

# **The Development of Private Enterprise in the People's Republic of China**

After more than two decades of sustained reform, the economy of the People's Republic of China (PRC) bears scant resemblance to the erratically performing command economy that preceded efforts beginning in 1979 to re-introduce market principles. Twenty plus years of growth at around 9% a year have quadrupled gross domestic product and made the PRC into a trillion (US) dollar economy. To a very large extent, the driving force behind the PRC's spectacular economic gains has been the re-emergence of a dynamic private sector.

Exactly what comprises the "private sector" in the PRC is murky, and a lack of clarity is evident in the data on economic performance provided by the State Statistical Office.<sup>3</sup> What is entirely clear, however, is that the PRC's ability to sustain fast growth and continue to improve the welfare of its people depends overwhelmingly on how effectively the resurgent private sector performs. But, in investigating what policy and other changes would help the private sector to continue to perform well, governments at all levels need to recognize that, no matter how well-meaning they are, changes to laws, regulations, institutions, and policies that stifle entrepreneurship and impede competition will erode the dynamism of the private sector and harm the country's economy.

This report expands earlier work that documents the growth of private enterprise in the PRC, and identifies the policy, institutional, and other constraints that threaten the ability of private firms to thrive. In particular, it builds on the analysis found in an earlier study by the International Finance Corporation (IFC),<sup>4</sup> as well as on a new survey of private enterprises in the PRC conducted for this study by faculty and students of the School of Economics and Management of Tsinghua University (see their report in Annex 2). The study is funded under Technical Assistance Grant No. 3543-PRC "Private Sector Development" (TAR: 33447-01) by the Asian Development Bank (ADB). The main beneficiary of the technical assistance project is the China General Chamber of Commerce (CGCC), also known as the All-China Federation of Industry and Commerce (ACFIC). The objectives of the project are: (i) to assist CGCC in identifying and promoting appropriate policies and conditions for private enterprise development and (ii) to enhance CGCC's business support services.

## **Section 1: Private Enterprise in the People's Republic of China**

Two notable events in 2001 contributed to a significant improvement in the climate for private enterprise in the PRC. The first was the speech by President Jiang Zemin on 1 July that extended membership in the Communist Party of China (CPC) to the owners of private businesses.<sup>5</sup> Of the people interviewed for this study, officials and entrepreneurs alike interpreted this development as an important elevation in the status of the private sector, and one that remains controversial with hardline party members. The second event was the PRC's long-awaited accession to the World Trade Organization (WTO). With accession at hand, senior officials, especially in Beijing,

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<sup>3</sup> See *China Statistical Yearbook*, various editions, as well as Annex 1, which discusses the data available on enterprises according to ownership structure.

<sup>4</sup> See *China's Emerging Private Enterprises: Prospects for the New Century*, IFC (2000).

<sup>5</sup> See the speech made by Jiang Zemin, General Secretary of the Central Committee of the Communist Party of China (CPC), at the Meeting celebrating the Eightieth Anniversary of the Founding of the CPC.

increasingly realized that the PRC soon would be obligated to extend to foreign privately owned ventures rights and privileges that have been denied to domestic private firms. Membership in the WTO will oblige the PRC to revise countless rules and regulations to eliminate distinctions made on the basis of the nature and location of ownership. As one official of the State Economic and Trade Commission (SETC) observed: “The current concern is to level the playing field for all enterprises: domestic, foreign and private.” Nothing is being done specifically to favor private firms, which would be “a recipe for discrimination;” change is designed to improve enterprise performance. “We don’t care about ownership. We care about efficiency and competitive ability.”<sup>6</sup>

That is the only sensible view to take as private activity already comprises the predominant share of the PRC economy, with that share lying somewhere between one-half and two-thirds depending on how narrowly one defines the term “private” (See Annex 1 for a detailed discussion). In its report, the IFC estimated the composition of the PRC economy by ownership in 1998.<sup>7</sup> Based on official statistics and assumptions about ownership shares in seven sectors (agriculture, industry, construction, transport, post and telecommunications, wholesale and retail trade, and others), the IFC study estimates a share of 62% of total gross domestic product (GDP) in the nonstate sector. Of that, twelve percentage points are estimated to be contributed by truly collectively owned enterprises (with another eleven percentage points contributed by firms that are nominally collectively owned, but really are “red hat” firms, owned and managed by a small group—which might have just a single member—of private individuals). In its *2001 White Paper*, the American Chamber of Commerce in the PRC estimates the size of the nonstate sector at two thirds of GDP in 2000.<sup>8</sup>

There is no need to repeat the IFC exercise to infer that in 2002 the share of PRC GDP produced in the nonstate sector exceeds two-thirds, with the share produced by truly private activity comprising comfortably more than half. This inference would follow from a continuation of the trend growth observed through 2000, and the reclassification of firms that either have been sold or otherwise transferred to private owners, or have removed their red hats.

## **How Ownership Classes Contribute to Output and Employment**

The State Statistical Office presents data for seven different classes of enterprise ownership: individual ownership, private ownership, foreign ownership, joint ownership, shareholding corporations, collective ownership, and state ownership.<sup>9</sup> Unfortunately, information is not uniformly available for these classifications for all of the indicators of interest to analysts; frequently, some of the ownership categories are aggregated as “other types of ownership.” Moreover, there are breaks in the series due to changes in composition of the reporting firms and to periodic clean-up of data series (as, for example, in 2000) that show in a single year events that clearly occurred over an unknown number of prior years. As Annex 1 indicates, there can be problems with double counting as well.

Since 1985, the private sector has been the most dynamic source of industrial output growth. As Figure 1.1 illustrates, “private and individual ownership,” together with “other

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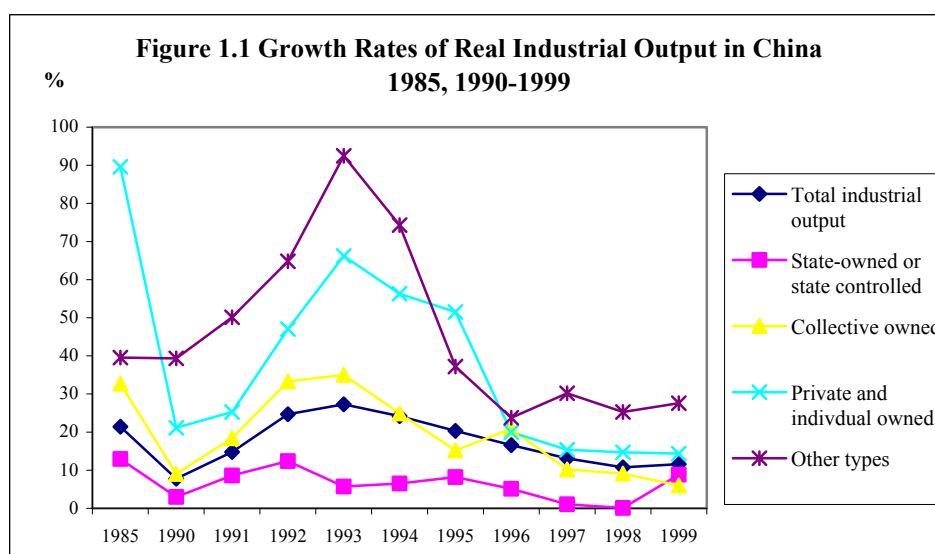
<sup>6</sup> Conversation with official of the SETC, October 25, 2001.

<sup>7</sup> See IFC, *op.cit.* Table 2.3, page 18.

<sup>8</sup> *2001 White Paper: American Business in China* The American Chamber of Commerce, People’s Republic of China 2001. See page 30. The same source estimates that defining the private sector narrowly as comprising *siying qiye* firms (see below) would lower the estimate to about one-sixth of GDP.

<sup>9</sup> There is also an additional, undefined classification: “Other,” which is small enough to be disregarded here.

ownership types,” which mostly comprise foreign-funded firms and shareholding corporations, have comprehensively outpaced the state-owned sector and even the collectively owned town and village enterprises (TVEs) in the past 15 years. The persistent growth differentials have translated into a significant shift in composition of the level of industrial output by ownership types (see Figure A1.a in Annex 1). Until 1990, state-owned and collectively owned firms produced more than 90% of gross industrial output. Since then, the shares being produced by private firms, broadly defined to include foreign and shareholding firms, have risen rapidly, reaching 44% in 1999, when the share of state-owned firms was only 28%, a far cry from the almost two thirds of gross industrial output produced by state-owned firms in 1985.



Notes:

1. “Private and individual owned” include *siying qiye* firms and *getihu*.
2. “Other types” include foreign-funded firms and non-state-controlled shareholding corporations.
3. Since the *China Statistical Yearbook 2001* does not report total industrial output by ownership (it does so only for firms with revenues of 5 million yuan or more), this figure presents growth rates only up to 1999.
4. The gross output data are adjusted using GDP deflators.

Source: *China Statistical Yearbook*, 2000.

The sustained more rapid growth of the private sector strongly suggests that *productivity growth* is also higher in the private sector, and that inference seems all the more likely when one recognizes the evident advantages that foreign-funded firms possess in technology, management practices, and information of all kinds. Table 1.1 presents several indicators, for firms with annual sales exceeding five million yuan<sup>10</sup>, from which we can infer comparative productivity across some ownership types. Unfortunately, Table 1.1 excludes information on private and individual ownership, both of which ownership classes (as Table 1.2 shows) tend to concentrate in industries that typically exhibit higher labor intensity (e.g., such service sectors as retail trade and restaurants). Potential confirmation of the rising competition that small private ventures confront in these sectors might lie in the gradual decline in their very high concentration in trade and food services, combined with their rising presence in manufacturing and social services.

<sup>10</sup> This is one of the areas where the *China Statistical Yearbook* provides less than fully comprehensive data.

**Table 1.1 Selected Indicators for all State-Owned or State-Controlled Firms and Nonstate-Owned Firms with Sales over 5 million yuan in 2000**

Item	National	of which:			
		State-owned State-controlled	Collective	Shareholding corporation	Foreign- funded <sup>1</sup>
<b>Number of enterprises</b> (in billion yuan)	<b>162,885</b>	<b>53,489</b>	<b>37,841</b>	<b>5,086</b>	<b>28,445</b>
Gross industrial output	8,567	4,055	1,191	1,009	2,346
Industrial value-added	2,539	1,378	307	358	609
Total paid-in capital	3,294	2,016	231	376	908
Total assets	12,621	8,401	963	1,493	2,568
Total sales	8415	4,220	1,080	982	2,255
Total profits (in million yuan)	439	241	45	125	128
Assets per firm	77	157	25	294	90
Profits per firm	2.7	4.5	1.2	24.6	4.5
Return on assets (%)	3.5	2.9	4.7	8.4	5.0
Value-added/gross output (%)	29.6	34.0	25.8	35.5	26.0

Note: Foreign-funded firms include those funded by investors from Hong Kong, China; Taipei, China; and Macau.  
Source: *China Statistical Yearbook*, 2001

Another assessment of the potentially superior productivity of firms under private ownership is found in a study by Li and Rozelle (2000),<sup>11</sup> who analyze the impact of a transfer to private ownership on the performance of a sample of rural collectives, or those collective firms that have taken off their red hats. They find that financial indicators—the ratios of revenue to employment, revenue to capital, profit to employment, and profit to capital—serve as partial measurements of efficiency, and that such data provide insufficient evidence for superior efficiency of privatized firms. However, by explicitly modeling the production functions and correcting for selection bias, they demonstrate that firms that have been privately owned for 2 years or more produce from the same inputs 7% more output on average than rural collectives. They also find that, although privatization brings productivity gains after 2 years, its immediate effect on productivity may be negative. In the year in which they are privatized the firms' performance can deteriorate by 11–17%. In all, one can surmise that there are credible reasons to associate higher productivity with private firms, but the evidence is inconclusive with more research needed to establish the facts.

<sup>11</sup> Li, Hongbin and Scott Rozelle (2000) "Saving or Stripping Rural Industry: An Analysis of Privatization and Efficiency in China," *Journal of Agricultural Economics*, v23, n3, pp. 241-53.

**Table 1.2 Shares of Total Urban Private Employment in the PRC, by Industry**

Year	Share of Total (%)						
	Total (millions)	Trade and Restaurant	Manufac- turing	Social Services	Transport, Storage, Post and Telecom	Construction	Others
1985	4.5	72	11	9	5	1	1
1990	6.7	64	14	14	5	1	2
1991	7.6	64	17	10	6	1	1
1992	8.4	66	15	11	6	1	2
1993	11.2	64	15	11	6	1	4
1994	15.6	63	17	11	6	1	2
1995	20.4	62	17	12	5	1	3
1996	23.3	61	17	12	6	1	3
1997	26.7	61	17	12	6	1	3
1998	32.3	59	17	12	6	1	4
1999	34.7	58	17	13	6	2	4
2000	34.0	57	19	13	5	2	4

Source: *China Statistical Yearbook*, 2001.

### Individual and Privately Owned Ventures

More comprehensive output and employment data are available on individual businesses and privately owned enterprises that are wholly owned by domestic residents. The predominant form of ownership by frequency is **individual businesses** (*getihu* 个体户). Table 1.3 shows that in 2000 the PRC had almost 26 million such enterprises employing more than 50 million people, impressive figures that nevertheless represent a sharp decline from corresponding figures of almost 32 million enterprises and more than 62 million employees in 1999. The main reason for the decline was an exercise that the State Administration for Industry and Commerce (SAIC) conducted during 2000 to remove data on individual businesses that were no longer in operation. Millions of new small ventures start up each year in the PRC, but just as in other countries many of them fail to prosper. After initial registration, not all of the individual businesses have been monitored closely, hence the need to adjust data in 2000 to reflect events occurring in several earlier years. Officials observed in conversation that some *getihu* successfully make the transition to larger entities that are registered differently, but individual businesses increasingly tend to fail due to the heightened competition they face from larger enterprises, especially in retailing and food outlets where larger “chains” and “supermarkets” are emerging rapidly in all large cities.

Simple arithmetic shows that most of the individual businesses are single person or husband/wife endeavors. But their vitality is astonishing nevertheless; even with the data corrections in 2000; since 1993 the number of such undertakings has increased by more than half, and those employed in them by more than two-thirds.

**Table 1.3 Individual Businesses (*getihu*) Development Since 1993**

Year	Number of Businesses			Employment		
	Number (millions)	Growth Rate (%)	Absolute Increase (millions)	Number (millions)	Growth Rate (%)	Absolute Increase (millions)
1993	17.7			29.4		
1994	21.9	23.8	4.2	37.8	28.5	8.4
1995	25.3	15.6	3.4	46.1	22.2	8.4
1996	27.0	6.9	1.8	50.2	8.7	4.0
1997	28.5	5.4	1.5	54.4	8.5	4.2
1998	31.2	9.4	2.7	61.1	12.4	6.7
1999	31.6	1.3	0.4	62.4	2.1	1.3
2000	25.7	-18.6	-5.9	50.7	-18.8	-11.7
<b>Average</b>		5.5	1.1		5.6	3.0

Notes:

1. The dramatic decline in 2000 is due to the removal of registered but inactive businesses.

2. The average growth rates are computed as the compounded average annual growth rates.

Source: *China Statistical Yearbook*, 1994-2001.

Firms owned by Chinese residents that employ eight or more persons are termed **privately owned (*siying qiye* 私营企业)**, and this is the class of firms that is often meant in official references as the "private sector." Though dwarfed by the absolute number of *getihu*, *siying qiye* firms as a class have expanded much faster since 1993 (Table 1.4), growth that has been sustained throughout the period with no sign of the apparent sharp slowdown in numbers exhibited by *getihu* since the mid-1990s.<sup>12</sup> There were more than 1.7 million privately owned firms by 2000, employing more than 24 million people, with the number of firms and people employed by them growing annually, respectively, at 33% and 31% over 1993–2000.

Together, private firms and individual firms accounted for almost 11% of total national employment in 2000 (more than 16% of urban employment), compared with 5% in 1993 (at 6%)—see Figure 1.2 and its notes. The faster growth of *siying qiye* firms saw their share of total employment in the PRC's narrowly defined private firms rise from a ninth in 1993 to a third in 2000. One can observe, however, that employment by the average *siying qiye* firm is still very low—fewer than 14 workers per enterprise. Given that some of the enterprises are sizeable (see Annex 3), the clear implication is that the vast majority of *siying qiye* firms are also very small. An important issue for policy makers is to foster conditions under which these firms can accelerate their growth and create many more jobs. That is all the more needed as governments push ahead in restructuring the government and enterprise sectors, and the collectives also restructure themselves to compete more effectively.

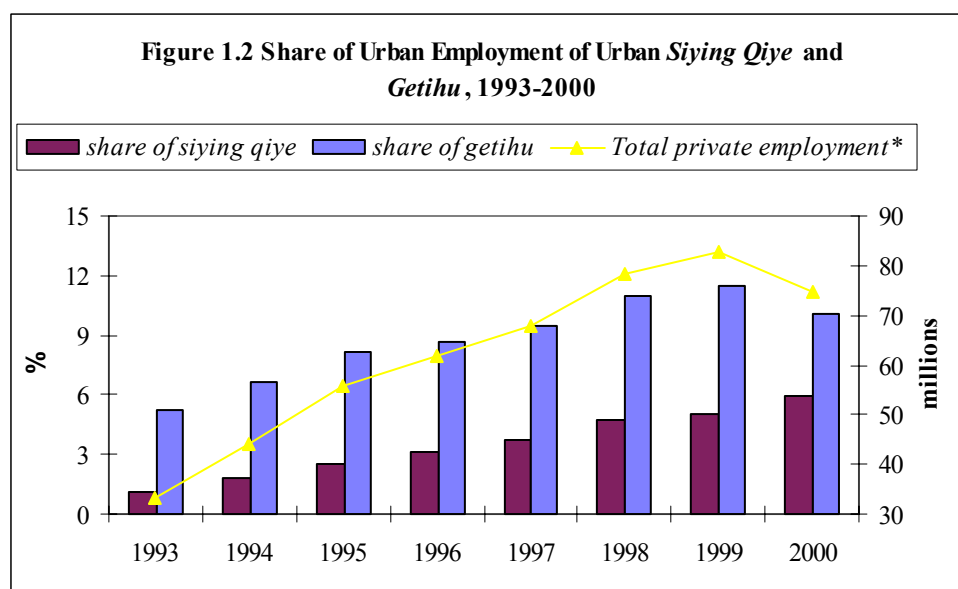
<sup>12</sup> The data make no allowance for reclassification of enterprises as a result of either the conversion of state-owned or collectively owned enterprises to private ownership or the registration of firms as private that might have existed but was unregistered before the constitutional amendment of 1999 that legitimized the key role of the private sector in the "socialist market economy" of the PRC.

**Table 1.4 Privately Owned Enterprises (*Siying Qiye*) Development Since 1993**

Year	Number of Firms			Employment		
	Number (thousands)	Growth Rate (%)	Absolute Increase (thousands)	Number (millions)	Growth Rate (%)	Absolute Increase (millions)
1993	238			3.7		
1994	432	81.4	194	6.5	74.0	2.8
1995	654	51.4	222	9.6	47.4	3.1
1996	819	25.2	165	11.7	22.5	2.2
1997	960	17.2	141	13.5	15.2	1.8
1998	1201	25.1	241	17.1	26.7	3.6
1999	1509	25.6	308	20.2	18.3	3.1
2000	1762	16.8	253	24.1	19.0	3.9
<b>Average</b>		33.1	218		30.7	2.9

Note: The average growth rates are computed as the compounded average annual growth rates.

Source: *China Statistical Yearbook*, 1994-2001.



Notes:

1. The decline in *getihu* employment in 2000 is due to the removal of registered but inactive businesses.
2. Total private employment includes employment by all *siying qiye* and *getihu*; total national employment rose from 664 million in 1993 to 712 million in 2000, at a compounded annual average growth rate of 1%.

Source: *China Statistical Yearbook*, 1994-2001.

That conclusion is supported by the extraordinary growth in employment in the *getihu* and *siying qiye* in combination. From 1993 to 2000, total employment in the PRC increased by 48 million to 712 million, with 37 million of those new jobs being located in urban areas, which saw total employment expand from 176 million in 1993 to 213 million in 2000. During the same period, employment in *getihu* and *siying qiye* ventures grew by almost 42 million, implying that, aside from creating employment opportunities for new entrants to the labor market, the narrow

private sector is also providing job opportunities for workers shed by the shrinking state sector. Between January 1998 and September 2000, 21 million workers have left the state sector, 13 million of whom have found re-employment.<sup>13</sup>

### Regional Dispersion of *Siying Qiye*

Data are available on the location of privately owned firms defined narrowly to comprise *siying qiye*. Table 1.5 shows that both the numbers and the employment in these firms in the coastal region continue comfortably to exceed the numbers for the central and western regions combined. For all regions, though, the numbers of firms have grown rapidly, contributing more or less proportionately to the overall rapid growth noted in Table 1.5. If anything, the numbers are growing somewhat faster in the central and western regions. An interesting observation is that, in 1993, the average employment in *siying qiye* firms in the central and western regions, though small at 17 and 18, respectively, was considerably higher than the 15 for the corresponding indicator on the coast. In all regions, the average employment per firm fell by two by 2000: private firms countrywide are employing fewer workers on average. Clearly, new entry by firms of very small size offsets the growth of some firms to the much larger size observed in the survey of five cities described in Section 2.

**Table 1.5 Distribution of Number of *Siying Qiye* Firms and Their Employment by Region**

Year	Coastal <sup>1</sup>			Central <sup>2</sup>			Western <sup>3</sup>		
	Firms	Employment (‘000s)	Share of Total Employment (%)	Firms	Employment (‘000s)	Share of Total Employment (%)	Firms	Employment (‘000s)	Share of Total Employment (%)
1993	159	2,351	63	45	769	21	34	606	16
1994	285	4,055	63	91	1,478	23	56	952	15
1995	433	5,998	63	138	2,182	23	84	1,379	14
1996	530	7,231	62	178	2,742	23	112	1,737	15
1997	611	8,211	61	211	3,189	24	140	2,093	16
1998	759	10,365	61	250	3,835	22	193	2,892	17
1999	933	12,453	62	276	4,237	21	240	3,527	17
2000	1,185	15,774	66	293	4,160	17	284	4,132	17

Notes:

1. Coastal: Liaoning, Hebei, Beijing, Tianjin, Shandong, Jiangsu, Shanghai, Zhejiang, Fujian, Guangdong, and Hainan.

2. Central: Heilongjiang, Jilin, Shanxi, Henan, Hubei, Anhui, Jiangxi, and Hunan.

3. Western: Inner Mongolia, Shaanxi, Ningxia, Gansu, Qinghai, Xinjiang, Tibet, Sichuan, Chongqing (from 1998 onward), Guizhou, Yunnan, and Guangxi

Source: *China Statistical Yearbook*, 1994-2001.

### Private Ownership and Exports

When it comes to *export activities*, the general perception is that the (narrowly defined) PRC private sector, at least partly due to entry constraints, has yet to play a role in the rapid growth of

<sup>13</sup> World Bank, “China, Macroeconomic Update,” March 2001.

the country's international trade comparable to its already large contributions to the national output and employment. In the pre-reform era, PRC international trade was effectively monopolized by about a dozen foreign trade corporations (FTCs) that allocated import and export quotas to various industrial ministries, as dictated by the plan.<sup>14</sup> Since then, the PRC's trade regime has gone through substantial liberalization, with the plan gradually replaced (effectively, by 1992) by market prices, which now largely determine the inflow and outflow of goods and services.

The number of FTCs gradually proliferated; as a result, the right to trade internationally became widely provided to branches of the FTCs controlled by the central and local governments. Foreign-funded firms, including the joint ventures between foreign and domestic firms and those located in the Special Economic Zones (SEZs), were granted rights to export their products early in the reform era. By contrast with the purely Chinese owned private firms, the PRC's rapid progress as an international trading power owes much to the export orientation of these foreign-invested firms. More recently, large domestic enterprises increasingly have obtained import and export licenses that enable them to trade with foreigners directly. By 1994, according to a report of the International Trade Center (ITC), FTCs, SOEs and foreign-funded firms accounted for 53%, 17% and 28% of exports, respectively, while collectively and privately owned firms together accounted for only about 1% of total exports.<sup>15</sup> One analyst estimates that in 1998 the share of exports from foreign-funded firms reached 45%.<sup>16</sup> Unfortunately, more recent ITC reports are unavailable. And the *China Statistical Yearbook* includes no breakdown of the PRC's exports by ownership of the originating enterprises.

Some indirect evidence about the role of foreign-funded firms in the PRC's trade might be inferred from the tendency of those firms to be located predominantly in the coastal regions.<sup>17</sup> Table 1.6 displays export data, for 1999 and 2000 (from the Statistical Yearbook), and 2001 (from the Ministry of Foreign Trade and Economic Cooperation [MOFTEC] using customs data). The value of exports is shown for the coastal, central, and western regions,<sup>18</sup> as well as for the provinces (including Beijing) in which the survey cities for this study are located. As the figures show, export performance is extremely concentrated by region, with coastal provinces accounting for 90% of total exports in 2000, when Guangdong alone accounted for 37% of total PRC exports. The customs data from MOFTEC suggest that the corresponding shares are 92% and 36% in 2001, respectively. The same 2001 customs data show that almost two fifths of Guangdong's exports are sourced from Shenzhen alone, a graphic illustration of the advantages enjoyed by the early SEZs, as well as of the benefits they derive from hosting large inflows of foreign direct investment (FDI).

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<sup>14</sup> For an outline of the trade liberalization in the PRC, see Martin, Will, Betina Dimaranan, Thomas W. Hertel, and Elena Ianchovichina (2000) "Trade Policy, Structural Change and China's Trade Growth," Working Paper No. 64, Center for Research on Economic Development and Policy Reform, Stanford University.

<sup>15</sup> *Ibid.*

<sup>16</sup> Nicholas Lardy (1999), "China's WTO Membership," Policy Brief # 47, Brookings Institution.

<sup>17</sup> Of course, most Chinese firms that export are also more likely to be located in coastal areas; see the survey information from Nanhai and Wenzhou.

<sup>18</sup> The definitions of the geographical regions are as in the IFC study, *op. cit.* (see notes to Table 1.6).

**Table 1.6 Geographic Composition of Exports from the PRC, by Origin and Destination, 1999–2001**

Area	Exports	Share of	Exports	Share of	Exports	Share of
	(\$ million)	Total (%)	(\$ million)	Total (%)	(\$ million)	Total (%)
	1999 <sup>2</sup>		2000 <sup>2</sup>		2001 <sup>3</sup>	
PRC	194,931		249,203		266,155	
Coastal <sup>4</sup>	176,124	90	224,460	90	243,987	92
Central <sup>5</sup>	10,996	6	14,428	6	13,118	5
Western <sup>6</sup>	7,811	4	10,315	4	9,050	3
Beijing	6,285	3	7,667	3	11,787	4
Guangdong	78,760	40	93,428	37	95,426	36
Liaoning	8,128	4	10,589	4	11,008	4
Shaanxi	1,019	0.5	1,327	0.5	1,108	0.4
Zhejiang	13,654	7	20,482	8	22,976	9

Notes:

1. Export values in current prices.

2. Exports by origin, not by location of the exporting agent.

3. From Customs data published on the Ministry of Foreign Trade and Economic Cooperation website.

4. Coastal: Liaoning, Hebei, Beijing, Tianjin, Shandong, Jiangsu, Shanghai, Zhejiang, Fujian, Guangdong, and Hainan.

5. Central: Heilongjiang, Jilin, Shanxi, Henan, Hubei, Anhui, Jiangxi, and Hunan.

6. Western: Inner Mongolia, Shaanxi, Ningxia, Gansu, Qinghai, Xinjiang, Tibet, Sichuan, Chongqing (from 1998 on), Guizhou, Yunnan, and Guangxi.

Sources: *China Statistical Yearbook*, 2000 and 2001; Ministry of Foreign Trade and Economic Cooperation website.

## Investment and Financing

The PRC's privately owned firms have emerged rapidly despite facing seemingly difficult conditions. Apart from uncertainty about property rights due to the lack of official recognition of private ownership until very recently (essentially, the Constitutional Amendment in 1999), these firms have been effectively excluded from credits from banks. Table 1.7 shows that, although TVEs and foreign-funded firms in recent years have gained greater access to credit, short-term lending received by private firms is still minute, at about 1% of the total. The access of these firms to formal sources of financing is totally disproportionate to their contribution to output and employment.

Given that the PRC's private ownership is still dominated by small firms, raising capital on the domestic equity markets, which until recently were still subject to stringent regulations and quotas for listings, is impossible for most of them. As a consequence, one would expect that the tremendous growth of these domestic private firms has been financed mostly from retained earnings, such informal credit sources as personal networks, and extensive use of trade credit. The capacity to rely largely on self-generated funds for new investment ultimately will limit unnecessarily the speed at which these firms can grow. Table 1.8 shows the sources of financing for fixed asset investment for different ownership types in selected years.

**Table 1.7 Loans by Financial Institutions in the PRC at Year-end: 1994–2000**

Item	1994	1995	1996	1997	1998	1999	2000
Total loans (billion yuan)	3,998	5,054	6,116	7,491	8,652	9,373	9,937
Total short-term loans <sup>1</sup> (billion yuan)	2,695	3,337	4,021	5,542	6,061	6,389	6,575
	<i>Shares of total short-term loans (%)</i>						
Industrial, commercial and construction enterprises	78.2	76.1	75.9	65.8	64.7	61.5	55.5
Agriculture	4.2	4.6	4.8	6.0	7.3	7.5	7.4
Township and village enterprises	7.4	7.5	7.0	9.1	9.2	9.6	9.2
Foreign-funded <sup>2</sup>	2.9	3.0	3.3	3.4	4.1	4.7	4.6
<i>Siying qiye</i> and <i>getihu</i>	0.6	0.6	0.7	0.7	0.8	0.9	1.0
Other short-term loans	6.6	8.1	8.3	15	13.9	15.7	22.2

Notes:

1. Short-term loans are loans with maturity of no more than 12 months.

2. Includes firms funded by investors from Hong Kong, China; Taipei, China; and Macau.

Source: *China Statistical Yearbook*, 1995-2001.

**Table 1.8 Sources of Financing for Fixed Asset Investment by Ownership: 1985, 1990, 1995, and 2001**

Item	State		Collective		Private		Shareholding Corp		Foreign- Funded <sup>2</sup>		Total	
	1985	1990	1985	1990	1985	1990	1985	1990	1985	1990	1985	1990
Fixed asset investment (billion yuan)	168	299	33	53	54	100	n.a.	n.a.	n.a.	n.a.	254	452
	<i>Financing Sources (%)</i>											
Budgetary allocation	24	13	1	0	0	0					16	9
Domestic loans	23	24	38	27	0	4					20	20
Foreign loans	5	9	1	2	0	0	n.a.	n.a.	n.a.	n.a.	4	6
Self-financing	40	43	60	48	100	85					60	65
Others <sup>3</sup>	7	11	0	22	0	12					0	0
	<b>1995</b>		<b>2000</b>		<b>1995</b>		<b>2000</b>		<b>1995</b>		<b>2000</b>	
Fixed asset investment (billion yuan)	1,090	1,650	329	480	256	471	86	406	223	261	2,002	3,292
	<i>Financing Sources (%)</i>											
Budgetary allocation	5	10	2	7	0	0	1	1	0	0	3	6
Domestic loans	24	25	26	12	3	5	30	28	17	22	21	20
Foreign loans	8	2	6	4	0	0	7	5	52	35	11	5
Self-financing	49	45	56	67	96	80	51	47	24	30	67	52
Others <sup>3</sup>	15	17	10	10	1	15	11	19	7	13	-3	16

Note:

1. Investments are in current prices.

2. Include firms funded by investors from Hong Kong, China; Taipei, China; and Macau.

3. Unspecified; calculated as residuals.

Source: *China Statistical Yearbook*, 1996 and 2001.

The data show clearly that the share of self-financing for private firms has decreased only modestly since 1985; domestic loans still finance a very small fraction of fixed asset investment. At the same time, when compared with the 1980s, SOEs gradually are being weaned from their dependence on formal budget allocations. And the rise in the share of financing derived from the budget from 1995 to 2000 probably is best attributed to the Government's expansionary fiscal policies to combat deflationary pressure in the aftermath of the East Asian currency crises in 1997. By contrast, the SOEs' reliance on bank lending, much of which can be considered "quasi-fiscal" support, persists. The credit that goes to shareholding corporations, although a small percentage of the total, consistently accounts for about one third of those firms' total fixed asset investment. Foreign-funded firms, apart from their obvious advantage of having foreign investors, have been successful—perhaps somewhat surprisingly so—in obtaining close to a fifth of fixed investment funds from domestic banks.

## Summary

This review of national aggregate data supports the observations of the earlier IFC study, as well as the prevailing views of Chinese and foreign analysts. Specifically, private enterprises are becoming an ever more important source of PRC growth and employment, although evidence for their superior productivity is inconclusive. Private firms are still located predominantly in the coastal provinces. Their rapid emergence indicates comparatively free entry into markets, but they remain relatively small. To unleash their full growth potential, these firms continue to need more accommodating policies, especially to raise their access to investment funds. Although foreign-funded firms, members of the more broadly defined private sector, have become leading exporters, domestic private firms continue to focus primarily on supplying the domestic market for goods and services.

## Section 2: Findings from the Survey and Fieldwork<sup>19</sup>

National statistics convey a broad general understanding of the growth of private enterprise in the PRC and its contribution to the national economy. But there is very considerable regional variation in the influence of private enterprise, as well as in the climate for private economic activity. This study followed the earlier IFC study in also conducting a field survey, in this case, of *siying qiye* firms that are members of the China General Chamber of Commerce. Its objectives were to determine the status of the private economy in five survey cities, and to identify the principal constraints on the development of the private sector. Teams from Tsinghua University (Domestic Consultant—DC) conducted the survey from 15 July to 30 August 2001. Officials of the CGCC and its Local Chapters (LCs) aided the teams in their work. The detailed survey report (including the questionnaires) prepared by the DC is in Annex 2, and supplementary statistical analysis prepared by the International Consultant (IC) is in Annex 3.

The 2001 survey followed the methodology underlying that in the IFC (2000) study in several ways. First, it struck a similar balance between geographical representation and resource constraints by conducting fieldwork in five cities that are representative of the regional differences in private sector development in the PRC. Second, the 2001 survey comprised

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<sup>19</sup> For details see Annex 2, *Survey Report: Development of Private Enterprises in China*, School of Economics and Management, Tsinghua University, Beijing, China, September 2001.