Institutional Foundations of China’s Growth

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China’s Growth Not Due to Rule of Law

World Bank Doing Business Indicators

"Ease of Doing Business"

    China: 91 (same as Guatemala and Zambia)
    Peru is 43, Mexico is 48

"Ease of Entry"

    China ranks 151 (same as Congo)
    Significantly below Iran (87) and Pakistan (98)
Acemoglu and Robinson: “Why Nations Fail”

Jiangsu Tieben Iron and Steel (from Richard McGregor of the Financial Times)

Private company supported by local government of Changzhou

"As a low cost producer, he thought he could easily grab a profitable market share away from the relatively pampered state-owned giants like Baosteel, 150 kilometres away down the Yangtze, near Shanghai."
Started to build in 2003, but stopped in March 2004 when Communist Party ordered banks to stop lending.

CEO (Dai Guofang) arrested and spent five years in jail.

**Acemoglu-Robinson:** China is no different from other failed states

**Vested interests protected; entrepreneurs are blocked**
Aluminum Market in China

Chinalco dominated aluminum market until 2008

Chinalco had exclusive rights to buy bauxite at below market prices

Bauxite deposits in Sanmenxia Prefecture in Western Henan Province
East Hope Group

Sales of $8.8 billion, 80,000 employees

Started in 1982 in rural Sichuan Province selling quail eggs. Later expanded to pig feed

CEO Liu Yongxing: Currently sixth richest person in China (net worth US$ 7 billion)
Decided to go into Aluminum

Liu Yongxing: "Make sure my company did not become the next Tieben. Tieben is a lesson for us all. It was a tragedy."

East Hope cut a deal with Party Secretary of Sanmenxia

Chinalco fought East Hope Group every step of the way

Chinalco’s market share dropped by 98% in 2005 to 50% by 2008.
Why was East Hope able to do it?

Private Money (did not depend on state owned banks)

Tap into interests of local government

East Hope CEO: "Forgive me for being frank, but local officials, even corrupt ones, all need to have political achievements."
Shanghai-GM

Largest car manufacturer in China

49% owned by GM, 51% owned by SAIC Motor Co.

SAIC Motor Co. (original state owned firm) is publicly listed but majority stake held by SAIC Group

SAIC Group is owned by local government of Shanghai

SAIC Motor also owns 50% of Shanghai-Volkswagen

SAIC also owns a stand-alone car company
Shanghai-GM's business model

Sell low quality cars at monopoly prices (who owns the firm?)

Buick New Century

Opel Corsa rebranded as Buick Sail

Daewoo Matiz rebranded as Chevrolet Spark

Six months before Shanghai-GM was ready, Chery-Wuhu came out with an identical car (Chery QQ)
Buick New Century
Opel Corsa
Chevrolet Spark and Chery QQ
Chery-Wuhu (Wuhu, Anhui Province)

Started by engineers at First Auto Work ("Red Flag" sedan)

Approached Wuhu Party Secretary in 1996

Party Secretary of Wuhu: "You let me take care of the licenses and land; you just focus on getting some cars built here."

Bought and shipped assembly plant in Spain

First car was a clone of VW Jetta

Second car was clone of Chevrolet Spark (clone of Daewoo Matiz)
Chery-Wuhu

Legally registered as state owned firm (Wuhu local government holds majority stake)

Is it really a state owned firm?

Party Secretary of Wuhu promoted to Vice Party Secretary of Anhui Province

Chery-Wuhu is major exporter

Shanghai-GM does not export
What is the Chinese model?

**Suharto Model:** Crony Capitalism Controlled by Local Mafia Bosses

“My Friends Get Everything, Everybody Else Gets Nothing”

This is capitalism in most poor countries – Gains by Cronies is Outweighted by Losses to Everyone Else

**3,000 Suhartos**

Local Suhartos/Mafia bosses competing ferociously for business

Out of favor businesses can go to other localities and become the favored firms there