# Chinese Corporate Capitalism in Comparative Context

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*Capitalism will be much more robust if it's not a monopoly of the West, but flourishes in societies with different cultures, religions, histories, and political systems.*[1]

## Introduction

The "Beijing Consensus" is a broad label applied to China's approach to economic governance, one in which the state plays a pervasive role and (at least in theory) markets serve the higher interests of national development. As such, the Beijing Consensus may be an alternative term for "state capitalism," a concept that has attracted considerable attention due to China's spectacular economic growth. These labels suggest something unique about China's developmental path. However, the Chinese economy shares with all other developed and developing economies a key feature: *corporate* capitalism. That is, the central actors in the Chinese economy are legal entities enjoying separate and perpetual existence, governed ostensibly by a board of directors and appointed managers, with ownership interests represented by shares held by the providers of capital.[2]

Using this fundamental commonality as a starting point, this essay looks behind the "Beijing Consensus" or "state capitalism" by briefly examining Chinese corporate capitalism in comparative context, with particular reference to other countries that have influenced China's approach to economic organization: Japan, South Korea, and Singapore. It seeks to distill the common and distinctive features of China's approach to corporate capitalism, explain their existence in the context of the Chinese political economy, and examine the feasibility and normative appeal of replicating Chinese corporate capitalism in other developing countries. Simply put, the essay asks what is unique about Chinese corporate capitalism and whether those unique elements can or should be transplanted elsewhere.

To briefly state the conclusions, the essay argues that the organizational foundation of Chinese state capitalism is not particularly unique, because *state* capitalism is a species of *corporate* capitalism.

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[*] Parker Professor of Comparative Corporate Law; Fuyo Professor of Japanese Law, Columbia Law School. I received a wealth of stimulating comments on this essay – more than I could fully respond to in such a short piece. Any shortcomings in the essay remain in spite of the extremely helpful input I received from Jinhua Cheng, Ron Gilson, Jed Kroncke, Li-Wen Lin, Tomo Marukawa, Daniel Puchniak, Wentong Zheng, and participants at a workshop on Scaling the State at Columbia University and the Beijing Consensus workshop at National University of Singapore. Portions of this essay draw upon Lin & Milhaupt (2013).

[1] Coase & Wang (2013).

[2] Of course, form does not necessarily mean function. Does a Chinese corporation – particularly a state-owned enterprise (SOE) – perform the same function as, for example, a U.S., German or Japanese corporation in credibly constraining the behavior of its participants, particularly its majority shareholder? Or is the corporate form in China – again, especially as adopted by an SOE, simply a convenient means of organizing and accounting for the state's assets? A more direct version of this question is whether the corporate form meaningful constrains the state from dictating the decisions of the SOE's managers and maximizing the state's (rather than the firm's) interests. As I suggest but do not fully substantiate here, I believe the corporate form in China is important both for its form and its function, though it probably constrains the behavior of its controlling shareholder more weakly than its counterparts in more institutionally robust, less state-centric economies. I am grateful to Ron Gilson for highlighting the importance of these questions in understanding the role of the corporation in Chinese capitalism.

The corporate form – with its inherent characteristics – lends a familiar structure even to a form of economic organization that looks novel (or sinister) to outside observers. Yet the essay argues that Chinese corporate capitalism does have some distinctive features, namely "party centrality" and "institutional bridging" (concepts elaborated below), although they have rough functional parallels in the comparison countries. These distinctive features are mostly a matter of degree, yet they suggest shifting emphasis in the Chinese case from "state" capitalism to "party-state" capitalism. This is not a "model" system: even if the Chinese approach could be replicated elsewhere, at least in functional terms, the benefits of doing so are likely to be outweighed by the governance weaknesses and other costs engendered by this particular configuration of corporate capitalism. Nonetheless, undertaking a comparative analysis of Chinese corporate capitalism is useful because it appears to reinforce several important lessons about economic development that have emerged from the collective experience of other countries.

Part I of the essay highlights a basic but generally overlooked point in the burgeoning field of taxonomic classification of capitalism: all of the forms of economic organization being classified are species of *corporate capitalism*. This simple observation can be leveraged to clarify what "state capitalism" is and the dimensions along which it can be distinguished from other forms of corporate capitalism. Part II surveys the key features of Chinese state capitalism by mining the prosaic *corporate* underpinnings of this system of economic organization. It also places the Chinese system in comparative context, to highlight shared and distinctive traits vis-à-vis other systems. Part III draws some possible lessons from the analysis for law and development literature.

## I Varieties of Capitalism – The Prequel

Comparative scholarship on capitalist systems is a growth industry. *Liberal Market Economy/Coordinated Market Economy… Shareholder Capitalism/Stakeholder Capitalism/Crony Capitalism … Market Capitalism/State Capitalism … Washington Consensus/Beijing Consensus…* The taxonomy grows more extensive with each financial crisis and the appearance of each newly emerging economy on the world stage.

The object of this essay is not to quarrel with the expanding taxonomies or to question the insights generated by debates about the efficiency, welfare effects, or sustainability of different approaches to economic organization. Rather, the aim is to explore the implications of an observation so obvious that it is generally overlooked: labels aside, virtually all viable economies today, regardless of size, stage of development, or political orientation – including most relevantly for this volume, China – take the corporate form as the central organizing device in the economy.[3] The bulk of economic activities in the global capitalist system are conducted by or through the corporate form – a legal device enabled by the state, featuring separate and full legal personality; perpetual existence; limited liability

[3] I am mindful that other organizational forms, particularly the trust and the partnership, are also widely used in and important to global capitalism, see Pistor (2014), but the corporate form would dominate a census of the most significant global economic actors. For example, a search of the suffixes (Corp, Inc. Partnership, Trust, etc.) of the names of the 3,281 firms listed on the New York Stock Exchange turns up only one partnership and twenty-three LLCs. Of the 2426 firms listed on the London Stock Exchange, only about 200 have non-corporate suffixes; No firm in the CSI 300 (a capitalization-weighted index of firms listed on the Shanghai and Shenzhen exchanges) has a non-corporate suffix. Company List (NYSE), NASDAQ, http://www.nasdaq.com/screening/companies-by-name.aspx?letter=0&exchange=nyse&render=download (last visited April 24, 2015); List of all Companies, LONDON STOCK EXCHANGE (last visited March 31, 2015), http://www.londonstockexchange.com/statistics/companies-and-issuers/companies-and-issuers.htm; CSI 300, CHINA SECURITIES INDEX, http://www.csindex.com.cn/sseportal/ps/zhs/hqjt/csi/000300cons.xls (last visited April 24, 2015).

for investors and managers; delegated management under a board of directors; and free transferability of shares.

The first point of the essay is simply that Chinese "state capitalism" is a species of *corporate* capitalism. (See Figure 1) This claim actually follows directly from the uncontroversial starting point for Hansmann and Kraakmann's (2001) controversial article, *The End of History for Corporate Law*. That work is widely cited and often criticized for its muscular normative claim that intellectual convergence on the "shareholder-oriented model of the corporate form," working hand-in-hand with market forces, will erode differences among national corporate governance regimes and lead to convergence in economic systems. Generating virtually no comment, however, is the article's foundational descriptive claim: the *corporate* form has triumphed worldwide as a means of organizing capitalist economic activity.[4] Precisely why this is so need not detain us here, but I will return to this point later in the essay.[5]

**Figure 1 Taxonomy**

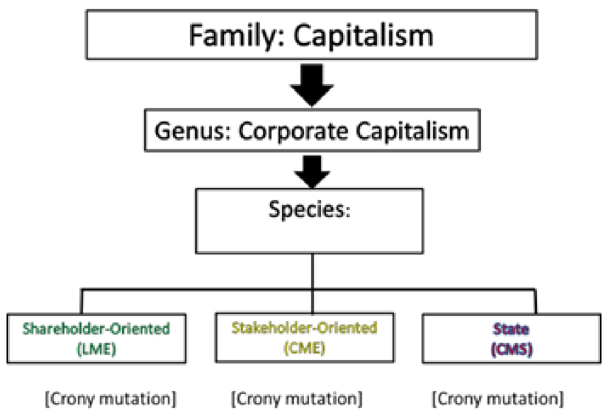


Figure 1 is a graphical depiction of two foundational points that animate the essay: First, reality assuages doubts that China's state-oriented economic system is not capitalist because capitalism "is a form of economic activity dominated by *private* firms" and profits are the "key test of a capitalistic enterprise."[6] This view of capitalism is ahistorical and perhaps U.S.-centric: at an earlier state of economic and political development in the United States, the UK and elsewhere, corporations were typically chartered as a grant of authority from the state to perform a specific purpose providing public benefits, such as to operate a railroad. Thus, the earliest corporations were public-private hybrids,

[4] As one gauge of its usefulness, even North Korea, hardly a paragon of capitalism, uses the corporate form for the state's engagement with the economy, though tellingly, the state does not allow private entrepreneurs access to this powerful form of organization. See (Park 2009).

[5] Much has been written about this subject. Suffice it to say that the combination of corporate attributes enumerated in the text has proven to be an extremely efficient device for pooling and investing capital while limiting and diversifying risk; while its drawbacks, mostly pertaining to externalization of risk and amplification of agency costs, are basically (though imperfectly) manageable through insurance and regulation (for risk) and governance and incentive mechanisms (for agency costs). The global policy choice implicit in the corporation's ubiquity is that the benefits to society from extensive use of the corporate form outweigh the costs. Of course, it is also possible that path dependence rather than economic efficiency explains the widespread adoption of the corporate form in China (and many other later-developing countries). That is, the corporate form may have been attractive to Chinese economic strategists, not because of its inherent superiority over possible alternatives, but because it had already been widely adopted elsewhere.

[6] See Meyer (2011, p.8) (emphasis added).

serving as an organizational bridge between the state and the body public (Barkan 2013). Stated differently, "[h]istorically, corporations, like states, have been used to achieve ends of government" (Ibid, p. 5). The British East India Company is a dramatic early example of this phenomenon. The conceptualization of the corporation as private property, and capitalism as a project of national development by means of the promotion of private property, emerged later and is most closely associated with American schools of thought. China's economic system, in which capital, labor, goods and services are allocated (largely) in markets for profit (see Lardy 2014), is properly classified as capitalism, and since it is organized around the corporate form (as detailed below), it is properly classified as a species of corporate capitalism.[7]

A second foundational point, implicit from the figure, is that, due to its reliance on the corporate form, Chinese capitalism shares more traits in common with other species of capitalism than is commonly acknowledged, particularly by those who see in state capitalism something novel and potentially menacing.[8] Corporations everywhere have the same basic attributes, although the prominence of a given attribute in the overall constellation (for example, the priority assigned to ownership interests held by the providers of capital), may vary from country to country. This constellation of attributes offers the same basic advantages to everyone who utilizes the corporate form, and generates the same fundamental risks (insolvency being a key risk to shareholders and employees, and externalization of "public bads" such as financial contagion or environmental disasters being a key risk to society). Thus, the corporate form, by its very nature, powerfully channels the ways in which capitalism operates in every country. (As an important aside, the figure also depicts the reality that all species of corporate capitalism are susceptible to mutation into crony capitalism – whereby the operation or regulation of markets for capital, labor or goods and services is corrupted by illicit relationships; this pathology is not uniquely identified with any particular species, although of course the propensity and severity of the pathology may vary significantly across species.[9])

Advancing these basic claims about the prosaic features of Chinese state capitalism will contribute to the essay's chief ambition: clarifying the ways in which the *state* species of *corporate* capitalism as practiced in China differs from the other species. I will argue that some of the differences are internal to the corporate form; others are external. The internal differences pertain to the way in which standard corporate structures and operations, such as the working of the board of directors, have been supplemented or altered by Chinese Communist Party organs. The external differences pertain to how the Chinese corporation is viewed and treated *as an actor* in the political economy, including the comparatively limited degree of autonomy it enjoys from the state, and the comparatively broad scope of objectives it may pursue, which extend beyond the corporation's first degree stakeholders (shareholders, managers, and employees) to encompass "the citizens," "national interests," or "government/party policy." By developing these points, I hope the essay will provide a novel perspective on Chinese state capitalism (or, if the reader prefers, the organizational DNA of the "Beijing Consensus").

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[7] Some commenters on an earlier draft suggested that all capitalism is properly classified as corporate, such that there is no meaningful taxonomic distinction between what I have labeled the family (capitalism) and the species (corporate capitalism). I think it is conceptually helpful to consider other genera of capitalism that do not rely on the corporate form, such as family capitalism, Islamic capitalism using the *wafq* and *mudaraba* organizational forms, and many other forms of proto-capitalism that emerged prior to the Industrial Revolution. See Neal & Williamson (2014). In any event, taxonomical precision for its own sake is not the objective of this essay. Devoting attention to disambiguation highlights the important fact that all major "varieties of capitalism" today, including "state capitalism," are organized around a common organizational form. This development was not preordained and is testament to the power and adaptability of the corporate form.

[8] See, e.g. Bremmer (2010).

[9] Recent research suggests that rent seeking tends to be sector specific and appears not to be closely correlated with the strength of national institutions or varieties of capitalism. See Economist (2014a, p. 13); Economist (2014b, p. 57).

## II Chinese Corporate Capitalism

This section sketches key attributes of Chinese corporate capitalism as they have evolved in the reform era. Relevant features of other species of corporate capitalism, such as those of Japan, Korea and Singapore, are discussed for purposes of comparison. Several conjectures about the principal developmental consequences of Chinese corporate capitalism are then briefly discussed.

### A. Attributes

*Corporatization of the economy*: Although Chinese "state capitalism" is not entirely synonymous with state-owned enterprises (SOEs), they are certainly of one of its principal mechanisms (Liebman & Milhaupt 2015). Consistent with the argument that the corporate form is the basic building block of all market-oriented economies, a crucial early move in China's reform process was "corporatization" of the economy.[10] This entailed transformation of the production arms of state agencies into joint stock corporations.[11] Through this process, production functions were formally separated from public regulatory functions and cloaked in an organizational form that is both prevalent and readily understood around the world. Shares were issued to the corporation's governmental owners (in theory, on behalf of the ultimate owners, the Chinese people). Ostensibly, at least, the newly formed corporations were imbued with the standard governance organs of boards of directors and shareholders meetings. A Corporate Law was enacted, very much with SOEs in mind (see Clarke 2003), to provide the norms of governance for and allocation of rights among the corporate stakeholders. Some of the best state assets were packaged into corporations which issued shares to minority public investors on Chinese and global capital markets. These listings, which would not have been possible without the transformation of state assets into an organizational form recognizable to international investors, provided capital, managerial expertise, and global visibility to the firms. The local Chinese governments were also integrally involved in the corporatization process. As Cheng (2011, p. 185) states, "local legislative experiments [with incorporation rules, public offerings and capital requirements] had significantly contributed to institutionalizing corporations and other business organizations in transitional China," greatly reducing the costs of developing the national corporate economy.

*Corporate Groups*: Chinese SOEs, particularly at the national level, are organized into business groups comprised of numerous separate corporations arranged in hierarchical order. The decision to organize the firms into groups was a strategy based on observations of economic development elsewhere, particularly the high growth economies of East Asia. Governmental encouragement of business group formation to foster the growth of national champions has been a common strategy around the developing world, followed by a wide range of governments pursuing diverse macro-economic policies. Such countries include late-nineteenth century Japan under the Meiji oligarchs, South Korea under military strongman Park Chung Hee in the early 1970s, and Chile under Pinochet in the late 1970s and 1980s. The Chinese leadership's decision to organize its corporatized SOEs into groups probably reflected the same motivations for business group formation found in these and other

[10] Several commenters pointed out that non-corporate entities, such as the TVE, were actually the first actors in China's movement toward a market-oriented economy. This is accurate, but the shift away from these entities in favor of corporatization reinforces the claim that the corporation proved to be a superior organizational form – perhaps not only economically but also from the standpoint of retaining the Communist Party's political control over the economy.

[11] Clarke (2015) persuasively argues that the corporatization project was driven by several misconceptions about what ailed China's state sector, and consequently about the potential for corporatization to remedy those ills. Nonetheless, there can be little doubt that corporatization was a necessary, if not sufficient, step in China's economic reform process.

developing countries, including filling institutional voids in weak rule-of-law environments, internalizing capital markets, marshaling scarce resources (including both monetary capital and entrepreneurial human capital), and reducing the transaction costs of administering economic policy.

Business groups around the world have typically originated with family-founded enterprises. In China, group formation took place along a very different path, because there were no home-grown entrepreneurs in the immediate post-Mao era to serve as partners of government in the development project. Chinese economic strategists were intrigued by Japanese *keiretsu* and Korean *chaebol* business groups as models for promoting growth, but there was no shortcut available for replicating such groups in China. The SOE business groups in existence today are the result of a long process of experimentation with collaborative forms of production. Business alliances based on contract were tried first as a means of coordinating production and resource allocation, but they proved ineffective. In the next phase, in place of contracts, policy makers used organizational structures based on shareholding to link firms along the production chain and across complementary industries. Eventually, the business group concept was enshrined in regulations that permitted registration as a business group if it had certain required components and layers of entities. Registration as a business group afforded certain benefits, including most importantly eligibility to establish a finance company to handle intra-group lending, underwriting, cash management and other financial functions that are otherwise prohibited on an inter-company level (Lin & Milhaupt 2013).

In contrast to the main postwar Japanese *keiretsu* and Korean *chaebol* corporate groups, Chinese business groups are vertically integrated firms focused on a particular industry or sector, not diversified groups involved in a range of industries. Again in contrast to *keiretsu* and *chaebol* structures, shareholding is hierarchical: firms higher in the structure, particularly the parent company in which strategic and managerial decisionmaking are concentrated, own downstream subsidiaries, but there is very little upstream or cross ownership among group firms. Governance concerns – both corporate and political – are the primary reason for top-down ownership patterns. Parent companies have little use for upstream share ownership; top-down stock holdings reflect and reinforce the hierarchical structure of the groups. Moreover, given pervasive involvement of the Chinese Communist Party in group firms and other forms of party-state monitoring (discussed in the next subsection), the risk sharing and monitoring functions of cross ownership performed in other countries, most prominently Japan, are not complementary to Chinese corporate group structures.

At least ostensibly, the controlling shareholder atop this giant web of corporate groups is an agency formed in 2003 called SASAC, the State-Owned Assets Supervision and Administration Commission. SASAC's formal role is to serve as the investor in the approximately 100 massive corporate groups under its supervision, on behalf of the Chinese state and people. But SASAC is a peculiar entity: part investor, part regulator and consolidated compliance department, part conduit for Party influence and government policy dissemination. While it formally "supervises" the central SOEs, it often must yield to the instructions of other ministries or to the prerogatives of the most politically well-connected SOEs themselves.

*Holding Company Structure*: Arguably the closest model for Chinese SOE reform and corporate structure, particularly following the formation of SASAC at the national level, can be found in Singapore. As in China, Singapore's development strategy has relied heavily on what are known in that country as government linked companies (GLCs). Shares of Singapore's GLCs are owned by a holding company, Temasek, which was formed in 1974 as a wholly owned subsidiary of the Ministry of Finance. Temasek took control of a number of companies that had been held by other government bodies, completing a separation of regulatory authority and enterprise ownership. These companies had already been formed into groups by the government, also in a manner reminiscent of the Korean *chaebol*, in order to foster national champions. Each of the companies in Temasek's portfolio is the head of its own corporate group with numerous affiliated companies (Kirkpatrick 2014). According to Tan et al. (2014), 37 percent of Singapore's total stock market capitalization is comprised of companies in which the government is the controlling shareholder.

The basic structural similarities between Temasek and SASAC reflect similarities in the two government's motivations for adopting a state capitalist approach. Singapore's GLC-centered strategy, developed in the late 1950s and 1960s, grew out of "the ruling PAP [People's Action Party] government's perceived need to support the transformation of the Singapore economy," based on the conclusion that "control over key domestic markets and institutions [was] the most effective way to … meet the main planning objectives of absorbing surplus labour and promoting economic growth" (Tan et al. 2014, p. 9). Moreover, in both countries, there is a strong link between economic success and political legitimacy. Particularly given the strength of these parallels and the success of Singapore's approach, it is not surprising that the Chinese Communist Party, along with many other analysts concerned with Chinese SOE reform, have continued to look toward Temasek as a model (see, e.g. World Bank 2012; Boston Consulting Group & China Development Research Foundation 2014).[12]

But China adopted the Singapore holding company structure only selectively: SASAC is far from a copy of Temasek,[13] which has two closely related defining features that signal its role as a true holding company: (1) an unambiguously commercial orientation articulated in public documents and verified by its performance; and (2) a high degree of independence from direct political influence vis-à-vis the companies in its portfolio.[14] *Commercial orientation*: Temasek refers to itself as an active investor and steward of state assets. This claim is backed up by its performance. It has achieved a total shareholder return of 16 percent compounded annually since its inception in 1974. Temasek uses various devices to increase its financial discipline, such as issuing bonds (rated AAA by S&P) and making detailed annual disclosures of its performance and portfolio. Market benchmarks are used to structure incentive compensation for managers. *Independence*: Temasek's board of directors is highly professional and non-political in its orientation. The thirteen-member board (expanded from ten in January 2015) is presently comprised of a majority of independent private-sector directors, three of whom are non-Singapore nationals, including Robert Zoellick, former president of the World Bank. There is no ministerial representative on the board. To be sure, Temasek is not entirely free from political influence. Its current CEO is linked by marriage to modern Singapore's founding father Lee Kwan Yew. Members of the boards of both Temasek and its portfolio companies have historically been drawn from civil service and the military. Even today, the managers of Temasek's portfolio firms are chosen from the "ruling strata of Singapore. As a result, there [is] widespread agreement about the developmental objectives of the government, which has remained in the hands of the Peoples Action Party since independence" (Kirkpatrick 2014, p. 10). As the quote suggests, the boards of directors of the GLCs themselves are not completely independent of the government in its role as controlling shareholder. But there is something of a "best of both worlds" quality to this arrangement: the presence of a controlling shareholder with

[12] Although the World Bank (2013, p. 119) does not explicitly reference Temasek, it argues: "It is critical … that SASAC confine itself to policy making and oversight, leaving asset management to the SAMCs [state asset management companies that the World Bank recommends establishing to represent the government as shareholder and professionally manage the assets in financial markets]." The SAMCs contemplated by the World Bank are basically a description of Temasek.

[13] See, e.g., Rutkowski (2014).

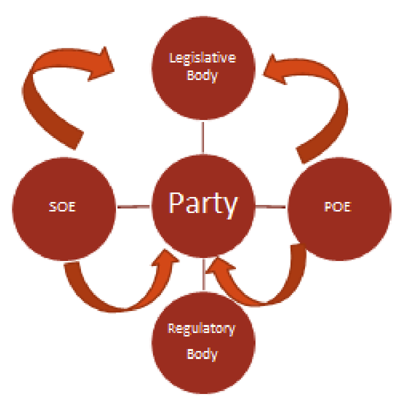
[14] The information in this paragraph is drawn largely from Temasek (2014).

incentives to monitor the portfolio firms, but one whose overriding motive is maximizing the firms' economic outcomes, not extracting wealth from minority shareholders.

*Party Centrality*: Thus far, we have described a Chinese system that has parallels with group-oriented corporate capitalism elsewhere. But ending the description of Chinese corporate capitalism here would be highly incomplete, because the more-or-less universally recognizable features described thus far are supplemented (and perhaps functionally displaced) by some distinctive non-corporate features. The first I will call "Party centrality." This refers to the use of party organs and party structures to act as a shadow monitor of corporate actors as well as a personnel office for high-level managerial appointments in Chinese SOEs (and large private firms as well). In an extension of the Leninist approach to state organization, the Chinese Communist Party shadows *corporate* organizational structures in the same way that the Party shadows governmental structures. Every large firm in China has a party committee responsible for high-level managerial appointments and promotions.[15] These committees also appear to play an anti-corruption/information and reporting role very roughly analogous to that of internal control structures in western firms. The managerial elite of the SOEs (and again, many large POEs), are overwhelmingly Party members,[16] and they simultaneously serve roles in Party and government bodies. The Party thus permeates Chinese corporate capitalism. Indeed, when focusing on large Chinese corporations, it may be more instructive to understand them as *Party Linked Companies* (PLCs) rather than analyzing them within the standard state-owned versus privately owned (SOE-POE) dichotomy.

*Institutional Bridging:* Party centrality is closely associated with a second distinctive characteristic of Chinese corporate capitalism, a feature (Lin & Milhaupt 2013) call "institutional bridging." This refers to the way in which the various firms that comprise an SOE business group (as well as many large POEs) are extensively networked to the larger system of industrial organization and governmental authority, all of which are shadowed by the party. In effect, the party is the hub of a complex wheel whose spokes radiate out to business enterprise, banks, governmental organs, and other units of the state such as universities and research institutes. (Figure 2)

**Figure 2**
**Party Centrality and Institutional Bridging**




[15] Large POEs have internal party committees just like SOEs, and their founders and/or controlling shareholders are often linked to party and governmental organs in the same fashion as SOEs managerial elites. Milhaupt & Zheng (2015).

[16] In the national-level SOEs, 99% of the CEOs and 90% of the vice-CEOs are Party members. (Lin 2015).

Although the groups are legally and functionally distinct from each other, complementary groups are linked through joint ventures, strategic alliances, and inter-group equity ownership. The dense networks linking individual components of China's state sector were engineered by various means. Some, like the equity ownership linkages, make use of the corporate form and corporate law. Others are the result of personnel practices of the Party Organization Department and SASAC, in which senior managers are rotated within and among groups. Still others result from distinctive notions of representation in party and governmental organs, in which a number of seats are assigned to business leaders. These institutional bridges link the separate components of Chinese state capitalism into a complementary whole.

Since all of the parent companies of the national SOE groups are ultimately controlled, at least as a matter of formal law, by SASAC, the Chinese group structure as a whole outwardly resembles the structure of a single Korean *chaebol*. That is, while individual corporate groups in China are vertically integrated along the production line and lack cross-shareholding among member firms, the groups under SASAC supervision, taken as a whole, resemble a giant diversified conglomerate under a single controlling shareholder, with extensive cross-ownership and other forms of collaboration, including extensive personnel rotation, among member firms. But the analogy should not be stretched too far: the SOEs themselves are quite heterogeneous, including in the degree to which they answer to SASAC as opposed to other regulators and political masters. And as Milhaupt & Zheng (2015) point out, there are many reasons to be skeptical of "the state's" ability to actually *control* state-owned enterprises in China.

How might the structures just described have contributed to Chinese economic development? As Gilson & Milhaupt (2011) have noted, the alliances formed by the party-state with firms offering growth potential and the role of the party-state in funding, incentivizing and monitoring the managers of such firms is reminiscent of a private equity partnership: high-powered incentives for growth are provided by the party structure of rotations and job movement across the boundaries of business and politics. Moreover, as noted in Lin & Milhaupt (2013), the integration of a large swath of the entrepreneurial population into the formal structures of party-state governance calls to mind Mancur Olson's concept of an "encompassing coalition" – a group representing a large enough segment of the population that it has incentives to grow the pie, as opposed to a "distributional coalition" representing a narrow segment of society. By creating dense networks of managerial elites migrating across the spheres of politics, public governance and business in China, an encompassing coalition has been created with control over developmental policy formulation and implementation. The Chinese firm is but one component of party-centered economic and public governance – *Party-State, Inc.* if you will. But again, the structure in operation is not one of simple top-down control, but rather loose linkages of firms (many of which are operating in competitive markets) and other state organs managed by elites enmeshed in, and responding to incentives flowing from, China's political system.

### B. Assessing the "Corporate-ness" of Chinese Capitalism

A short thematic essay is not the place for an extended analysis of Chinese corporate law and governance in the context of the country's economic development. My aim in this subsection is simply to highlight the potential importance of the corporation to Chinese capitalism and to raise some questions about how the universal characteristics of the corporate form may be affected by Chinese state capitalism.

China's developmental experience is highly suggestive of the importance of the corporate form to economic development. The corporatization process was central to the hydraulics of industrial organization in the reform era: separating (incompletely and problematically, to be sure) the regulatory from the operational aspects of enterprise in the corporatization process was a crucial first step in the development of a functional state sector. The corporate form has proven to be extraordinarily useful in providing the Chinese party-state with a scalable, adaptable, and relatively anonymous[17] vehicle for investment and economic activity. It provided a template for the structure of the state sector and its scaling to globally important proportions. Its inherent features have provided an "off-the-rack" organizational device no less serviceable to the strategists of Party-State Inc. than to entrepreneurs in other economies.[18] The corporate form has also provided a template for the emergence of private entrepreneurship and a pathway for the possible retreat of the Party from direct involvement in business enterprise, should it ever chose to do so. (Note that the current SOE reform plan promoted by the Xi Jinping administration draws upon a standard corporate turnaround strategy -- obtaining capital injections from investors capable of improving managerial and financial performance – but falls short of true privatization.)

Yet throughout the reform period, Chinese economic strategists have chosen selectively from among the menu of corporate attributes, making extensive use of the corporation's hierarchical governance structure and separate legal existence in building networks of firms responsive to influence from party-state organs, and leveraging the power of the state in its ostensible role as controlling shareholder. At the same time, the universal, supreme decision making and oversight organ provided by the corporate form – the board of directors – has often been sidelined by the Party's own monitoring structures. Here the contrast with Singapore is instructive. Temasek is a professional asset management company in a high quality institutional environment, pursuing commercial objectives, albeit in service of political legitimacy and preservation of national wealth and influence; SASAC is a holding company in form; but functionally it is a vehicle for pursuing two highly conflicting objectives: enhancing the performance and global reach of Chinese SOEs while maintaining the Party's direct influence over, and rent extraction from, important firms in the economy.

Thus, it may be instructive to briefly analyze how the universal attributes of the corporate form have been adapted to, and affected by, the ecology of Chinese capitalism:

*Separate legal personality/limited liability*: One of the principal concerns with SOEs everywhere is that they operate under a "soft budget constraint." That is, their managers do not fear financial failure because the state implicitly guarantees their debts and stands ready to cover deficits that arise in their operation. Under a soft budget constraint, and particularly given the personnel overlaps and rotations between SOE managers and party officials, one might conclude that neither separate legal personality nor limited liability carry the same import in China as in other species of corporate capitalism. However, as noted above, the separate, universally recognizable legal personality of the corporate form played a big role both in the internal re-arrangement of organizational actors during China's reforms and their scaling to global proportions. Limited liability may yet prove to be important, as Chinese growth slows and budget constraints harden.[19]

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[17] Anonymity of the corporate form may be useful to state capitalists in masking the state operating behind the corporation. At the same time, however, this very masking can subject all firms operating out of a state capitalist system, whether closely linked to the state or not, to fears that they have non-commercial motives – a "suspicion tax" of sorts. This was most apparent in the case of two globally successful Chinese telecom firms Huawei and ZTE, which were the subject of a U.S. House of Representatives investigation. Although the House committee found no conclusive evidence that the firms were affiliated with the Chinese state or Communist Party, it recommended that their future investment activity in the United States be blocked because they did not provide information sufficient to conclude that they were *not* linked to the state. In other words, the U.S. politicians placed the burden of proof for demonstrating a 100 per cent commercial orientation on the Chinese firms.

[18] This is particularly the case because, as noted above, China developed its corporate law with SOE reform, and the state as controlling shareholder, very much in mind. See Clarke (2003).

[19] China recently experienced its first bond default by an SOE.

*Delegated management*: As argued above, the board of directors in SOEs is often bypassed by the Party system. Developing functional boards of directors of Chinese SOEs has been a relatively slow process. As long as Communist Party organs continue to parallel and shadow corporate organs in the state sector, and as long as the party-state retains direct influence over SOEs, Chinese corporate governance in the state sector will retain a distinctly shareholder-centric (that is, party-state-centric) bias in tension with the principle of delegated management.

*Transferable shares*: Until recently, China maintained a share classification system that rendered shares of SOEs effectively non-transferrable to non-state organs. Today, while all shares are transferrable as a formal matter and despite "mixed ownership" reforms to encourage more private investment in SOEs, the Chinese government shows no signs of relinquishing control over SOEs in sectors of the economy deemed to be critical. There is effectively no market for corporate control in China. On the other hand, creation of stock markets in the early 1990s was a major institutional step in China's developmental process, and it seems safe to conclude that liquidity facilitated by transferability of shares has been a major factor in foreign portfolio investments in China's state sector, including the banking sector.

*Investor ownership*: SOEs, like all corporations, feature ownership by the providers of one factor of production – capital. But the state is unlike any other shareholder; and the Chinese party-state is unlike any other state. The distinctiveness of the state as shareholder is a defining feature of state capitalism, and the distinctiveness of the party-state sets Chinese state capitalism apart from that practiced in other countries (see Wu 2015), at least as a matter of degree.

As this brief survey suggests, most universal corporate attributes are affected by state capitalism, including perhaps in particular China's subspecies of state capitalism. Thus, it is fair to ask whether the system should still be classified as a species of corporate capitalism. I believe the answer is affirmative. The basic corporate attributes are affected by and adapted to every species of corporate capitalism around the world. For example, few would question whether Japan evinces a species of corporate capitalism, notwithstanding the fact that Japanese managers, at least traditionally, have overwhelmingly placed the interests of employees over those of shareholders.

## III Lessons

### A. *What is "state capitalism" as practiced in China (aka the Beijing Consensus)?*

The discussion thus far suggests that Chinese state capitalism is a species of corporate capitalism (1) featuring political involvement in, or at times displacement of, the standard corporate governance organs of the board of directors, professional managers, and shareholders meetings (the internal dimension); and (2) in which the corporation is treated by the state, or political actors closely identified with the state, as an integral part of the "Capital G" Governance apparatus and not simply as an object of regulation, as it is in (the idealized versions of) other species of corporate capitalism. Thus, its objectives are not limited to serving the interests of its first-degree stakeholders, but also encompass political and policy agendas (the external dimension). As a consequence, in state capitalism the firm is influenced by and influences public governance considerations to a larger extent than in other systems of corporate capitalism, and the unit of maximization is not the individual firm, but state interests as a whole (at least as those interests are defined by Party elites). Distinctiveness along what I have termed the external dimension suggests a potentially key tension between state capitalism other species of corporate capitalism – but it is a tension that at least one other practitioner of state capitalism, Singapore, has managed to resolve, as discussed below.

The most distinctive quality of Chinese corporate capitalism as currently practiced is the degree to which political and managerial interests and incentives have been integrated in the state sector. A high degree of overlap between political and managerial interests may be common in a country's takeoff stage of development. This raises the important question of whether Chinese corporate capitalism in its current *Party-State Inc.* form is transitional or enduring. I believe there are good reasons to think the latter (see below), but I defer extended discussion of this point to future work.

### B. *Should Chinese corporate capitalism be regarded as a "Model," such that its features serve as the basis for a new "Consensus" about how to organize a successful economy? No.*

As just discussed, the Chinese species of corporate capitalism does have several distinctive qualities, both internally and externally. But as argued throughout the essay, Chinese "state" capitalism is not distinctive at its organizational core; the corporate building blocks are familiar to capitalists everywhere.

Even the distinctive aspects of the Chinese system have rough functional analogues in other countries. Close connections between political leadership and groups of favored business elites to transmit economic policy, finance industries deemed critical to national development, and manage competition were also a major facet of South Korea's and Japan's developmental paths, but other countries such as Taiwan and Brazil could also be mentioned. These interactions were institutionalized in Japan in the form of *amakudari* (descent from heaven), a practice in which high-level officials from the most powerful ministries parachuted into the private-sector in mid-career. There they served as an important bridge between the government and the business and financial establishment, forming a network of managerial elites with shared backgrounds and basic values (Colignon & Usui, 2003). Chinese state-business interactions differ from most other examples on account of extensive state ownership of enterprise. But in the context of a developing economy, state- versus private- property ownership, of itself, may be relatively unrevealing of the proximity between corporations and political elites. In weak institutional environments that typify developing economies, the autonomy from governmental authority usually associated with private property ownership is often illusory; governments retain fairly extensive, unspecified residual control rights in all firms, whether state or privately owned, due to a lack of political accountability mechanisms and underdevelopment of institutions to secure private property against state incursions.

Thus, China is distinctive in the *extent* of state ownership of enterprise, the *degree* to which political considerations influence corporate decisions, particularly on managerial appointments, and the *degree* to which the managers of all major firms, regardless of equity ownership, are linked to a political party, particularly one with a monopoly on power. But it is very difficult to make the case that distinctiveness along these dimensions is beneficial to corporate performance and sound institutional development. This conclusion merits more substantiation than I can provide in this short essay. But for evidence of the negative impact of state ownership and political control on firm performance, see Batson (2014); Meyer & Wu (2014). For the deleterious impact of China's SOEs on the legal system, see Zheng, Liebman & Milhaupt (2015).

### C. *Even if the Chinese species of corporate capitalism does not merit exalted status as a "Model" or "Consensus" for developing countries, does it nonetheless provide lessons for other countries seeking to replicate China's successful growth experience, if not the precise means by which it was achieved? Yes.*

Why? Because China's growth story reinforces several basic lessons that emerge from careful analysis of other developmental success stories:

1. *Institutions matter, but political will probably matters more at the takeoff stage*: As elaborated by Gilson & Milhaupt (2011), China's expericne confirms that "economically benevolent dictators" can achieve development even in the absence of strong formal institutions. That is, in the admittedly rare circumstance in which a strong political leader prioritizes national development over personal enrichment, credible commitments to growth can be made even in the absence of strong formal institutions which allow a small-scale, relationship-based economy to be scaled up for linkage to the global economy. Indeed, twentieth-century experience suggests that political will engendering credible commitment to growth is more important to a country's developmental transformation than the pursuit of a particular macro-economic strategy or the quality of its judiciary.

2. *Organizational forms matter*: while history indicates that countries can grow dramatically without strong formal institutions, no country in the last three hundred years has achieved significant development except in reliance upon *corporate* capitalism. In other words, the corporate form is common to all national development stories. For all the discussion about varieties of capitalism and the law-finance connection, a particular legal form – the corporation – is an indispensable component of any functional national economic system, regardless of the legal family to which the country belongs, the left-right dimension of its politics, or the libertarian to authoritarian range of the roots of its political economy. Corporate capitalism has many species because adaptability is one of the key attributes of the corporate form. It serves as a template for businesses ranging from a family operated hardware store in Peoria to global technology behemoth Microsoft. The corporate form also has a chameleon-like ability to take on the characteristics of the political economy in which it operates. Witness the stakeholder orientation of German co-determination firms and the relentless focus on shareholder wealth maximization often found in publicly held U.S. corporations. It is not surprising, then, that the corporate form has also been readily adapted to the Chinese party-state. The corporate form can be shareholder-centric, board centric, employee-centric, or state centric, depending on the institutional setting and political economy in which it is nested.

3. *Incentives matter*: The melding of political objectives and business enterprises in China has worked not only due to the adaptability of the corporate form, but also because corporate values and performance have been fitted into a complementary system for political advancement that generates incentives compatible with economic growth. To be sure, the current incentive structure also engenders rent-seeking on a large scale, and most likely contributes to a host of public "bads," such as environmental degradation and corruption. To date, however, the negative effects of the arrangement have not completely overwhelmed the benefits produced by political will and growth incentives. (But see point 4 below.)

4. *Organizational forms shape institutions in the long run*: Corporations are not simply passive takers of rules and norms; they actively shape the institutional setting in which they operate.[20] National economic histories demonstrate the profound impact of corporations on institutional development. This was true of the transformative period of U.S. economic history in the

[20] As Barkan (2013, p.5) notes: "Once constituted, corporations and states share a range of techniques – from the consensual to the coercive – for establishing order within their institutional structures and across the places and territories in which they operate."

nineteenth century. It also seems true of China in its first thirty years of experience with corporate capitalism – at least those portions of the experience shaped by SOEs (see Zheng, Liebman & Milhaupt 2015).[21]

But here is where the claim to a new China "Model" or "Beijing Consensus" may fall flat. In the long run,[22] the Chinese version of corporate capitalism will likely prove to be unappealing because its distinctive internal dimension – direct political monitoring and selection of corporate actors, particularly by a party with a monopoly on power – is a poor substitute for robust corporate mechanisms of accountability based on law, markets and media scrutiny. This is particularly so because the concomitant, distinctive external dimension of Chinese corporate capitalism – treating the corporation as an integral component of the party-state's governance network – leads to systematic distortion of the regulatory environment for corporate conduct (see Zheng, Liebman & Milhaupt 2015). Without a major retreat of the Party from Chinese corporate capitalism, the country's institutional arrangements are likely to become increasingly statist in their operation, regardless of whether they outwardly converge on global standards. As one commentator concludes, "[e]ven if governance institutions change, the thread of party influence will still run throughout China's economy as members continue to occupy key positions in the party, the government, and business hierarchies – often at the same time." (Hersh 2014, p. 1).

It is of course possible that the Chinese Communist Party will find ways to continue improving the governance and global reach of SOEs while employing their profits to expand social expenditures for Chinese citizens – in other words, to replicate and scale up Singapore's version of state capitalism. As Huat (2015) notes,

> Should China, despite its severe deficit in all measures of democracy, be able to successfully transform [and] institutionalize its state capitalism, then neoliberal capitalism may be said to have met its other – a hegemonic single-party state with a strong state capitalist sector in a developed market economy which is an integral part of global capitalism, where the material life of a majority of its population is progressively improving. This status as the other of neoliberalism is one that the small island nation of Singapore could not claim.

But this sort of transformation would require major reform of the distinctive internal dimension of Chinese corporate capitalism – if not a complete withdrawal of the Party from the internal workings of SOEs, then at least the creation of a professional, arm's length relationship between the party-state in its role as controlling shareholder and the SOEs whose shares it holds for the benefit of the Chinese people.

**Conclusion**

This essay has attempted to understand what is unique about China's approach to economic organization. First, it has argued that Chinese "state" capitalism is a species of corporate capitalism, and

[21] For a fascinating parallel analysis of national-local government institutional dynamics in relation to corporate capitalism in nineteenth century U.S. and reform era China, see Cheng (2011).

[22] I will not hazard a prediction about how long "the long run" is, but China has already been growing at an exceptional rate for a historically unprecedented period of time. Pritchett & Summers (2014, p. 36): "China's experience from 1977 to 2010 already holds the distinction of being the only instance, quite possibly in the history of mankind, but certainly in the data, with a sustained episode of super-rapid (> 6 ppa) growth for more than 32 years." Thus, a reversion to the mean in a time frame measured in years rather than decades seems rather likely. See Pritchett & Summers (2014).

as such, it shares fundamental traits with all other major systems of capitalism. Second, it has argued that Chinese corporate capitalism's distinctive qualities are manifest both internally and externally in relation to the corporate form. These distinctive features, like the distinctive features of every system of corporate capitalism, were cobbled together by trial and error over time and were heavily shaped by the domestic political economy; they did not spring forth fully formed from the minds of party strategists. Satisficing, not optimizing, characterizes China's developmental journey.[23] The not-very-surprising conclusion following from this analysis is that the "Beijing Consensus" is a fancy name for an un-fancy contraption – a successful one to date if measured by GDP growth and the alleviation of poverty – but one whose distinctive features are likely to have deleterious consequences for the long-term global attractiveness of this particular species of corporate capitalism.

China has developed spectacularly over the past three decades. Its success is a function of many factors, including the navigational skills of its economic strategists and the growth focus of its authoritarian leadership. But if a "Consensus" is to be formed around Beijing's developmental miracle, it just might begin with the genius of a legal fiction available to dictators and democrats alike throughout the world – the corporation.

[23] "They [Chinese officials] are satisficing." Senior U.S. official with responsibility for China policy, in telephone discussion with author, regarding China's approach to SOE reform and development of market-oriented economic regulation.

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