CHINA'S STATE ENTERPRISE REFORM:
THE LATEST DEVELOPMENT

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Executive Summary

1. After a prolonged period of stagnation, state-owned enterprise (SOE) reform is once again moving ahead. Since 2006, a complex mixture of new rules and institutions has been adopted. The new measures will make China's state-owned sector more **financialised,** but also more **politicised.**

2. Every publicly owned system has to trade-off among incentives, oversight and assigning of multiple objectives. China's recent SOE reforms appear to be designed to achieve better incentives, stronger oversight and greater emphasis on developmental and political objectives, "an impossible trinity".

3. A milestone of the current corporate governance reform is the corporatisation of the 'apex' central SOEs, only 22 years after the Company Law was passed.

4. Almost as important is the division of SOEs into "public service" and "commercial" types, with the commercial type further sub-divided into those in "fully competitive" and "not-fully-competitive" markets. Fully competitive commercial enterprises are cued up for further reforms.

5. "Mixed ownership" firms will expand. While China has had mixed ownership since it began listing SOE subsidiaries on the stock market in the late 1990s, "fully competitive commercial" firms will have greater freedom to restructure along with private investors.

6. There will be no privatisation—state shares cannot be sold outright to private parties—but firms can grow by attracting private investment, even if this brings the state's share down below 50%. SOEs can also take stakes in previously private firms, expanding the scale and complexity of mixed ownership.

7. SOEs will be "financialised". SOE equity (10%) will be gradually transferred to the social security fund and oversight of SOEs transferred from the State-owned Assets Supervision and Administration Commission of the State Council to the State

Capital Investment and Operations (SCIO) Corporations with a clearer financial governance structure. Notably, mixed ownership is a form of financialisation.

8. Communist Party oversight is being greatly strengthened with the embedding of the Party in the corporate governance system. The enterprise Party secretary should normally chair the Board of Directors (BoD) and important enterprise decisions must first be discussed by the enterprise Party committee before turning them over to the management and BoD.

9. The public ownership function will gradually be taken over by SCIOs which will manage existing government ownership stakes and invest in new firms and new "Industrial Guidance Funds".

10. Chinese SOEs are thus expected to pursue multiple objectives, and this is tightly linked to broader trends in Chinese economic policy today. SOEs are to play a bigger role in industrial policy, the Belt and Road initiative and environmental improvement.

11. While some measures will improve incentives and efficiency in some SOEs, the increased oversight, divided among government and Party actors, and linked to increasingly diverse and politicised objectives could result in opposite effects. The net impact of these contrasting measures is difficult to predict.