

The Depletion of State Assets in Mainland China

Ricky Tung

Research Fellow
Institute of International Relations
National Chengchi University

In the course of the reform of state-owned enterprises, large quantities of state assets have been lost as a result of the failure to solve questions concerning property rights. To overcome this problem, a decision was made at the Third Plenum of the Chinese Communist Party's (CCP's) Fourteenth Central Committee in November 1993 to set up a modernized enterprise system based on reform of the system of property rights. However, the pace of the reform has been reduced because state property has been divided up by some interest groups in the process. This article examines the reasons for the losses of state assets, the main channels through which they are being lost, and the impact of these losses. The conclusion drawn is that in the short or medium term, the Beijing government is unlikely to come up with any effective measures to prevent the continued losses of state assets.

Keywords: state assets, state-owned enterprises, property rights system, enterprise reform

* * *

A number of measures for the reform of state-owned enterprises have been adopted in mainland China in the course of the past decade. These include granting greater autonomy to enterprises, replacing the handing over of profits with tax payments, and the introduction of a contract system. These reforms, however, have not been as successful as expected. State-owned enterprises continue to perform much worse than firms in the nonstate sector, and one important side-effect of the reforms has been the serious drain on state assets. If this develops unchecked, state-owned firms will soon lose their leading role in the economy and social stability will be affected. At the Third Plenum of the Chinese Communist Party's (CCP's) Fourteenth Central Committee held on November 11-14, 1993, a decision was made to reform the system of property rights in the process of

modernizing enterprise management. The purpose of this measure was to ensure that state assets retain their value or even appreciate.

This article examines the reasons for the drain on state assets, how they have been transferred to other hands, the impact of this problem, and the preventive measures the regime has adopted.

The Depletion of State Assets

Pan Yue, deputy director of the National Administration of State Property, has defined this problem as the loss of property owned by the state and the profits accruing from that property as a result of violations of laws, regulations, or administrative rules by units in charge of the property.¹ In mainland China, state property falls into five main categories. The first is property the state has acquired by law, including that legally confiscated from “bureaucratic capitalists” and “the enemy”; urban land, mines, the country’s territorial waters, rivers, forests, and uncultivated mountain land; compulsorily purchased capitalist industrial and commercial assets; land requisitioned by the state; and other confiscated property and fines. The second category consists of capital invested by the state in state-owned enterprises, joint ventures, and shareholding enterprises and the profits accruing from such investments. Funds allocated to administrative units and institutions and the profits accruing make up the third category, donations made by Chinese or foreign nationals and foreign organizations or governments make up the fourth, and the fifth category consists of property for which the ownership rights are unclear.²

What should also be considered a part of state assets is intellectual property, the importance of which is increasing daily. Therefore, state assets may either be in the form of material objects—such as the movable and immovable property of state-owned enterprises and state administrative organizations and institutions—or something that is judged only by its value—such as financial assets and intellectual property.

What, then, is the total value of mainland China’s state assets? In 1950, it was estimated at approximately 20 billion *yuan*; by the

¹*Keji ribao* (Science and Technology Daily) (Beijing), February 17, 1995, 5.

²*Wen Wei Po* (Hong Kong), February 13, 1995, A3.

end of 1992, it had increased to 3,069.7 billion *yuan*,³ and the figure recorded at the end of 1993 was 3,049 billion *yuan*. About 74.5 percent of this state property yields a profit.⁴ By comparison, the state assets of the Republic of China on Taiwan were worth NT\$2,713.4 billion (about 825.2 billion *yuan*) in 1993, although the state-owned sector of the economy is much smaller in Taiwan than on the mainland, especially since the recent privatization drive.⁵

One would expect mainland China to have a formidable amount of state assets, but actually over the years, many of these assets have passed into other hands, and the central government did not become aware of the seriousness of the problem until as recently as three years ago.

Under the centralized planning system of the pre-1979 period, governments at all levels allocated property in kind, rather than cash, to units or individuals. During that time, enterprise earnings and how they could be spent were strictly regulated. Income was either used for specific purposes or handed over to government finance departments according to regulations. As a result, property in kind could not be transferred or traded as it had no corresponding financial value. Under such a system, there should have been no question of state assets falling into the hands of individuals or nonstate organizations, and as a result losses of state assets were negligible in this period.

Policy mistakes have been one important reason for the depletion of state assets. The most notable example was the losses caused by the massive switch to oil-fired boilers in mainland China's factories in the 1970s, when new oil fields were discovered, and the subsequent return to coal-fired boilers a few years later when the authorities realized that oil reserves were limited. This policy turnaround caused losses to the state of at least 4 or 5 billion *yuan*.⁶ By 1990, state assets stood at only 1.65 trillion *yuan*, although the state had invested over 4 trillion *yuan* in fixed assets.⁷

³Ibid., April 16, 1994, A3.

⁴See note 2 above.

⁵Directorate General of Budget, Accounting and Statistics, Executive Yuan, *Zhonghua minguo tongji nianjian: Minguo bashisan nian* (Statistical yearbook of the Republic of China: 1994) (Taipei: Cheng Chung Book Company, September 1994), 278.

⁶Zhang Renlei and Cheng Haiyan, "The Black Hole in Our National Economy," *Qiyejia* (Entrepreneurs) (Wuhan), 1991, no. 2:9.

⁷Yuan Zhigang, "Some Thoughts on the Depletion of State Assets," *Jingji yanjiu* (Economic Research) (Beijing), 1995, no. 4:38.

Since enterprise reform was introduced in urban areas in 1985, ownership has been separated from management rights. However, the government's lack of attention to the problem of property rights has resulted in an enormous amount of state property being embezzled by individuals and organizations. In the seven years from 1985 to 1992, a total of 500 billion *yuan* worth of state property was lost, 220 billion *yuan* of which was lost by state-owned industrial enterprises.⁸

The outflow of state assets grew more serious after 1993, when state-owned enterprises began issuing shares as a part of the market-oriented reforms. This may also be attributed to the failure to solve questions concerning property rights and to the financial disorder in society. At present, about 70 billion *yuan* worth of state assets are being lost each year.⁹ A check on 104,000 state-owned enterprises in 1994 revealed that their losses and debts totalled about 443.8 billion *yuan*. But without an effective capital market it is impossible to gauge the value of these losses accurately.

Reasons for the Losses

The first reason for the losses of state assets is the government's failure to clarify property rights. Enterprise reform has concentrated on devolving autonomy and material advantages to enterprises and making them responsible for their own profits and losses. Questions concerning property rights have not been touched upon. Although state assets are nominally owned by the whole people, no one really cares how their value can be retained and how they can be made to appreciate. Theorists are still debating which bodies should hold state property in the state's name. Many government departments have sought the right to do so but this question has yet to be settled by law. In 1988, the program of the National Administration of State Property stated that the right to hold property in the name of the state belonged to that body. However, in a notice issued by the State Council in 1990 on strengthening the administration of state property, the Finance Ministry was also specified as having the right to exercise ownership over state property. In 1992, in the "Regulations on the Transformation of the Management Mechanism of

⁸*Keji ribao*, January 21, 1994, 2.

⁹*Lianhe bao* (United Daily News) (Taipei), June 21, 1995, 10.

Industrial Enterprises Owned by the Whole People," the State Council was stipulated as the organization exercising ownership power over state property.¹⁰

This failure to clarify which body is in charge of state assets has meant that control over state property has gradually slipped out of the government's hands. Managers and other employees of state enterprises have begun to take control of state property for personal gain.¹¹ For example, some have used enterprise investment funds to build offices and dormitories, or to cover other expenses.

A second reason for the losses is abuse of power by officials. In the process of transition from a planned economy to the so-called socialist market economy, many kinds of ownership other than public ownership have emerged in mainland China, and state assets are gradually coming to be administered in the form of capital rather than material objects. To ensure that the new system is effective, mainland China will have to replace personal rule with the rule of law. This will be a long process, and it is inevitable that there will be a great deal of confusion in society along the way. Some administrative personnel (especially those in the industrial, commercial, taxation, foreign trade, judicial, urban administration, and public security departments of local governments, and those working in subdistrict offices) and enterprise management personnel (such as managers, factory heads, and Party secretaries) may take advantage of this confusion to abuse their power for personal gain. In mainland China, this kind of activity is known as the "economy of officialdom" (*guanchang jingji*).¹²

The third reason is the lack of a property market. According to one set of admittedly incomplete statistics, there were 174 organizations in charge of property rights transactions in 1994 (among which 14 operated at provincial level, 104 at district level, and 56 at county level). Only a small minority are actually engaged in property transactions, and the others are merely former property regulation centers or enterprise annexation agents.¹³ The property market can only work when stocks and stock rights can be exchanged in the

¹⁰Gao Shangquan, "The Three Practical Questions to Be Solved in Order to Further Reform the Property Rights System," *Gaige* (Reform) (Beijing), 1995, no. 1:14.

¹¹Yuan, "Some Thoughts on the Depletion of State Assets," 39.

¹²Liu Hongbo, "The Economy of Officialdom," *Keji ribao*, January 6 1995, 6.

¹³Zhu Zhigang and Ni Jixiang, "A Study of Transactions of State-owned Enterprises," *Jingji yanjiu*, 1994, no. 10:45.

market, and when property rights and management rights can be transferred openly. At present, stocks of state-owned enterprises cannot be exchanged on the market.

Since the sources of capital, ownership rights, and administrative responsibility for state assets are all unclear, and there is no open market through which the real value of state assets can be ascertained, cases of abuse of power for personal gain are inevitable. With no objective market price, people contracting to manage state-owned enterprises or those leasing or purchasing state assets can always force the price down.

The fourth reason for the losses is that the government has neglected to take proper care of state assets. Although it is stipulated in the Decision on Some Issues Concerning the Establishment of a Socialist Market Economic Structure, passed at the Third Plenum of the CCP's Fourteenth Central Committee, that state property should be owned by the state, supervised by governments at various levels, and managed by enterprises, the actual situation is that it is not clear which individual or organization has the real power to hold state property in the name of the state. There are still disputes over whether the State Council or the Standing Committee of the National People's Congress (NPC) should have that right, though theorists seem to have reached a consensus that state property should be held by the State Council under the authorization of the NPC. While the state has ultimate ownership, the rights of various departments, organizations, or individuals concerned should also be recognized. There is also a consensus that administration committees should be established at central, provincial, and prefectural levels to take care of state property, and that the management of state property should be put in the hands of state-owned enterprise groups, shareholding companies, and investment companies.¹⁴

Despite the existence of the National Administration of State Property, and the publication of a notice in 1990 concerning strengthening the administration of state property, state assets are still not controlled effectively. At present, the main task of the National Administration of State Property is to keep inventories of state assets, and the assets themselves are actually taken care of by administrative

¹⁴“A Study of the Modern System of Property Rights of State-owned Enterprises,” *Caijing yanjiu* (Study of Finance and Economics) (Shanghai), 1994, no. 11:7-8.

organizations at various levels.¹⁵ In the absence of strict supervision, factory directors or managers tend to make decisions to their own advantage or to the advantage of their relatives and at the expense of the state when transferring or reorganizing the property rights of state-owned enterprises.

The fifth reason is inadequate legislation. The Law on State Property has yet to be finalized, and for the time being, the administration of state assets is governed by five sets of regulations: the Administrative Measures for the Evaluation of State Property; the Regulations on the Supervision and Administration of the Assets of State Enterprises; the Detailed Rules on the Registration and Administration of State Property; the Basic Administration System for the State Assets of Central Government Departments; and the Administrative Measures for the State Assets of Administrative Organizations. Instead of relying on the law, the National Administration of State Property has sought to prevent losses of state assets by uncovering cases of embezzlement. In one case that was exposed last year, a wholesale market in Taiyuan, Shanxi Province, reorganized itself into a shareholding cooperative without authorization and distributed some of its property to individuals. In another case in Guiyang, Guizhou Province, the local Xinhua Bookstore used its real estate to form a joint venture before carrying out a proper inventory of its property.¹⁶ Such cases are the result of the general lack of respect for the law in mainland China and the habit among bureaucrats of shielding each other. In addition to malpractice of this kind, organizations which hold property in the state's name or which manage state property sometimes collaborate with one another for their own profit.¹⁷

There are still other reasons why state assets have been depleted in recent years. For example, in order to prevent further unemployment, banks continue to offer loans to state-owned enterprises already in default, thus incurring bad debts of approximately 800 billion

¹⁵Yu Tianyi, "In the Process of Promoting the Shareholding System, Attention Should Be Paid to Preventing Losses of State Property," *Jingji daoyin* (Economic Guide) (Beijing), 1995, no. 1:14.

¹⁶*Zhonggong guangbo jiyao* (A Summary of Broadcasts of Mainland Radio) (Taipei), June 19, 1995, 15.

¹⁷Zhang Jianshen, "On the Reasons for the Depletion of Invisible State Assets and the Measures That Should Be Adopted to Guard against Its Continuance," *Xibei daxue xuebao* (Journal of Northwest University) (Xi'an) 25, no. 1 (February 1995): 76.

yuan.¹⁸ In another example, the prices of public services and the basic means of production have been deliberately kept below cost price in order to control inflation.

Channels through Which State Assets Have Been Depleted

There are many channels through which state assets have passed into private hands. The first is through joint ventures or other forms of cooperation with foreign investors. In order to attract more foreign investment, some local officials are willing to sell or rent land to foreign investors at very low prices. Moreover, negotiated prices rather than competitive bidding are the rule in such transactions. In Shenzhen, for example, of the 101 pieces of land rented out in the first half of 1992, only one was subject to competitive bidding. In 1988-89, the average negotiated price for land was 108 *yuan* per square meter, compared to 1,213 *yuan* per square meter for land purchased or let through competitive bidding, and 2,528 *yuan* at auction.¹⁹ Obviously, the state is getting a bad deal by allowing land prices to be negotiated in this way. When state-owned enterprises form joint ventures with foreign businesses, the Chinese partners usually either fail to have their assets properly valued or they underestimate the value. It is estimated that approximately 90 percent of Chinese enterprises have failed to value their assets before forming joint ventures. In 1992, about ten thousand state-owned enterprises had their applications to form Chinese-foreign joint ventures approved. Only 2,900 of them bothered to have their assets valued at all, and most of these were undervalued by an estimated 75 percent. From this we may estimate that the enterprises that failed to value their assets at all actually suffered losses of 64.7 billion *yuan*.²⁰ It should be noted that none of the valuations included the value of trademarks, business reputation, patents, management rights, or production licenses. In contrast, the foreign partners often overestimate the value of the equipment, technology, management expertise, and services they contribute, and the joint venture is often required to

¹⁸ *Zhonggong guangbo jiyao*, March 8, 1995, 10.

¹⁹ Yu Tianxin and Jia Kang, "Questions Concerning the Decrease in the Amount of State-owned Urban Land," *Caizheng* (Finance) (Beijing), 1994, no. 12:47.

²⁰ Wang Baoxi, "How State Assets Are Depleted," *Zhongguo gongye jingji yanjiu* (Study of China's Industrial Economy) (Beijing), 1994, no. 5:22.

pay high prices for raw materials and parts and high interest on loans from the overseas parent company.

State assets have also been lost through the transformation of state-owned enterprises into joint stock companies. When valuing their assets in preparation for issuing shares, most state-owned enterprises fail to include the value of such invisible assets as land-use rights and business reputation. Also, the price of stock varies depending on who is buying it. In one case in Chengdu, Sichuan Province, individuals were charged 1.15 *yuan* per share while corporations had to pay 3.5 *yuan*.²¹ Dividends and bonuses also vary. In Fuxin City, Liaoning Province, for example, shareholders of state-owned enterprises received no dividends or bonuses.²² In many places, state-owned enterprises have been allowed to repay losses incurred before the implementation of the shareholding system by issuing shares to the state. However, these state shares yield only capital and interest; they do not yield any dividends.²³ In other places, the dividends paid on state shares are lower than those on shares issued to individuals. For example, in the period 1988-92, one enterprise in Wuhan declared dividends of 11.5 to 13.7 percent per annum for state shares, 17 to 17.5 percent for individual shares, and only 2 percent for shares held by its own staff.²⁴ In some cases, stocks are issued at below the premium price. For example, in Chengdu, shares of state-owned enterprises appreciated by only 29 percent, compared to the nationwide average appreciation rate of 54 percent.²⁵

In order to earn more funds and provide employment opportunities for their employees' dependents, government departments have tended to establish their own collective economic entities, and these have managed to siphon off substantial quantities of state assets. For example, some have secured the use of state property free of charge: by 1991, 10 billion *yuan* worth of property of state-owned enterprises was being used by such entities without any payment changing hands. In 1995, the value of off-the-book fixed assets

²¹Ibid., 24.

²²"How State Assets Have Drained Away," *Jingji ribao* (Economic Daily) (Beijing), December 11, 1994, 5.

²³Miao Helin, "A Caution to 'Five Empty Shells' in Building a Modern Enterprise System," *Jiangnan luntan* (Jiangnan Tribune) (Wuhan), 1994, no. 7:77.

²⁴Yu, "In the Process of Promoting the Shareholding System," 14.

²⁵Ibid., 26.

reached 14.67 billion *yuan*.²⁶ One collective enterprise in Fuxin City, Liaoning, was found to be utilizing 31.88 million *yuan* worth of state property, and it owed 3.46 million *yuan* in utilization fees.²⁷ Some collective entities have sold the machinery and equipment they have obtained to make up their losses. Others procure scarce commodities from state departments at low prices and then sell them at a profit.

Many administrative units have used state-owned land, buildings, and equipment to engage in profit-making activities, and have even diverted funds earmarked for subsidizing agriculture or for poor relief. According to one report, in 1992 an estimated 19.7 billion *yuan* worth of state property was used in this way.²⁸ In most cases, the rent for the use of such property was very low, and sometimes no rent was paid at all. In order to facilitate the activities of such money-making entities, some units draw on their extrabudgetary funds, often failing to charge interest or to demand repayment. Some of these economic entities do not submit honest reports of their costs and expenditures, and the administrative units that spawned them sometimes have to pay for these expenditures.²⁹

Some enterprises try to avoid paying back loans from the state by declaring themselves bankrupt. In March 1995 it was reported that the outstanding loans of state-owned enterprises totalled 2 trillion *yuan*, with an average liability ratio of 70 percent.³⁰ To avoid repayment, quite a few of these firms have declared themselves bankrupt.³¹ In mainland China, firms have to settle the wages of their employees before they can declare bankruptcy, so many poorly managed enterprises embezzle state property by submitting fraudulent claims for wages and staff living expenses.³² To dodge creditors, state-owned enterprises have been known to transfer capital and equipment to subsidiaries or to use it to establish a new company.³³ In one example, a wholesale business in Northeast China is reported to have used 95

²⁶Wang Hengfeng, "The Losses of State Assets Are Horrifying," *Jing bao* (The Mirror) (Hong Kong), 1995, no. 5:46.

²⁷See note 22 above.

²⁸Wang, "The Losses of State Assets Are Horrifying," 47.

²⁹Wang, "How State Assets Are Depleted," 25.

³⁰*Zhonggong guangbo jiyao*, March 12, 1995, 3.

³¹Yi Cui and Ding Ying, "Pay Attention to the Handling of Bankruptcy," *Keji ribao*, June 2, 1995, 6.

³²See note 22 above.

³³*Keji ribao*, February 17, 1995, 5.

percent of its capital, 22.17 million *yuan*, and equipment to establish a new company before declaring itself bankrupt.³⁴

Property and land-use rights transactions are another channel through which state assets have passed into private hands. The land market in mainland China is still in its infancy, and about 90 percent of land used by enterprises and individuals is subject to administrative allocation, rather than changing hands on the market. Many units and individuals have illegally sold the rights to the land allocated to them. There are an estimated 500,000 black market land transactions each year, which have resulted in losses to the state of over 20 billion *yuan*.³⁵ Even when land is transferred through legal channels, the official price is much lower than the market price. In Beihai City, Guangxi, for example, the official price is about 100,000 *yuan* per *mu*, while the market price ranges from seven to ten times that amount.³⁶ Many administrative organizations and enterprises have made money by selling the land allotted to them, and the state loses at least 10 billion *yuan* this way each year.³⁷ Some public housing has been sold at below cost price. In one such case, in Hengyang City, Hunan Province, houses that cost approximately 950 *yuan* per square meter to build were sold at 120 *yuan* per square meter at the end of June 1993, while the market price of private housing was 1,200 *yuan* per square meter.³⁸ Administrative units or enterprises have also made unfair profits by transferring mines and forests under their control.

Mainland Chinese state assets abroad are also inadequately supervised. For example, it was only recently reported that a unit was established to supervise the country's investments in Hong Kong, which total over US\$10 billion. Laws governing state assets overseas are only just being drafted,³⁹ and this situation has provided the personnel in charge of such assets with many opportunities for embezzlement.

Claims for depreciation of assets and for the cost of technological renovation are often falsified. Some state-owned enterprises set the

³⁴Dongfang Yan, "It Is Not Easy to Cope with Bankruptcy," *ibid.*, June 2, 1995, 2.

³⁵See note 19 above.

³⁶Wang, "How State Assets Are Depleted," 26.

³⁷Wang, "The Losses of State Assets Are Horrifying," 47.

³⁸Wang "How State Assets Are Depleted," 26.

³⁹*Sirzg Tao Daily* (Hong Kong), February 10, 1995, A4.

depreciation rate very low or simply do not claim depreciation, and some do not include the cost of technical renovation in their fixed assets, thus overestimating their economic performance.⁴⁰

Applications for reimbursement of expenses are another method used by officials to get their hands on state funds. According to a report delivered to the Secretariat of the CCP Central Committee by the Ministry of Supervision on May 21, 1993, provincial-level officials claimed 120 billion *yuan* in entertainment expenses in 1992.⁴¹ Although this figure dropped to 87.5 billion *yuan* in 1993, a total of 100 billion *yuan* in public funds was spent by staff of government departments and state-owned enterprises on foreign travel.⁴² Besides this, government officials tend to use public funds to pay for their personal telephone bills,⁴³ to buy items such as cigarette lighters or concert tickets, or to pay their children's tuition fees.

State funds or revenues that should be handed over to the state are often deposited in private accounts rather than in the accounts of the administrative units or enterprises concerned. The assets deposited in these "private exchequers" are obtained in many different ways, including by issuing false invoices and receipts;⁴⁴ by offering products or raw materials to related or subordinate units at low prices or offering them labor or technological services in exchange for private gain; by embezzling income from transactions in stocks, bonds, or other investment items; by falsifying accounts for engineering projects; and by collecting sales commissions. In an example of this last practice, hospitals on the mainland generate an estimated 5.6 billion *yuan* in extra income each year by charging commissions and selling false drugs. This amount exceeds the national medical tax which totals 4.9 billion *yuan* each year.⁴⁵ Commissions collected by all professions are estimated to be worth 50 billion *yuan* each year.⁴⁶

⁴⁰See note 22 above.

⁴¹Liang Ming, "The Stomach of the Party Eats 100 Billion *Yuan* of Public Funds Each Year," *Cheng Ming* (Contending) (Hong Kong), 1993, no. 7:33.

⁴²*Zhongguo shibao* (China Times) (Taipei), October 23, 1994, 2.

⁴³Zhang Guoyun, "When Will the Embezzlement of Public Property by Enterprises and Individuals Be Stopped?" *Keji ribao*, December 2, 1994, 8.

⁴⁴Peng Hong, "'Small Exchequers' Disarmed Not Killed," *Keji ribao*, June 9, 1995, 5.

⁴⁵Ma Shiwei, Zhang Jinghui, and Zhao Jinhe, "Unhealthy Trends in the Purchase and Sale of Pharmaceuticals: Who Benefits? Who Suffers?" *Liaowang zhouban* (Outlook Weekly) (Beijing), 1993, no. 13:48.

⁴⁶Wang Yanlong, "On the Disorderly Depletion of State Financial Resources and How It Should Be Dealt with," *Zhongguo jingji wenti* (China's Economic Problems) (Xiamen), 1995, no. 2:38.

Tax evasion and failure to pay tax bills constitutes another important drain on state assets. Sample surveys indicate that about 50 percent of all state-owned enterprises, 60-70 percent of township enterprises, 80-90 percent of the self-employed, and 95 percent of individual citizens have evaded taxes to the tune of 100 billion *yuan* each year.⁴⁷ With enterprises registering debts of 600 billion *yuan* in November 1994⁴⁸ and 400 billion *yuan* in the first quarter of 1995,⁴⁹ many firms have no funds available to pay power, water, telephone, and wage bills,⁵⁰ let alone taxes.

Cases have come to light in which the income and funds of a state-owned enterprise have been deposited in the accounts of the firm's finance, accounting, or sales personnel. By doing this, the enterprise can escape supervision by the bank, and the individuals concerned can help themselves to the interest on the account.⁵¹ Cadres and administrative staff of state-owned enterprises, especially those in charge of purchasing, supply, and marketing, have long been accustomed to embezzling public funds. One investigation of thirty state-owned and collective enterprises in Junyang County, Hunan, revealed that as much as 1.79 million *yuan* had been embezzled up to the end of June 1992, accounting for 37.3 percent of the enterprises' circulating funds. Most of the culprits had been helping themselves over a period of more than six months, and some for as long as ten years.⁵²

The invisible assets of state-owned enterprises often disappear. Employees transfer technology developed by state-owned firms to private or township enterprises for which they work in their spare time, and some even use the technology to start up their own companies. A state-owned chemical plant in Jilin City, for example, invested a great deal of time and human and material resources to develop a certain advanced production technique. Although this was profitable at first, the firm ran into debt after it found itself competing with private firms started by its own employees who had

⁴⁷Ibid., 37.

⁴⁸*Xin bao* (Hong Kong Economic Journal), March 1, 1995, 23.

⁴⁹Ibid., May 3, 1995, 21.

⁵⁰*People's Daily* (Domestic edition, Beijing), December 24, 1994, 5.

⁵¹Chen Guangjin, "Public Funds Deceitfully Transferred, Ranking Officials Urged Not to Treat This Question Lightly," *Sing Tao Daily*, January 16, 1995, A4.

⁵²Huang Qunli and Chen Rongli, "Nibbling from Inside," *Jingji ribao*, February 27, 1993, 2.

filched the technology for their own use.⁵³ There is no law against such practice in mainland China at present.

These are some of the main reasons for the depletion of state assets in recent years. Of course, there are other reasons, including policy mistakes and improper management.⁵⁴

Impact of the Loss of State Assets

One important result of the steady drain of state assets is that it has exacerbated the government's financial problems. Some local and state-owned enterprises have withheld funds that should be delivered to the state treasury and used them to create so-called extrabudgetary income. In 1994, income in that category amounted to more than 400 billion *yuan*, and it is estimated to have exceeded 500 billion *yuan* in 1995,⁵⁵ almost equal to total state revenue. This practice of withholding funds is the cause of the decline in the ratio of government revenue to gross domestic product (GDP) to 11.8 percent in 1994 (compared to 18 percent in Hong Kong) and the ratio of central government revenue to GDP to 5.1 percent (compared to 5.6 percent in Yugoslavia just before its collapse).⁵⁶ This situation has greatly weakened the central government's ability to exercise overall control over the economy and decide capital distribution. Also, the government is short of funds for large-scale infrastructure projects, technology development, education, and for supporting development in the backward midwest of the country.

The large-scale transfer of public assets into private hands is one important cause of inflation. Whether the public funds are embezzled by individuals or collective units, the inevitable result is an increase in consumption in society, thereby leading to higher inflation. Money embezzled by administrative staff of state-owned units accounts for about one-third of their income. In some places, the funds they obtain illegally exceed their official salaries. In spite of their losses, state-owned enterprises have maintained wage scales only slightly inferior to those of the much more profitable nonstate

⁵³Li Xuebin, "The Strategy of Protecting Intellectual Property Rights in the Modern Enterprise System," *Keji ribao*, June 3, 1995, 4.

⁵⁴For example, state-owned units in Liaoning served as guarantors for loans totalling about 100 million *yuan* and caused a loss of 50 million *yuan*.

⁵⁵Li Zhengping, "Why the Deficit Is Increasing," *Sing Tao Daily*, April 22, 1995, A8.

⁵⁶*Ibid.*, June 17, 1995, A5.

sector. In the period 1990-93, although the production rate of state-owned enterprises increased by only 8 percent, the wages of their employees increased by 15 percent. In the first half of 1994, wages increased by 30 percent,⁵⁷ a most remarkable increase rate for mainland China. Mainly as a result of this increase, the inflation rate soared to 21.7 percent that year.

Cadres with public money to spend on private pleasures have encouraged the growth of vices such as gambling and prostitution in mainland China.⁵⁸ Nightclubs and dancehalls catering to corrupt officials and managers have appeared even in the most poverty-stricken areas.

With state assets being siphoned off into the pockets of government officials and ordinary members of the public being forced to pay higher taxes, dissatisfaction with the CCP regime has mounted and social stability is under threat. The depletion of state assets has brought more and more state-owned enterprises to the brink of bankruptcy. It is estimated that by the year 2000, many enterprises will be bankrupt and the number of the unemployed will have risen to 18 million.⁵⁹ This will have a serious impact on social stability.

The depletion of state assets will also slow down the pace of reform. The importance of the state-owned sector has continued to dwindle over the past few years, while the nonstate sector has grown rapidly. Despite the fact that they hold 75 percent of mainland China's fixed industrial assets,⁶⁰ state-owned industrial enterprises account for only 43.8 percent of the total industrial output.⁶¹ Conservative elements within the regime maintain that the transfer of the property rights of state-owned enterprises to individuals and the work force and the system of transferring stock to corporations and foreign businessmen are disguised forms of privatization. In a January 1995 article, Yuan Mu, a leading conservative, strongly advocated the continuation of the public ownership system and criticized the practice of converting state-owned enterprises at county level into nonpublic

⁵⁷Li Xiaoxi, "Structural Inflation in the Course of Transition," *Jingji yanjiu*, 1994, no. 10:30.

⁵⁸Lu Ming, Bo Yue, and Xiong Dafang, "Small Exchequers Have Become More Serious," *Jing bao*, 1995, no. 5:48.

⁵⁹*Lianhe bao*, July 1, 1995, 10.

⁶⁰*Zhongguo jingji xinwen* (China's Economic News) (Beijing), 1995, no. 3:17.

⁶¹*Zhonggong guangbo jiyao*, April 1, 1995, 39.

entities.⁶² The reformists have decided to slow the pace of property rights reform, although they believe that such reforms will help to halt the outflow of state assets. They argue that it is this depletion of assets, rather than the reforms, that will really result in privatization.⁶³ In 1995, the focus of reform was shifted to carrying out a thorough inventory of state assets. Meanwhile, experiments to create modernized enterprises have been conducted in eighteen cities, and this scheme is to be promoted throughout mainland China from 1997 to 2000.⁶⁴

Conclusion

Losses of state assets occur in the process of production, exchange, distribution, and consumption, and the Beijing regime faces an arduous task in halting the outflow. The first thing that needs to be done is to clear up questions concerning property rights. It is also necessary to develop a proper capital market and establish a society ruled by law. None of these things can be achieved in five or even ten years. Indeed, the only solution is to introduce private ownership and a market economy.

There are, however, a number of stopgap measures that can be adopted to prevent the outflow of state assets and the corruption it causes. The first thing that should be done is to carry out a thorough valuation of state assets by qualified personnel. Although there are as many as 162 units authorized by the National Administration of State Property to carry out property valuation,⁶⁵ they are staffed mostly by retired or part-time accounting or auditing personnel. A system of nationwide examinations for valuers should be introduced as soon as possible.

Another solution would be to have loss-making state-owned enterprises sell off some of their assets and lay off staff, so they can repay some of their debts. An investigation of 124,000 state-owned enterprises in August 1994 indicated that the liability rate was 75.1 percent. If net losses and purchases on credit, which to-

⁶²Yuan Mu, "A Basic Understanding of Some Questions Concerning the Reform of the State-owned Enterprises," *People's Daily* (Domestic edition), January 28, 1995, 10.

⁶³Fan Hengshan, "Walk out of the Area of Misunderstanding, Further the Reform of State-owned Enterprises," *Liaowang zhoukan*, 1995, no. 16:25.

⁶⁴*Jingji daobao* (Economic Reporter) (Hong Kong), 1995, no. 22:3.

⁶⁵*Gongshang shibao* (Industrial and Commercial Times) (Shanghai), March 24, 1995, 2.

talled over 400 billion *yuan*, had been included, the liability rate could have reached 83.3 percent.⁶⁶ Continued indebtedness may leave half of all state-owned enterprises with no assets at all.

A third solution would be to establish state property administration bureaus at provincial, city, and county levels, although the problem here is that it is not clear which body has ultimate responsibility for state property. There should also be units authorized by the government to manage state property and an adequate evaluation system to oversee the output of state-owned enterprises.

Political reform involving the introduction of a multiparty system would enhance supervision of state assets. This kind of reform appears to be a long way off in mainland China, however. The CCP still clings to its one-party dictatorship and the people's congresses and local committees of the Chinese People's Political Consultative Conference have been unable to play a supervisory role. At present, individuals are asked to supervise state property. For example, the Finance Ministry encourages public tip-offs over the telephone.⁶⁷ This is a small step toward public supervision of the government and its results remain to be seen.

⁶⁶Dai Xianglong, "Gradually Readjust the Ratio Between Assets and Liabilities of State-owned Enterprises," *Zhongguo gaige* (China Reform) (Beijing), 1995, no. 5:10.

⁶⁷See note 44 above.