

NOT FOR PUBLICATION

ADB-1952-6

Five Anti Campaign V: Control Over Private Enterprise

INSTITUTE OF CURRENT WORLD AFFAIRS

15 Peak Road (Small House)

Hong Kong

August 6, 1952

Mr. Walter S. Rogers  
Institute of Current World Affairs  
522 Fifth Avenue  
New York 36, N.Y.

Dear Mr. Rogers:

The growth of government control over private enterprise has been a continuous process in China since the Communists came to power in 1949, and since the beginning of this year the process has been speeded up. One of the most significant results of the recent Five Anti Campaign against the "poisons" of the bourgeoisie has been what might be called - despite a seeming contradiction in terms - the socialization of private enterprise. Very few businesses or industries were nationalized during the campaign, but the government increased its controls to such an extent that at present many so-called private enterprises have become, in reality, appendages of the state, and in these cases although private ownership continues it means very little. The fiction of private enterprise continues in many instances after socialized control, in disguised forms, has been firmly established.

The Chinese Communists' ultimate aim, of course, is to socialize the entire economy, and they have already nationalized a great many important economic enterprises. Transportation, utilities, virtually all heavy industry, and the majority of large-scale consumer goods industries are already state-owned or state-operated. Foreign trade is for all practical purposes a state monopoly; private companies still in business operate on a commission basis for government organizations. The purchase and sale of major agricultural products such as wheat and cotton are handled by government companies; the same is true of most important industrial raw materials. Almost all wholesale trade in the larger cities is monopolized by the state. And the government has already gone into retail trade in a big way and has established extensive chains of specialized stores dealing in foodstuffs and other necessities as well as state consumer goods stores selling general products.

Despite the expansion of state enterprises, however, the Chinese Communists continue to assert that private enterprise is to play a significant role in the Chinese economy during the present period of "New Democracy". But this assertion is always qualified in many ways. For example, Premier Chou En-lai in a speech on January 5 of this year stated that private enterprise must accept the "guidance of the state economy" and the "leadership of the working class", that there must be a "general plan of production" for the entire economy, and that "only legitimate profit is permissible (for private enterprise) within the limit set by the state or the price fixed by the state." Ever since 1949 Chinese businessmen have speculated on what phrases of this sort would really mean in practical terms, and they have hoped for the best. As a result of the Five Anti Campaign, however, many have come to expect the worst. They have concluded that the "significant role" for many private

enterprises will amount to nothing more than being sub-contractors, agents, or employees of the state.

The distinctions between state and private enterprises have become blurred. One Chinese businessman who has recently come out of Shanghai puts it this way: "It is useless to try to draw a clear line between government and private enterprise in China today. Actually there are very few differences between the two. Owners and managers of so-called private enterprises are for all practical purposes in the employ of the state. The government makes their important decisions for them. The only reason the government doesn't take over all private enterprise completely is that they don't have the trained personnel yet." This description of the situation is undoubtedly an exaggeration, but I believe it accurately indicates the current trend in China. It appears that during the present "New Democratic" period, when the Chinese Communists are laying the groundwork and preparing for general nationalization at a future date, more and more private enterprises in China will move into a sort of twilight zone in which they will be neither state-owned nor "private" in any real sense of that word. The Five Anti Campaign had many effects which accelerated this trend.

Private enterprise in China lost its fluid capital, and therefore its real independence, during the Five Anti Campaign. Under the guise of obtaining "illegal profits", back taxes, and so on, the government even took from many thousands of enterprises - probably the majority, if one can judge from reports received in Hong Kong - the capital needed for current operations; it then turned around and loaned them what they needed to keep going. In other cases, the Five Anti fines and assessments were obviously more than could be paid, and the government accepted IOU's which created an indebtedness to, and consequent dependence upon, the government. To cite one specific example, a business establishment in Hankow which I know about was assessed for an amount equivalent to US\$100,000 during the campaign, which was 30 per cent more than the total net income of the establishment since the Communist takeover in 1949. After considerable haggling the amount was slightly reduced. Then the company paid what it could and gave an IOU for the rest. Private enterprises which have been forced into a position of indebtedness to the government either in the form of loans or IOU notes as a result of the Five Anti Campaign could be taken over by the government at any time, but there is no indication that this is the government's intention. Instead, the government seems to prefer indirect control. The granting of loans was used as a wedge for direct infiltration of many private enterprises, however. For example, often when the People's Bank gave loans to a company it also sent representatives to take over key watchdog positions, such as those of assistant manager, accountant, and personnel chief.

The assessments and fines imposed during the Five Anti Campaign were not the only factors which robbed private enterprises of their financial independence; they were supplemented by a process of natural attrition which took place as a result of the campaign. While business stagnated, private companies were required to continue supporting their full payrolls. Government companies lowered prices, and private businesses which had stocks on hand took large losses. Industrial companies which were able to continue production piled up unsold stocks, and the govern-

ment "helped them out" by buying up their stocks at low prices. Other industrial establishments had difficulty selling, even to the government, because the functioning of government agencies was also disrupted during the campaign. Still others had difficulties keeping up production; they couldn't obtain raw materials, largely monopolized by the government; yet they too had to maintain their payrolls and keep paying fixed costs. Then, on top of everything, the business income tax came due at the peak of the Five Anti Campaign, and the People's Bank discovered that many businessmen had to obtain loans to pay their tax.

The combination of Five Anti levies, taxes, and the attrition caused by depressed markets was a one-two-three blow from which private enterprise in China is unlikely to recover as long as the Communists are in power. The government was remarkably solicitous as the Five Anti Campaign drew to a close - loans were extended at very reasonable rates and payments on both Five Anti levies and taxes were sometimes postponed or reduced - but this didn't alter the basic fact that thousands of private enterprises had lost all financial independence as a result of the Five Anti Campaign.

During the Five Anti Campaign, the government also increased its direct control over private enterprise in a variety of ways. Rarely did it resort to outright nationalization, however; the theory of "New Democracy" seemed to impose restraints even when nationalization was logical as a result of conditions which the Five Anti Campaign had created.

One of the most successful methods by which the government took over direct control of private enterprises was the organization of "joint public-private" companies. Businessmen from Shanghai report that the number of such companies increased during the Five Anti Campaign, and there is some indication that as this pattern can be applied more generally it may become standard for the larger and more important private enterprises during the transitional period of "New Democracy". From the government's point of view, this pattern is both simple and effective; a "joint" board of directors is established, and the government representatives on the board make all the important decisions. Sometimes a number of private companies in the same line of business are grouped together as a combine under a "joint" board. One specific case which I know about involves a group of over ten private companies in Shanghai (I am compelled throughout this report to avoid using names and exact figures, at the request of the persons who provided the information). Each of these companies still retains its managerial staff and board of directors, but they have lost their power. Superimposed on top of them is a central office of several hundred persons, controlled by government functionaries, and a joint board of directors, with government representatives as well as representatives of each member company. The government men on the board and in the joint office decide important policies and make the vital decisions. The capital, personnel, and accounts of the member companies

are pooled and can be interchanged. There is, in fact, very little substance to the idea that the member companies are still in existence as individual private enterprises. Almost the only "private" characteristic which they have now - and it is largely theoretical - is the fact that if any dividends are issued the original stock owners will receive them. Managerial control is completely in the hands of the government, and the "private" companies act as branches of the government agency controlling them. The advantage of this scheme, from the government's point of view, is that the personnel of the private companies can be fully utilized. Even on this score, however, the government is selective; at least two of the managers of individual companies in this "joint" enterprise were arrested during the Five Anti Campaign.

Another method employed during the Five Anti Campaign to establish firm government control over private enterprises without resorting to nationalization was instigation by Communist cadres of internal takeover by the staff members and workers of an enterprise. The case of a large retail store in Shanghai can be cited as an example. The staff and workers of this store were encouraged to denounce the owner-manager and subsequently to announce their assumption of control. The owner-manager was informed that henceforth he would not be permitted to exercise managerial functions or to withdraw profits from the store. He was granted, in lieu of his profits, a monthly allowance.

In other cases the government established direct control of private enterprises by purchasing blocks of shares. I know of one company in Shanghai, for example, in which the government bought a 30 per cent share of the stocks and then took over approximately one third of the positions on the board of directors. Since then the Communist board members have been in control. In theory, of course, the non-Communist members of the board can still out-vote the government men, but if you ask a businessman from Shanghai if this actually happens he will laugh in your face. Fear intimidates the majority, and any dissent or opposition to the decisions of the Communist minority involves the possibility of psychological persecution or worse.

It is not really necessary for the government to have representatives in a company or on its board of directors in order to control it, but such representatives obviously facilitate control. They are able to integrate private enterprises into the state's economic plans, ensure implementation of government policies, and prevent evasion of government regulations. Because the process of government infiltration is far from completed, however, the government still finds it necessary to exercise much of its control over private enterprises by less direct methods. Remote control can be very effective, however, and in many ways it extends even to Hong Kong, where the branches of mainland companies are in many instances closely supervised by Communist representatives. Hong Kong branches of mainland "private" banks, for example, no longer can make their own decisions on how they will use their capital; they receive instructions from a Chinese Communist representative, resident in the colony.

Private enterprises in China no longer have any secrets as a result of the Five Anti Campaign, and being private does not carry any

prerogative of privacy. The investigations carried out during the Five Anti Campaign were very thorough, and the details of methods, organization, costs, prices, and profits of private enterprises are now known to both the government and the employees of private companies. If exclusive information or techniques had anything to do with a company's competitive position relative to other private enterprises or its bargaining position in dealing with the government on contracts and purchase orders, these are now gone.

Another result of the Five Anti Campaign was the emergence of both employers associations and labor unions as effective instruments of government control over private enterprises. This was not a new development, but the economic control functions of these organizations were expanded during the campaign.

All private enterprises in China today must belong to a trade association, and in every city these associations are organized into a general Federation of Industry and Commerce. In theory, these are private organizations, but actually they serve as government-controlled front organizations. The owner of a Shanghai factory, who himself was an executive of one of these associations, described to me how this works. His association was made up of representatives of all Shanghai companies in his line of business, and it held a general meeting about once every two weeks and executive meetings several times a week. At each meeting, whether general or executive, a man sent by the Municipal Federation of Industry and Commerce attended and, in a quiet way, played the leading role. This man, although not a Communist Party member, worked for the party as a political worker and he received his instructions from the party. Every night, he, and similar political workers who controlled about eight other associations, met with a Communist Party member who outlined to them current policies. The genuine businessmen in the association did not control it; the quiet little man who attended their meetings was recognized as being in charge.

These organizations were greatly strengthened during the Five Anti Campaign and were used by the authorities to put pressure on businessmen. At the conclusion of the campaign, steps were taken to bring them into a more effective nationwide organization. An All-China Federation of Industry and Commerce Preparatory Conference, attended by 160 leading businessmen from various parts of China, was held in Peking during the last ten days of June, and it adopted a constitution for a permanent organization.

Already some of these associations, in consultation with government agencies and companies, set maximum prices and minimum standards for their members, and it is likely that in the future they will be utilized to obtain from private businessmen all sorts of "voluntary" agreements and pledges in line with government policies. This development was suggested by an article in the February 10 issue of Study, a leading Chinese Communist journal, which said: "After the conclusion of the (Five Anti) movement, the Federations of Industry and Commerce should call upon and organize industrialists and merchants for the conclusion of new patriotic pacts, with opposition to the five vices

as their contents, and undertake regular inspection and supervision over the faithful implementation of such compacts."

Labor unions have also developed into an important instrument of government control over private enterprises. During the Five Anti Campaign they were used, in accordance with the basic principles of class warfare, as one of the principal means of applying pressure on businessmen and extracting information and confessions from them. They were strengthened organizationally during the campaign, and their economic control functions were increased.

The Workers Daily, organ of the All-China Federation of Labor in Peking, defined the responsibilities of unions as follows, in an article published on May Day this year: "Under the leadership of the Economy Check-Up Committee, trade unions should organize the working masses to supervise the capitalists so that they may be restrained from repeating acts of the 'five poisons'. This is the main task confronting employees and workers in private enterprises." Their main responsibility, in short, is to help the government control private enterprises rather than to concern themselves with problems of more direct concern to workers.

In some cities in China, all contracts between state agencies and private enterprises must now be signed by union representatives who together with representatives of the enterprises' senior staff members sit in on the contract negotiations, review contracts, and help to determine "legitimate profits". Because of the detailed knowledge of operations which union members possess, they are called upon particularly to review cost estimates made by the managers of private enterprises.

Unions have also been given a share of responsibility for internal plant management in private factories, which they exercise through Labor-Management Consultative Committees. The line separating management and union responsibilities in this respect is sometimes rather vague, and there have been cases in which the Communists have reprimanded unions for going too far in encroaching upon management functions, reminding them that their job is merely to supervise and that the managers of private enterprises do still have basic responsibility for managerial functions.

As a result of developments during the Five Anti Campaign, the organizational mechanism now exists in Communist China for the government to make decisions of many sorts affecting private enterprises - decisions regarding production plans, specifications, costs, production rates, and profits - and ensure that they are implemented. This means that in a sense the Chinese Communists can include the remaining private sector of the economy in their overall state planning. The integration of private enterprises into their economic planning may be somewhat less than perfect, but at least the government is in a position to fit private enterprises into their plans.

To date I have only mentioned methods by which the government developed, during the course of the Five Anti Campaign, organizational techniques for improving its control over private enterprises. This is only one side of the picture. During the campaign, the dominant position of state enterprise in the urban economy also increased, and this in itself reduced the independence of private enterprises.

"The government is the only buyer in China's cities today." This statement made by a Chinese businessman who came to Hong Kong from Shanghai recently is a great exaggeration, but it has a kernel of truth. There is a clear trend toward narrowing and limiting the free market, and this trend was accelerated during the Five Anti Campaign.

More and more private enterprises in the production field are finding themselves in the position of working for the government on a contract basis. In some cases, the government buys the produce of private enterprises, setting the price and profit margin, after the goods are put on the market. In others, the government moves in at an earlier stage and places "processing orders"; when it does this it is able to set specifications and delivery time as well as prices and profits. The scale of government buying is already so large that many private producers cannot find non-government buyers.

Even when government buying does not completely dominate the market, and some private outlets for sales remain, government purchases are often large enough to establish prices. This is true even in the consumer goods field in big cities now. In Shanghai, for example, if the State Consumer Goods Stores reduce the price of soap, private sellers are forced to reduce their price too. This is often very hard on private enterprises because their costs and overhead are usually higher. (Two different wage scales prevail, for example, and the one in state enterprises is lower.) By dumping or buying, and manipulating their prices, government companies are now able to exercise a high degree of regulation over the free market.

The Five Anti Campaign greatly increased government buying and selling, and the influence of these operations on the urban economy as a whole. Because the free market stagnated, the government was able to move in and take over. It bought stocks which weren't being sold. It placed orders with producers who had no markets. And it sold at prices which were difficult for private business to match. As a result the government established itself as the undisputed leading buyer and seller in the free market.

The campaign not only increased the volume of government contracts with private enterprises, it also strengthened the controls which the government exercises over establishments under contract. Cheating on government contracts was one of the specific vices publicised in the slogans of the campaign, and great emphasis was placed upon the need to investigate cost estimates and profits, with a view to reducing both. Private enterprises were severely penalized for past sins in this regard: over-statement of costs, production of sub-standard goods, late deliveries, "unreasonable profits", and so on. It was decided that in the future costs and profits would be more carefully supervised, and that

costs would be determined on the basis of "average conditions obtaining in factories managed properly and reasonably". And on June 24, Ch'en Yun, head of the Committee of Finance and Economics in the Peking Government outlined a national policy of restricting profits on contracts with private enterprises to 10 or 20, or in exceptional cases 30, per cent.

One important psychological factor must also be mentioned in explaining the increase of government control over private enterprises in the free market which took place as a result of the Five Anti Campaign. During the campaign many private companies were penalized for "illegal profits", and so on, on the basis of comparisons with the prices, costs, and quality of the products of state enterprises. In short, the practices of state enterprises were used as a standard for judging private enterprises. As a consequence, many private businessmen decided that to avoid future trouble they would have to follow the lead of state enterprises as closely as possible. One Shanghai businessman whom I know tells me that he is now selling his products at a price which entails a considerable loss, "just to stay out of trouble."

The results of the Five Anti Campaign as it affected private enterprises in Chinese cities can be summarized, therefore, as a great decrease in the independence of private enterprises and a great increase in government control. The state is becoming the real entrepreneur for the economy as a whole, and private businessmen find the scope for independent decisions on their part steadily decreasing. In short, the Five Anti Campaign made it possible for the government to speed up the process of socialization without resorting to nationalization except in a relatively few cases.

Now the Peking Government has embarked on a great program to increase production and develop industry. Top leaders maintain that the Five Anti Campaign has laid the groundwork for this new campaign. In one sense it undoubtedly has. Tight government control over private enterprises will make it possible to formulate plans for the economy as a whole. But one cannot help but speculate about the possible effects of reduced incentives and loss of initiative on the part of private businessmen. Chinese businessmen have already lost so much, and have so little to gain even if the new campaign is successful, that they can be expected to show little enthusiasm.

Sincerely yours,

*A. Doak Barnett*

A. Doak Barnett