in the central cities. Now there are over one hundred City Commerce Banks throughout China.

In addition to the officially approved banks mentioned above, there also are some pawnshops and private moneychangers, established underground in the cities or countryside. These help satisfy the financing demands of individuals and mid-sized and small private enterprises by lending money. However, their interest rate requirements are always a great deal higher than the officially registered banks. In some areas, for example in Wenzhou, this kind of the "banking" is trustworthy in its



commercial credit activities. But most of these lenders in long-term credit are not. Some even defraud the depositor or borrower. As a result, the government decided that they should be completely regulated. We believe that by regulating this kind of “banking behavior,” the banking system will achieve healthy growth and will also contribute to the nation’s economic development. The alternative of closing or canceling them completely is not a good choice for the further development of China’s national economy.

## ACCESS TO CAPITAL

During the period when China’s economy was planned, the government appropriated most of the economic surplus from state-owned enterprises. Under these conditions, workers in the state-owned units, who had little capital, were usually in a poor position to set up an enterprise. Based on our survey, after the economic reform, most private entrepreneurs came from the ranks of individual workers, drivers, leaders of handicraft factories or government branches, state contractors or collective-owned firms. This is because they had the chance to have markets or more money or they already had the skills to run a business. Even so, to run their businesses or enterprises, they had to borrow more money from their relatives or from banks and mutual credit unions. Some of them also borrowed money from the underground pawnshops or private moneychangers. As a result, the joint-owned share was for them the norm for establishing an enterprise. Stone Co. Ltd., Kelong Co. Ltd. and Hope Group are examples of firms that concentrated the founder/member’s initial capital, many of them with only several thousand RMB yuan in their start-up phase. Before the end of the 1980s, some of the private entrepreneurs preferred to take the “red hat” and borrow money from the bank or mutual credit funds in order to support their enterprises. But during the 1990s, especially after the liquidating policies implemented by the government’s central bank, the People’s Bank of China, private entrepreneurs could not easily get loans from the commercial banks. With the banks requiring mortgages as security for their loans and entrepreneurs having accrued more money and the deposit held by their households increasing rapidly, private entrepreneurs turned to partners, relatives and friends to finance their capital gaps. As Table 9 illustrates, during different periods, the private sector has relied on different financing resources.

**Table 9. The Proportion of the Capital Sources Used by the Private Sector (%)**

Year	Capital From Entrepreneurs	Capital From Partners	Loan from Friends & Relatives	Fund from Employees	Bank Loan/ Mutual Credit Fund	Others
1987	37.5	--	20	1.9	40.6	--
1993	45.3	12.1	16.2		10.7	15.7
1997	69	24.9		1	--	5.1

*Source: Chinese Government and Private Economy, The China Federal of Industry and Commerce Press 2000, pp. 348-349.*

Although the stock market developed rapidly in the 1990s, the private sector hardly uses it to finance its businesses. For instance, in December 2000 the market value of stock-A reached 15 percent of GDP and the market value of all stock equities reached 45.3 percent of GDP. Although SOEs were given the priority and right to issue stocks publicly, before 1998 private enterprises hardly issued stocks to enlarge their capital even if their businesses were successful. During that period if they wanted to use the stock market for financing, they had to buy the equities from the listed enterprises, i.e. “to borrow a shell for the egg.” In recent years only, some private enterprises have been directly listed in the stock-A market. But the cost for them to be listed is much higher

than for other state-owned enterprises. In fact, until now, few private entrepreneurs have received this kind of opportunity or right. As a result, in China the private sector still faces many difficulties in access to the capital market for financing.

### LENDING AND INVESTMENT ENVIRONMENT

Before the 15th National Congress of the CCP in 1997, the private economy was regarded as a source of economic disorder and a social evil. When the government decided to enhance the economic order or restructure the national economy, private entrepreneurs were often the targets of attack, and in fact, some private entrepreneurs wretched on their liabilities. As a result, the commercial banks were unwilling to grant loans to private entrepreneurs.

After 1997, when the Central Committee of the CCP announced that the “Government should create environments which offer equal opportunities to participants of all kinds of ownerships, treat all kinds of enterprise without discrimination,” the lending and investment environments began to change in certain ways. The 15th National Congress of the CCP temporized the trend of socio-economic development and further announced that, “Non-state-owned economy, including private economy, of course, is important component of our national economy. The Party encourages and allows factors of production to participate in income-distribution, protects legal income.” These changes of the CCP and government’s views on the private sector should help clear the channels by which private enterprises can obtain more loans from state-owned commercial banks and other credit units. The Chinese Minsheng Banking Corporation was also established in that year. This private share holding bank was created in order to offer more financing services to the private sector.

**Table 10. Shares of Loans Granted to Non-SOEs by State-owned Banks (%)**

Year	Urban collective-economy	Private enterprise and individuals	TVEs	Agriculture	Total
1985	4.95	0.17	5.63	6.85	17.60
1988	5.58	0.17	7.59	7.19	20.53
1990	4.93	0.09	7.42	7.17	19.61
1992	4.76	0.012	7.84	8.27	20.88
1994	3.13	0.018	6.25	6.48	15.88
1998	-	0.03	2.51	2.56	5.1

*Source: Chinese Financial Yearbook, from 1989-99 editions.*

After 1997, the Southeast Asian financial crises exerted a negative impact on Chinese exports, the state-owned banks strengthened their risk controls and the mutual credit unions accrued vast number of non-performing loans. As a result, loans to private enterprises began to shrink. For example, in 1994, the proportion of bank loans to the private sector was 6.27 percent, much higher than in 1998.<sup>9</sup> In 1998, this proportion was only 2.54 percent, lowered by 3.73 percentage points from 1994 as shown in Table 10.

<sup>9</sup> To make this point, we have summed loans to private enterprises and individuals with TVEs as the total figure for the private sector.

To encourage commercial banks to lend more money to small and medium-sized businesses (including private enterprises) for supporting their development and meeting domestic demands, the government has set up a loan guarantee system and removed most restrictions on the investment field of private enterprises (which is summed up as “whatever is open to foreign investors is open to private enterprises”). Beginning in 1998, the government declared that private enterprises could invest in public substructure projects, such as urban bridge building, sewage processing, etc. A survey by the People’s Bank of China indicated that at the end of 2000, the loans granted to the private sector had reached 4.8 trillion RMB yuan, equal to 48 percent of all banking loans, and 9 percent higher than at the end of 1996.<sup>10</sup> In addition, after Mr. Jianqing Jiang, the head of Business and Commerce Bank of China (BCBC), stated on April 6, 2001, that ownership would not necessarily be considered when the BCBC made decisions about whether to grant loans to businesses<sup>11</sup>, the loans granted to small and medium-sized enterprises by BCBC amounted to 1.28 trillion RMB yuan by the end of 2001. This represented 49.8 percent of all its loans in the same period.<sup>12</sup> Recently the People’s Bank of China has again raised the interest rate ceiling controlling loans to small and medium-sized businesses. Obviously, this new ceiling is even better for further supporting private sector development.

### **IMPACT OF GLOBALIZATION AND THE WTO ON THE PRIVATE SECTOR**

China joined the WTO on December 12, 2001. WTO membership has several implications:

- (1) Since they were set up, China’s private enterprises have been operating according to market law. Joining the WTO means that China will participate in globalization and international economic diversification to a greater extent. As a result, WTO membership will expand opportunities for the development of the private sector, and it will help apply the cheap-labor advantage of China
- (2) According to the promises made to the WTO, the Chinese government will take measures to increase the transparency of economic management, which will help eliminate corruption and other social issues, enhance the efficiency of government management, and create a fair, orderly and competitive market environment. These measures will undoubtedly help remove discrimination against the private sector and boost this sector’s development
- (3) The entrance of multi-national corporations will intensify the competition and reveal the shortcomings of the private sector, such as smaller scale, less talent, lower-level technology and so on. We predict that the coming years will be a critical period for the restructuring of the private sector. Some private enterprises will grow up rapidly and some will become more efficient and competitive; others, faced with critical economic competition, will be likely to fail and declare bankruptcy. Since more foreign businesses and technologies will flow into China after its accession to the WTO, not only the state-owned and collective sectors but also the private sectors will face more challenges in the technological and marketing fields.

---

<sup>10</sup> Research group of People’s Bank of China: “On Prudential Monetary Policy,” URL <http://www.pbc.gov.cn>.

<sup>11</sup> <http://finance.sina.com.cn>, 6 April 2001.

<sup>12</sup> [www.xinhua.org/fortune/2002-03/06/content\\_304069.htm](http://www.xinhua.org/fortune/2002-03/06/content_304069.htm).

## GOVERNMENT POLICIES THAT SUPPORT OR HINDER ENTREPRENEURIAL ACTIVITIES IN CHINA

### EXTENT AND COMPLEXITY OF GOVERNMENT REGULATIONS IN CHINA

In China, the relationship between the government and the private sector is unlike the “father and son” relationship between the state-owned or collective sector and the government. In fact, in China there are many government branches that have responsibility for managing and protecting the public sector, but no responsibility for managing and protecting the private sector. The main branches that have direct responsibilities for managing and operating the private sector are the Bureau of Business and Commercial Management at the central government level as well as the local and county levels. The China Federation of Industry and Commerce (CFIC) is the institution that serves private enterprises, individual businesses and private entrepreneurs. There is only one CFIC at the national level, but at the provincial, local and county levels there are many Federations of Industry and Commerce (FICs). They are always thought of as “the home of the individual businessmen/women and private entrepreneurs.” Apart from these two institutions, the other government branches, including the Bureau of Taxation, Environment Protection Bureau, Ministry of Labor and Social Security, only have responsibility for regulating and inspecting private sector business activities but no other responsibilities for supporting their development. So private sector persons, including individual businessmen/women and private entrepreneurs as well as their staff and workers, always say they are like “no-mother’s babies” [orphans]. For example when individuals in the private sector encounter difficulties or have questions about the development of their enterprises, there is no way to get any help from the government branches, but when their enterprises have made money, there are always many government officials eager to inspect them according to government regulations, rules and laws. We suspect that in this situation these officials aim not only to regulate the private sector’s activities but also to get the chance to “rent-seek,” i.e. to gain some benefits for themselves by executing this kind of regulation. This might be a very important source of the corruption in China.

### GOVERNMENT SUPPORT/PROMOTION OF ENTREPRENEURSHIP

In recent years, especially after the 15th National Congress of the CCP, the governments, central and local, created many documents for supporting/promoting private sector development and enhancing private entrepreneurship.

First, the political status of private entrepreneurship has been enhanced a great deal. For example, up to the present time, private entrepreneurs who have been elected to the People’s Congress at the national and provincial levels as senior representatives are 48 and 372 persons respectively; the number elected to serve on the Committee of Chinese People’s Political Consultative Conference (CPPCC) at the national and provincial levels are 46 and 895 persons respectively; and those voted to the China Federation of Industry and Commerce (CFIC) as members of its executive committee are 183 persons with three as vice-chairmen and 46 as members of the Standing Committee.<sup>13</sup> According to Jiang Zemin’s speech on July 1, 2001, talented private entrepreneurs increasingly are being accepted into the CCP and will become government leaders in the coming years.

---

<sup>13</sup> See also Lu, Xueyi, ed., *Report on The Social Estates of Contemporary China*, (China Social Science Documentation Publishing House, 2002), 214-215.

Second, the role of private entrepreneurship in economic capacity has been strengthened a great deal too. For example, by the end of 2000, there were more than 3,950,000 entrepreneurs registered publicly, an increase of more 21.5 percent from 1999. In fact, these entrepreneurs are the property owners of their private firms. Their publicly registered capital is more than 133.08 billion RMB yuan, which is 13 times larger than it was in 1991.<sup>14</sup> If the government does not support, help and promote the private sector, its economic capacity and competitive ability will not develop rapidly. In fact, since 1999, there are a large number of provincial governments that have issued documents that support and promote private enterprises in order to help them develop and grow rapidly.

Third, the attitude of the people towards private entrepreneurship in practice has changed considerably from before. We can understand this fact by analyzing the structure of private entrepreneurial ventures. According to the results of a random sample survey (See Table 11), most private entrepreneurs come from government departments or the public enterprises. Among the private entrepreneurs, only 23.4 percent are from non-post and non-rank occupations, and most of these were regular workers, waiters or peasants before becoming entrepreneurs. These results illustrate the fact that many private entrepreneurs originally worked in the government, public-owned enterprises or some villages. So, if you want to say that in China the private entrepreneurs are incubated from the cadre-based infrastructure you might be correct.

**Table 11. Structure of Private Entrepreneurs' Former Occupation and Status**

Former occupation	Percentage	Status	Percentage
Technologist	10.3	Tenants of public firms	22.9
Cadres	43.3	Government cadres	21.5
Workers & waiters	14.2	Village cadres	3.6
Peasants	9.3	Non post and ranks	23.4
Individuals	17.4	Others	28.6
Others	5.2		
Total	100.0		100.0

*Source: From The Fourth Private Random Sample Survey Data.*

Lastly, the ideology is also propitious to enhance private entrepreneurship. For example, in his speech on July 1, 2001, Jiang Zemin said that although the composition of China's workers has changed, their class status would not change even though other new classes or estates have appeared. The new estates, e.g. private founder-members, private technicians, managers serving in private firms, individual businessmen/women, private owners, private brokers and free-professionals, all depend on honest employment and legitimately operating businesses to earn a living and make their contributions to the development of a prosperous socialist society. They are also creating the special socialist construction that fits China's practices.<sup>15</sup> Clearly, this speech predicated that in the future an increased number of new or covered "red hat" capitalists will enter the CCP since they will dominate China's economic resources and will have social wealth as long as they are successful in their social and economical practices. In this situation, if they are willing to follow the socialist road of the Chinese people and support the creeds and positions of the CCP, they will not only become members of the CCP but also leaders of the party. The CCP's basic object

<sup>14</sup> Ibid.

<sup>15</sup> See also Jiang, Zemin, *On the Theory of "Three Representations,"* (Central Documentation Publishing House, 2001), 169.

is to push forward the development of China's society and rapidly increase affluence in the country. Whoever is able to lead the people to achieve this goal will become a main member and even the leader of the CCP. This approach is in contrast with another document, "A Notice for Strengthening CCP's Construction," issued by the Central Committee in 1989. According to that document, private owners (i.e. private entrepreneurs) could not be accepted into the CCP. And if an old member of the CCP became a private owner but did not distribute most of his after-tax revenues in order to create more social wealth or develop public projects, he/she would not be able to retain his party membership.<sup>16</sup> If that policy were still implemented, the result is easily imagined. Happily, it is now noteworthy that the CCP's guidelines and theories have been completely changed and the private sector has joined the basic economic system of China. This change is very important. It means that the people-based infrastructure and physical infrastructure have been basically prepared for the future. The future development of the private sector is only a question of time, not a question of basic policies. We estimate that the 16th National Congress of the CCP will make more important decisions that will further advance and perfect these infrastructures.

### **TAX POLICIES**

There have been several problems pertaining to tax policies: irregular fee collection, arbitrary interpretation of the tax laws and regulations, and an undisciplined taxation system (e.g. some government officials or departments might continue rent-seeking for their own self-interest by ignoring the public's interest when executing their duties). Normally the private sector has to endure more injuries than the public sector. Recently these kinds of problems have been resolved to a certain extent but not corrected and eliminated completely. The central and provincial governments have considered including irregular fees in the tax system and prohibiting the imposition of any irregular fee on the private and public sectors. The goal of taxation system reform is to establish a uniform tax and fee collection and management system. All enterprises and businesses, whether they are publicly owned or privately owned, should have the same value-added tax, income tax or other normal taxes, and regular or irregular fees. Any government officials and departments will be required to implement the taxation system as well as the concrete tax laws and regulations, but will not have the right to change them at their discretion.

### **EXISTENCE OF A SOCIAL SAFETY NET AND IMPACT ON THE ENTREPRENEURIAL SPIRIT**

As we have discussed above, the basic environment for supporting and promoting private entrepreneurs and the development of the private enterprises is now in place and more perfect. But until now, private entrepreneurs have also worried about how to protect their private property rights by law. The Amendatory Act on the Constitution of PRC in 1988 stipulated that in China the state allows the private economy to exist and develop within the scope of the law (for the private economy is complementary to the socialist public economy), and announced that the state will protect the legal rights and benefits of private sector and implement policies to pilot, supervise and regulate them. Nevertheless, private entrepreneurs still worry about their future survival and development. Given this situation, the further development of the private economy is still difficult.

To resolve this problem, during the 15th National Congress of the CCP, Jiang Zemin analyzed the reasons why, for China's current economic development stage, the Chinese government has to

---

<sup>16</sup> A Notice for Strengthening CCP's Construction, quoted by Xueyi, 243.

jointly implement a basic and dominant economic system of public ownership with multi-property ownerships. Although in this important conference, the CCP offered to encourage the development of the private economy, it still emphasized the policies of piloting. As a result, the private sector has not been able to develop more rapidly since the problem of protecting private property rights against any encroachment still exists and is a source of worry for private entrepreneurs.

However, in Jiang Zemin's important speech on July 1, 2001, he further emphasized that the CCP will select more outstanding private entrepreneurs who accept the creed and constitution of the CCP and are willing to make every effort for the CCP and the party. As a result, the light for pushing forward private economy development should become brighter. And under this shining light, the private entrepreneurial spirit and private entrepreneurship, which are constantly innovating and making great strides in economic development, will rapidly mature.

### **RULE OF LAW AND PROTECTION OF INTELLECTUAL PROPERTY RIGHTS**

China is a developing county. Now she is a member of the WTO. As a result, the Rule of Law and the protection of intellectual property rights will be needed to further supplement and consummate China's new responsibilities. It is clear that if we want to advance scientific research and technological innovation and realize significant development, we must further protect intellectual property rights, including basic intellectual property rights, applicable technological property rights and social science research results. In this area, China has done a lot but needs to do more in the future.

### **CONCLUSIONS AND RECOMMENDATIONS FOR PROMOTING THE RAPID DEVELOPMENT OF PRIVATE ENTREPRENEURSHIP IN CHINA**

To sum up this four-part analysis, we are able to arrive at some important conclusions about the development of private entrepreneurship in China. First, China's basic political, economic, social, cultural and legal environments have changed completely from 1978 until now. The CCP and the governments, from central to local, have developed both the physical infrastructure and people-based infrastructure. Even the Rule of Law for supporting and promoting private entrepreneurship development has been reformed a great deal. Currently, the chief challenge for private entrepreneurs is how to achieve more rapid development in a shorter time period.

Second, the financing problem for private enterprises, due to the economic regulatory structure, has been largely overcome over the last year. Commercial banks (including state-owned and other shareholding banks) are more willing to lend money to the private sector, however only to the large and mid-sized private enterprises in good credit standing and not to the small and medium-sized private enterprises. This is mainly because the costs for the banks to lend to the small and medium-sized private enterprises are higher than the costs of lending to other private enterprises. Among these large and mid-sized private enterprises in good credit standing, some need to borrow more money from the banks, but others have no need to for bank loans since they have enough money to maintain their operations. Some in the first group who need loans are willing to get the "free lunch" from the bank but not willing to burden themselves with any loan risk. So most commercial banks prefer to give mortgage loans, not credit loans, to private enterprises. According to my survey,

among private enterprises that are willing to borrow money from the bank, there are a large number that have the ability to produce but no ability to take on a mortgage loan. The reason is not that they do not have sufficient assets to apply for a mortgage loan but rather that their assets are not authorized by the local government. If this information is correct, there needs to be a solution, for private entrepreneurs that find it difficult to apply for a loan. This should also address the question of why the small and medium-sized private enterprises are still unable to get loans from state-owned banks and the large share holding banks up until now.

Third, the movement by the government towards a rules-based environment is an essential step towards removing the major impediments to the private sector for realizing more rapid development and growth. Any improvement in commercial legal processes, effective regulatory supervision and the reduction in the arbitrary application of official regulations, will have dramatic effects on the environment faced by the private sector. All of the elements of discrimination against the private sector and private entrepreneurs should be removed as soon as possible to advance the process of market-oriented reform. The main challenge to China's national economic development in the coming years is having the Rule of Law but no court officials charged with following up on violations.

To summarize my opinions, I would like to make five suggestions to the government of China. First, strengthen the legal system and consolidate the management of court officials who enforce the laws. If the tipstuffs or court officials are violating the law when they enforce the Rule of Law, no one will follow the Rule of Law. In this situation, not only is the private economy unable to develop further, but the national economy, including the public sector, is also not able to make developmental strides under the market system.

Second, survey private sector assets and authorize the final owner of these assets. If the asset should be notarized to the private entrepreneur or the private enterprise, the government, especially the local government, should make the final decision to authorize it to the private entrepreneur or the private enterprise. To correctly determine the asset price, the cost of its original investment and normal depreciation rate in the same trade area should be calculated. Market price also fits into the calculation.

The third suggestion is that the government should distinguish the behavior of the two types of underground pawnshops and private moneychangers in the local areas. Some follow the rules of financing in the market economies of other countries and do their business well. We should not close these pawnshops and private moneychangers, but rather investigate them and confirm what rules and regulations will enable them to develop successfully. As for the other pawnshops and private moneychangers that do not follow the rules, the correct choice is to close them completely since even in other countries with market economies these types of financial organizations are not permitted. Some experts have suggested establishing more small private banks or other private financial organizations. I think that authorizing these underground pawnshops and private moneychangers and approving their operations will be the easiest way to develop private financing and banking systems in China in order allow small and medium-sized private enterprises to efficiently obtain needed financial services.

The fourth suggestion is to equalize the direct financing rights in the stock market for all enterprises, including state-owned, collective-owned, FDI and private enterprises. So far, most direct financing



rights are held by the state-owned enterprises. This deviates from and violates the rules of market economies. The present situation is not conducive to competition and does not eliminate idleness and corruption but rather is an impediment to economic development. For this reason, we need to change the current rules and permit all efficient enterprises to have an equal opportunity to be listed in the stock market.

My last suggestion is to revise the current Constitution of the PRC in order to decree that any private legal income or property is strictly protected by the government and its laws, and no one is able to violate any private legal income and property. Of course, the government and law should not protect illegitimate incomes and properties. Any such behavior that puts illegitimate income and properties into individual pocketbooks should be punished sternly by the law.

**Yingqiu Liu**, born on August 23, 1950, is a Senior Research Fellow and Professor of Economics at the Chinese Academy of Social Sciences (CASS) and Co-Professor of Economics at Nankai University, Shandong University, Lingnan University at the University of Zhongshan, and the Southwest Finance and Economics University. He has been the Director of the Center for Private Economy Studies at CASS since 1998. Dr. Liu graduated with a Ph.D. in Economics from Nankai University in 1991. From April 2001-02, Dr. Liu was a visiting professor at the China Data Center at the University of Michigan where he conducted economic research. Prior to that, he was the Deputy Director-General and Academic Committee Member of the Bureau of Scientific Research of CASS (1997-2001). Dr. Liu has published more than ten academic works and over two hundred research papers in the field of economic research, including his most recent publication, *Report on Great Development of Western China* (2000). He is set to publish his latest research, *China's Economy in the Second Period*, this year. Dr. Liu has won the Social Science Prize several times in China and received lifetime recognition with the Government Special Allowance of State Council in 1993. In 1996, he gained another title as a Standout Expert from the Chinese Academy of Social Sciences.

## REFERENCES

- Analysis Group: "On Prudential Monetary Policy," [http:// www.pbc.gov.cn](http://www.pbc.gov.cn).
- Bureau of Labor, Bureau of Urban Construction, Ministry of Public Security, and Bureau of Industry and Commerce Management. *Directives on Issues Related to Land Used by Urban Collective and Individual Economy*. May 6, 1981.
- Chinese Financial Yearbook*, 1989-99 editions.
- Chinese Government and Private Economy*. The China Federal of Industry and Commerce Press, 2000.
- Chinese Reform and Development Institution. *The Development of Chinese Private Economy*. Hainan: Democracy and Construction Press, 1995.
- Golay, Frank H. "Entrepreneurship and Economic Development in the Philippines." *Far Eastern Survey*. Vol. 29. (June 1960): 81-86.
- Jiang, Zemin. *On the Theory of "Three Representations."* Central Documentation Publishing House, 2001: 169.
- Liu, Yingiu, "On Necessities and Realities of China's Economic Non-governmentalization," *Economic Research*, No. 6, (June 1994).
- Lu, Xueyi, ed. *Report on The Social Estates of Contemporary China*. China Social Science Documentation Publishing House, 2002.
- Marx, Karl. *The Capital*. (1972, Chinese version).
- National Bureau of Statistics of PRC. *China Statistical Yearbook*. China Statistics Press, 2000.
- Office of the State Bureau of Business Management, ed. *Statistic Collection of Business Administrative Management*, 1989-2000 editions.
- Statistics Department of the PRC. "The People's Bank of China Quarterly Statistical Bulletin." (2002).
- [www.xinhua.org/fortune/2002-03/06/content\\_304069.htm](http://www.xinhua.org/fortune/2002-03/06/content_304069.htm).