Reflections on the Revitalization of Northeast China

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Abstract: This paper uses the key facts and figures to reveal that success of SOEs’ reform is the key to revitalize China’s Northeast Region. It also proposes innovatively that essence of being state-owned and letting the ownership of enterprise possessed by government, which functions as the service agency to handle national affairs, is the contrary to the principle of fair competition under the market mechanism. Thus, this article further points out the necessity to continue the completion of SOEs reform and reconsiders what is the real loss of state assets. Using national boundary as the standard is also a new perspective that is put forward for the first time. At last, this paper argues four approaches of marketization for state-owned enterprises in China’s Northeast region: delineation of Special Economic Zones, demise or sale of SOE assets and personnel separation, shareholding system reform and capital socialization.

Key words: northeast region revitalization, SOEs form, loss of state assets, capital socialization

1. Introduction

After 10 years of the implementation of revival strategy for old industrial bases, China’s Northeast region still remains a further step towards a new level. On July 17, 2015, Chairman Xi Jinping came visit and listen to the opinions and suggestions regarding the revitalization of old industrial bases such as China northeast region, and also delivered an important speech. Chairman Xi emphasized the necessity to deepen the reform of state-owned enterprises, improve the corporate governance model and management mechanism, truly establish the enterprise’s dominant position in the marketplace, enhance enterprise’s inherent vitality and market competitiveness, and develop enterprise’s leading force (Xi, 2015).

2. The Key to the Revitalization of Northeast Is State-Owned Enterprises

Does problem exist in China’s Northeast Economy after all? In 2014, the economic growth rate for the three provinces in China’s northeast region, namely Heilongjiang, Jilin, and Liaoning are 5.6%, 6.5% and 5.8%, respectively. However, growth rates are rather low compared to other provinces, and even below the average national economic growth rate in 2014, which is 7.4% (China Statistical Yearbook, 2014). As china entering the “New Normal” stage that signifies a future economic development downturn, the Economy in the China’s northeast region might possibly slow down at a greater rate, or even stagnation or retrogression, and eventually become economic depression. It would be very reluctant and painful for us to witness a rich land that comprises of the most abundant natural resource, the most developed transportation and infrastructure, and people of the most
spirit of adventure, to become degenerate!

2.1 The Reason of Economic Decline Is That the Resources Have Been Absorbed by SOEs

Northeast China used to be the typical representative of the global Soviet Union style economy. Nonetheless, even now the Soviet-Union’s planned economy has been demolished worldwide, the state-owned enterprises in China’s northeast region are still maintaining. Compared to the national economy, Northeast China has not really revitalized, and it missed two historic opportunity: in 1990s, a radical overhaul of state-owned enterprises took place, which resulted in the sale of a large number of small and medium state-owned enterprises, as well as the laid off of millions of workers. That was one opportunity to revive the northeast economy. Unfortunately, the reform was not thorough enough that many large state-owned survived.

In 2003 “Northeast revitalization” strategy launched, a lot of government investment to save the northeast state-owned enterprises, local governments again become strong. During this period of time, SOE’s reform direction has deviated from the original intention of this period, shifting from “sell state-owned enterprises, reject burden” in the 1990s to a “strategic restructuring, bigger and stronger”, and brought Northeast’s economy once more back to the era of planned economy. Enormous amounts of Northeast’s manpower, material and financial resources, were still inefficiently invested into state-owned enterprises, instead of being allocated by the market mechanism.

2.2 Northeast SOE Reform Did Not Complete Its Historic Mission

Commonly existed question within Northeast SOEs is “restructuring” but not “change the system”, the management mechanism of state-owned enterprises, decision-making mechanism, and the distribution mechanism is still with traces of many of the original System. The purpose is to change the substance of the restructuring mechanism, and thus for management and development of enterprises has brought a fundamental shift. That is an extension of the restructuring of state-owned enterprise reform is to improve and deepen the process of modern enterprise system. First, let the market decide the fate of the enterprise. In a competitive mechanism, let the market this “invisible hand” decide the survival of the fittest; the second is entirely independent enterprises. Government enterprises and public service agencies, large shareholders can only exercise their powers in the shareholders’ meeting and the board of directors; third is quantitative assessment of business operators. All along, the state-owned operator appointed by the government, no obvious “misdeeds” generally only rise, not fall, but the capital is profit-driven, state-owned assets should also strive to achieve and increase the value. Operator’s competent or not important criterion is its ability to create benefits for shareholders. With such features to measure the operating mechanism of state-owned enterprises in Northeast, relatively restructuring goals have still some distance.

2.3 Northeast Economic Environment Is Not Optimistic

Northeast’s economic environment is worrisome. In recent years, net population outflow of the three northeastern provinces has reached approximately 2 million each year, and this population outflow proportion is one of the highest among all regions of the country (Yu, 2014). The outflowing population basically is the social elite and with adventuring spirits, and in contrast, the inflowing population is neither technical elite nor talent. Moreover, under the auspices of the state-owned enterprises, the family planning policy has been thoroughly implemented, which leads to severely aging population. What would be way out for an economic environment like this? In cities like Shenyang, Panjin, Anshan, Benxi, Yingkou, the numbers of everywhere existed
state-owned enterprises and assets are remarkable. Many people are proud to work in state-owned enterprises where decent welfare, guaranteed career has. Therefore, they spared no expense to place their children into the state-owned enterprises even willingly taking low wages, because of the easy and comfortable jobs. However, those Northeasterners who are skillful and talented or graduated from university tend to move south to Beijing, Shanghai, Guangdong, to work and start careers in these economically developed regions. There is barely any nationwide famous private enterprise is form northeast.

2.4 Northeast’s Way Out Lies in the Resume of Reform

People may worry about what to do with a bunch of state-owned enterprises in Northeast? Compared to the 1990s, today’s economic situation has been much better and also its ability to digest pains is definitely stronger than in the past. The approach to manage state-owned enterprises is much more moderate than back then. Reform cannot be implemented without pain, people in the northeast have to endure and cross the hurdle to restart the reform so that northeast can be revitalized. Without great determination, absolute means, enduring patience, it would be impossible for Northeast to have way out. If northeast function as an experiment field for China’s second reform and opening, well-manage internal affairs, attract talent, and then Northeast region which is adjacent to the four countries will eventually become an economically open and developed business and trade center that enjoys convenient transportations and urban prosperity. In addition, the geopolitics of Northeast Asia will thus bind to improve. With another thirty years of time, this land in Northeast can certainly be harvested.

3. Reconsideration the Connotation of State-Owned Enterprises

3.1 The Concept of State-Owned Enterprises

SOE, generally known as a state-owned enterprise, which is legally autonomous, self-financing, independent accounting, socialist commodity production and business units. The National Bureau of Statistics’ NUC letter (2003) No. 44 defines state-owned enterprises as such: generalized state-owned enterprises refer to enterprise possesses national capital funds, the first category: the purely state-owned enterprises. Total capital funds of the business or company are state-owned; the second category: the state-owned holding enterprises. The third category: the state-owned shareholding enterprises. State-owned enterprises in narrow senses, refers only to the purely state-owned enterprises (National Bureau of Statistics, 2014).

3.2 State-Owned Enterprises Are Essentially Owned By Government

The definition of state-owned enterprises states that, from the ownership point of view, state-owned enterprises are owned by nation or all citizens, but in essence, are government. This is because that government, instead of all citizens, is the direct beneficiaries and loser of state-owned enterprises’ profits and loss. What worthy of further consideration is that a country’s government at all levels is meant to function as service agency that deals with all national affairs at different levels services. If a service agency is directly in charge of corporate excessively, then how is this government able to well perform its role as the service agency? Can the government also provide equitable services to their own invested enterprises and the enterprises invested by other parties? For investment and R&D in the minority fields that have important strategic significance, government usually has a monopolistic power. However, excessive monopoly in too many areas is not harmful for fair competition, and without competition, the utilization efficiency of social resources is relatively low, which is difficult for market
mechanism to realize.

3.3 How Does the Foreign Government Control Their Enterprises?

There are people worried about whether handing over industries such as aircraft manufacturing, steel, energy development to the private sector will cause these industries to be out of control. What about Boeing, Airbus, AT&T telecommunications, Rockefeller’s Standard Oil, Carnegie Steel Company, which one is not private-owned enterprise? Also taking a look at the practices of the governments in Europe and America: What their governments issued is the introduction of policies and regulations, which are: you can produce, but not a monopoly; you can sell products, but to who you can and cannot sell is decided by government. For example: who can buy alcohol, who can buy gun, who can hunt, and even who can watch erotica entertainment films, are all clearly defined, and offenders will be punished by law. The world’s order relies on regulations to sustain. Therefore, we can say that market economy is an economy based on legal system. Isn’t the working efficiency high for their private-owned enterprises? Isn’t it worthy for us to learn and adopt the numerous rules and regulation applied by these countries that have mature market economy?


State-owned enterprise is the product of the planned economy, its basic characteristics are: First, lifetime employment cadres and personnel; second, it’s established by national or local financial contribution; third is no shareholder constraints, only the higher administrative authorities, leading to the lack of pursuit of economic interests and social benefits. The so-called state-owned enterprise restructuring, refers to the restructuring of state-owned enterprises to corporate form, which is: independent directors, supervisors, independent operating, self-financing. The reasons state-owned enterprises have to restructure as follows:

4.1 The Operators Are Lack of Sense of Responsibility

SOE leaders are designated by the Government and he may be transferred at any time. If there is a certain risk for reform and innovation, the SOE leader will naturally choose to maintain stagnant by which they can reclaim security and peace, instead of moving forward. Enterprises rely on government funding and investment to expand the business. And leaders’ capability is based on whether they get the funds from the government. If the enterprise realizes a deficit, it is only a loss for government, the leader might just move to another place to work. Economist Wuchang Zhang’s ten-point summary of state-owned enterprises is very profound. He said: “The state-owned operators will not be cautious about spending money because they are not using their own money.” (Zhang, 2004). Just imagine: If reconstruct the SOEs from state-owned to private-owned in the form of shareholding, the state (government) can occupy a certain share, and also the company’s assets is not exclusively private-owned. But investors have the right of supervision, and the underperforming managers may be dismissed by a vote. More importantly, people that good at management can acquire companies when the share price is low, and realize the appreciation of wealth through good management. On the other hand, small shareholders can put their shares for sales if they are not satisfied. Transfer of the shares represents willingness, because to acquire or sell is the most powerful expression. Therefore, “as long as the business is private equity, it does not matter who owns the shares. Efficiency should be viewed rights of management and financial returns instead of the ownership.” (Zhang, 2004).
4.2 The Government Maintaining Monopolistic Power Is A Serious Damage to the Economy As A Whole

In the freely competitive markets, the state-owned enterprises mainly rely on the government maintaining a monopolistic power or patent to survive. Thus, state-owned enterprises’ social cost of the existence is in fact very high, and they do not fairly compete with private enterprises. The unprofitable state-owned enterprises have realized reform through the revolution in the past, but the profitable ones would encourage the government to continue to maintain the monopoly. This is simply a complex that we cannot overcome.

The government maintains a monopoly is a breeding ground for corruption. As long as the government manages the enterprise, then the system of controls and allocation of resources will deviate from the fair trajectory, or even intensify and result in self-evident rent-seeking behavior. Therefore, controlling power is the main cause of corruption. Just imagine, in recent years, enormous amounts of college students go attend the civil service exam, even though wages are not high, but the political privilege is rather attractive. Economist Wuchang Zhang said: “Once privileges to corruption can be defined, institutionalized, the end of reform follows.” (Zhang, 2004).

Therefore, it is necessary to reform and privatize state-owned enterprises in the form of shareholding or other methods. Operators will certainly be very careful when they use their own money, and this is the golden rule of economics. More importantly, the government can focus on collecting and spending taxes money and fulfill its service function, instead of worrying about maintaining the monopolistic power.

4.3 The High Costs of Excess Personnel Enable Enterprises to the Loss Competitiveness

Workers are reluctant to leave their positions in the state-owned enterprises, and this is a deep-rooted traditional thinking in the Northeast. And even now a quota place in the state-owned enterprises is priceless. If an undergraduate can get into state-owned enterprises, it would be something the whole family should be contented about.

In the eyes of many people in Northeast, working in state-owned enterprises is a lifetime guarantee, and they are convinced that the government will look after them anyhow. Many employees are reluctant to leave the company even though they have nothing to do at work. According to our survey, out of 90,000 employees in Benxi Iron and Steel Company in Liaoning Province, there are 70,000 surpluses. But the enterprise has to take care of people because of that, firstly, these people are unwillingly to leave; secondly, layoffs could lead to chaos. Especially during the petition, even business leader’s own position will be at risk if he cannot maintain the stability in the enterprise. In this case, who can he layoff? Bearing so many surplus employees, how will the enterprises maintain competitiveness?

For SOEs’ reform, as long as the rights of the assets can be clearly defined, the main issue should not be how to define it. Shareholding system is one approach, the sale of state-owned enterprises as a whole is another approach, and offering to employees or cadres can also be an alternative. It is important to clearly define who should possess the rights of the assets. For the first time defining, the rights of the assets may fall to the hands of poor management, but as long as the assets or shares can be transferred, it will soon be transferred to operators who are good at the management. And this is the choice of the business owner. After such property transfer, workers can be spread out, and talent can be retained and put into important positions.

5. How to Define the State-Owned Assets Loss

The loss of state assets that we usually refer is caused by the subjective intent or negligence, violation of laws,
administrative regulations and rules, of funder of state assets, managers, or operators. So how should we treat the loss of state-owned enterprise restructuring and asset loss? There is a principle in economics, known as the two evils, the lesser should be chosen.

Marxist political economy has been teaching us that the main driving force of social development is the contradiction between the productive forces and production relations. And social progress is reflected by a new production relationship’s promotion and liberation of the productive forces. The fundamental task of socialism is to develop productive forces. Marxism believes that before the proletariat seize power, its main task is to carry out a social revolution to overthrow the rule of capitalism, establish the proletarian power, and liberate of the productive forces. After the proletariat seizes power and establishes a socialist system, the main task is to further emancipate and develop the productive forces.

The development of social productivity is where socialist countries’ most important and fundamental interests lie. Deng Xiaoping’s cat theory also states that in the primary stage of socialism, the development of the productive forces is of overriding importance. SOEs’ such mode of production has presented many drawbacks, and it has been gradually falling behind and hindering the development of productive forces. Take a look at “Made in China” label these days throughout the world, but which one is produced by state-owned enterprises? Although the “Made in China” is also problematic, but compared with the shortage of materials before the reform and opening up in China, it has been really an immeasurably vast difference. Now we have to admit that SOEs reform is an important way to liberate the productive forces.

According to elaboration of the “People’s Republic of China State-owned Assets Law”, the alleged corporate restructuring means:

- State-owned sole proprietorship enterprises change to state-owned companies
- State-owned enterprises, state-owned companies change to the state-owned or non-state-owned capital-holding company
- State-owned capital-holding company change to non-state capital-holding company (People’s Republic of China State-owned Assets Law, 2008)

Just imagine, in these three ways, where will the state-owned assets loss to? Firstly, the assets lost to the hands of individuals, such as contractors, new operators, or stockholders, etc. Wuchang Zhang believed that as the members of a state-owned enterprises for many years, these people should be somewhat Preferential (Zhang, 2004). In fact, these people usually carry on the business, or participate in enterprise management as stakeholders. The assets are still in the Chinese territory, rather been transferred than disappeared. Even if the, assignment of the assets is imbalanced in some way, the result would not necessarily be worse than the mess before the restructuring. Just like the pain during a surgery for patients are inevitable, but it cures disease after all. Secondly, the assets are lost to the foreign investors that acquire enterprises in China. But the fact is that foreign factories are still on our land, cannot be taken away, and they have to employ Chinese labor. At best, they invest a lot of money, take over a business, but inject an efficient mode of management. Third, foreigners sell the SOEs for high prices after acquiring them. It’s slightly like arbitrage, and considered as a real loss of the state assets. But this usually occurs in the financial enterprise, with the nature of financial transactions and should be prevented by correctly judging the stock value, or prohibiting selling SOES to foreigners or financial institutions.

In fact, there are two ways to give up state-owned enterprises. Firstly, if the government no longer maintains a monopolistic power, abolish all the rules and regulations that support the state-owned enterprises, and let SOEs and private enterprises freely compete in the marketplace, state-owned enterprises will need to fend for
themselves in a competitive market. Assets of state-owned enterprises will not be lost, but be played out. But this will be the loss of government. Secondly, is to convert state-owned enterprises to private companies in the form of shareholding or other ways. Thus, the chance of survival for enterprise in a competitive is better, and it also possibly reduces the loss of the government.

6. Market-oriented approach for the state-owned enterprises in Northeast

SOE restructuring involves three major problems: the disposal of assets, equity setting, and personnel placement. What kind of approach should Northeast seek to break through the three SOEs restructuring dilemma and struggle for survival in desperate situation?

6.1 The Construction of Special Economic Zones to Form A Market Atmosphere

Why not replicate what Shenzhen did in the past? Government can draw a circle in the Northeast, mark it as a special economic zone and thoroughly pursue the free market operation mechanism, such as implementing the simplest and lowest level of taxation, or even building a first-class duty-free paradise in China. Government can offer the ownership of land to private and permit for trade as to encourage investment of the private capital. Government should also provide equal protection for both private and foreign investment, as well as abolish the rigid labor laws and welfare system in order to enable the Northeast business environment becomes simple and clear. Government are no longer supporting state-owned enterprises with subsidies, favoritism, or assistance, so that only the most efficient firms will survive while the inefficient enterprises be eliminated, and let Special Economic Zones absorb part of the state-owned assets and personnel after the restructuring. The allocation of resources will become more reasonable and efficient, and then expand the spillover effect of the economic zone and gradually form a market economy environment.

6.2 Encourage the Separation of Surplus Staff from State-Owned Assets, Together with Its Subsidiary Assets

State-owned enterprises have both idle equipment and personnel, and some obsolete equipment may still have utility value. The obsolete equipment will be given timely treatment in the private enterprise such as improved or transferred, in order to get some residual value. While if in the state-owned enterprises, such resources are usually waiting to be scrapped or disposed. Government should encourage surplus workers to separate from the SOEs and allocate or transfer certain subsidiary assets to workers. Or the assets can be contracted to individuals and transferred to the hands of private enterprise, which is also conducive to the public. According to our new understanding of state assets, this kind of shift of the state-owned assets is not essentially a loss. And auction of the state assets may be an even more equitable manner, as surplus personnel will be naturally dispersed after the sales of some assets. As a result, the reduced labor costs state-owned enterprises will enhance the competitiveness of enterprises.

6.3 The Sale of Shares

Privatization of state-owned assets allocation can easily lead to controversy. The criteria and price of estimation are also difficult and can lead to either overestimate or underestimate. Generally, the sale of shares is the least troublesome. The nature of joint-stock reform of state-owned enterprises lies in the realization of shareholder value as the ultimate goal of its operations. As can be seen by conventional practice, even if excluding the monopoly elements, monopolistic resource factors etc., the state-owned joint-stock company has more
advantage compared to private enterprise advantage as assets exercise body.

Based on the achievement and stock performance China’s large state-owned joint-stock enterprises, we can observe that although a number of large state-owned enterprises have a shareholding system reform and has been listed in the stock markets both at homeland and abroad, but their stock prices fluctuate with stock market volatility rarely significantly exceed the market price, as they have not yet implemented value-based management. Whereas those private listed company’s whose core strategic objectives are to seek any option to maximize shareholder values, has increased their share price performance far beyond the stock market index and achieved adverse economic rise despite the global economic crisis. Therefore, through performance assessment methods, such transmission mechanism with goal of maximizing shareholder value will be entirely possible to stimulate the state-owned operator of power and responsibility.

6.4 The Large State-Owned Enterprises’ Capital Socialization Path

Improving large state-owned enterprises’ efficiency cannot be achieved by simply transferring the ownership. Capital socialization may be a viable option. Besides the traditional form of capital privatization, capital socialization includes the following three conditions:

Firstly, combining the capital from several private investors and handing over to a nominated person to manage, so as to start a company and achieve mission of maximizing capital earnings; secondly, is the joint capital of social groups. For example, some equity investment fund companies take their investors’ money to other companies and stay as shareholders, even directors and themselves might be professional managers who can carried out certain business activities by law; the third is legal social capital. Harvard and Yale University in America both have assets that worth more than $10 billion and several thousand other universities in the United States also have large amount of money. These fund managers can invest with such a large-scale fund, and their purpose and mode of operation are different from shareholders and directors of the private capitalists. Nowadays shareholders of many big corporations are somehow nominee shareholders. Although shareholders are the true investor, but their source of capital are not just of their own. The nominee shareholders, the diversification of ownership’s definition, operator’s professionalism, workers capitalization, are one of the main modes of modern enterprises. Although the property socialization also have a lot of negative effects, the sustainability, standardization, and social platform it provides are far better than the private companies. Only such large-scale enterprise can create a wide range of white-collar working class, which is the basic force required for social stability.

To summarize, there are three basic paths to convert the large state-controlled enterprises share capital into share capital held by social institutions: one is to transform into social capital; the second is converted into equity capital of state ownership; the third is converted to an annuity capital. If state-owned capital could be either converted into annuity capital or for sale, but keep the equity capital while allocate the public capital, the capital appreciation can be separated from state-owned.

Chairman Jinping Xi has further pointed out the direction for Northeast’s revitalization, where he emphasized that we should resolve to get rid of structural and institutional obstacles and develop an institutional mechanism that completely docks with the market and fills with inherent vitality is the fundamental strategy to promote the revitalizing of the old industrial base in northeast. We should adhere to the direction of socialist market economic reforms, actively discover and develop the market, further decentralization, optimize the business environment, find ways and solutions from market liberalization (Xi, 2015). We are deeply convinced that the revitalization of
northeast will depends on the revival of the state-owned enterprises.

References