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Lessons for Africa in Chinese SOE Governance

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Executive summary

China's state-owned enterprise (SOE) sector is vast and diverse. There are more SOEs in China than companies of all kinds in most African countries, and China's state sector produces more and has grown faster than sub-Saharan Africa's entire economy. China's SOEs have gone through four waves of reform, roughly once per decade. Common themes have been the use of market competition within state ownership; increased operational autonomy alongside multi-faceted governance, using both capital markets and evolving state institutions; and high-cost compensation, formal and informal, for those affected, far beyond the facades of training programmes.

Countries in Africa seeking to learn from China's experience should note that state building preceded and continued alongside the reform of state ownership, and was necessary for the state to harness markets to its purposes. However, opportunities for state building and reform at scale are rare, and several tactical lessons can be learned in the interim. Those include the use of quality global exchanges and strategic investors in listings; dividing easily separable SOEs into competing units, even if still all state-owned; structuring reporting lines carefully; and laying the political preconditions of continued action in each round of reform. The ultimate lesson is to see SOE governance as an evolving system, requiring continuous learning and little dogma.

Introduction

China's SOEs are the subject of much debate. SOEs in China earn a lower return on assets than private enterprises and absorb a disproportionate share of credit. On the other hand, they operate in lower-return but economically necessary sectors, and shoulder a range of difficult-to-price externalities. The debate about them can become dogmatic and not very helpful.[1]

This policy insight will not enter that debate. It will instead focus on the following questions: What is the landscape of Chinese SOEs? How have they changed over time? What principles have underpinned their governance and its reform? In doing so, it hopes to be useful to policymakers and others in Africa reforming local SOEs, in contexts where both full privatisation and unreformed public ownership are unfeasible or undesirable, for technical or political reasons.

Much of China's experience with SOE reform will be hard to replicate elsewhere. Its political system and governance traditions are unique. As will be seen, China could break SOEs up into province-sized units, because its provinces are larger than most countries; and it could stitch the units back together, because it is ultimately centralised. Observing up close how

1 Usefully summarised in Adam Tooze, "*Reading China's State Capitalism*", *Chartbook Newsletter* 9 (December 13, 2020).

China has put its attributes to work, however, does provide some lessons that may be of value in Africa, both in phases of strategic state building and reform, and more tactically.

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This policy insight will first cover the variations among China's SOEs at different levels of government. It will summarise the waves of SOE reform in China over the past four decades, then consider in detail two common principles of that reform: competition, and mixed governance, under common state ownership. It will conclude with possible lessons in African contexts, accounting for constraints on replication.

The variation in China's SOEs

The overall landscape of SOEs in China is one of considerable diversity. The country's governance structure has four tiers: central government, provinces, municipalities, and districts/counties.[2] The government at each of these levels can own enterprises, so China has central SOEs, provincial SOEs, and so forth. Since most Chinese provinces are considerably larger than some countries, the provincial and local SOEs are extensive and can be very large. The tenth-largest province in China (Hubei) has a slightly larger population, and considerably larger economy, than Kenya. There are more SOEs in China than there are companies of any kind in many countries in Africa (Figure 1).[3]

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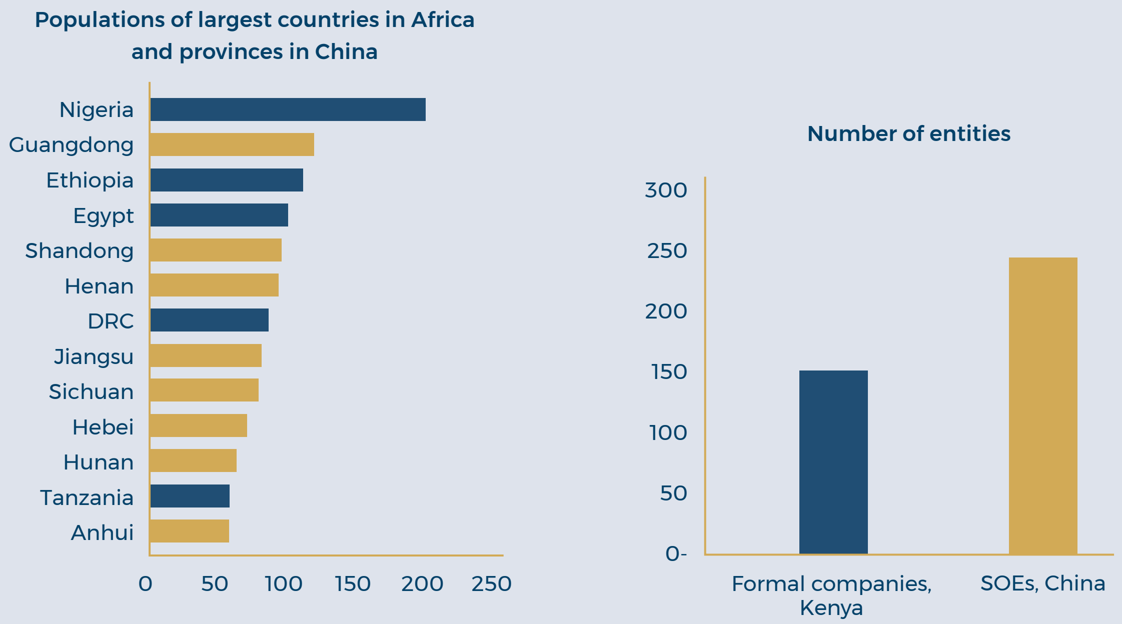
In general, the higher the tier of ownership the larger the enterprise, even if some provincial and municipal SOEs can be extremely large. For example, Shanghai Electric, owned by the Shanghai government, is the largest power equipment producer in the world, with a

2 Sebastian Heilmann, ed., *China's Political System* (Maryland: Rowman & Littlefield, 2016).

3 "Over 84% of Companies in China Are Private", *China Daily*, November 28, 2019; Business Registration Service (Kenya), "Summary of Registered Entities in 2020".

revenue of over $20 billion per year. Local SOEs tend to concentrate on the provision of local public services and local infrastructure, such as water and sanitation or public transport, while the central SOEs focus on national public goods, such as the national high-speed rail system and the national financial system, or on achieving global competitiveness in 'strategic sectors'. Again, these are not hard-and-fast divisions. China's most successful entrant into the global semiconductor industry, Yangtze Memory Technologies, is owned, via multiple subsidiaries, by both the Hubei and Beijing provincial governments. Ownership structures can become so complex that thousands of enterprises are or are not SOEs depending on the definition – and this is not a theoretical question, but one often affecting the price of hundreds of billions of dollars in bonds.[4]

Figure 1 SOE sizes in China



Source: "Over 84% of Companies in China Are Private", *China Daily*, November 28, 2019; Business Registration Service (Kenya), "Summary of Registered Entities in 2020"

Centrally owned SOEs are overseen by the State-Owned Assets Supervision and Administration Commission (SASAC). The exceptions are the large state-owned banks, which are overseen by the China Investment Corporation (CIC), China's sovereign wealth fund. Most provinces, and many municipalities, have their own versions of SASAC. Again, some ownership stakes may be held through somewhat complicated structures, involving

4 Junyeop Lee, "State Owned Enterprises in China: Reviewing the Evidence" (Paper 6-7, Organisation for Economic Co-operation and Development, Paris, January 2009); Chunlin Zhang, "How Much Do State-Owned Enterprises Contribute to China's GDP and Employment?" (Working Paper, World Bank, Washington DC, July 2019).

provincial 'investment funds', crossholdings among local SOEs, and even holdings by universities. The composition and role of both SASAC and the CIC are covered in some detail below.

The waves of reform

China's SOE governance has gone through four waves of reform since 1978, roughly corresponding to one wave per decade.

1980s: Gradual increases in autonomy

China's economy was wholly dominated by SOEs at the start of its reform period. SOEs then had almost no autonomy: they were assigned inputs and required to produce a quota of outputs. They were also responsible for providing social security to their employees, the so-called 'iron rice bowl'. During the 1980s the SOEs were first allowed to produce as they saw fit, once their minimum targets were met, and then were allowed flexibility in setting prices.[5] Officials in these early reform efforts would later play significant roles in the formation of SASAC and in the process to publicly list the largest SOEs.

1990s: Mass-scale rationalisation

SOEs' role in the economy was dramatically reduced in the 1990s. Under then-premier Zhu Rongji, tens of thousands of uncompetitive SOEs were privatised or shut down.[6] Mitigating the harm from the resulting job losses was a priority across government. A new Ministry for Social Security was created, and export growth was dynamic in the lead-up to World Trade Organization accession. Housing reform gave workers ownership of the apartments they lived in and set off a construction boom that absorbed as much labour as manufacturing. Some policies were highly improvised, and sometimes inefficient: for example, many cities employed laid-off SOE workers as largely superfluous 'traffic wardens'. Yet the focus on employment generation, in ways often far beyond orthodoxy, was the necessary complement to the orthodox policy of mass-scale rationalisation of SOEs. Without this complement, the reform drive at the time would not have succeeded. Fierce political opposition was mounted to SOE reform, including at senior levels within government, and was only overcome through the containment of the fallout by the aggressive deployment of policies to compensate workers in multiple, creative and pragmatic ways.[7]

5 Justin Yifu Lin, Fang Cai and Zhou Li, "Competition, Policy Burdens, and State-Owned Enterprise Reform", *The American Economic Review* 88, no. 2 (1998): 422–427; Trevor MacMurray and Jonathan Woetzel, "The Challenge of Facing China's State-Owned Enterprises", *The McKinsey Quarterly* (Spring 1994).

6 Shahid Yusuf, Kaoru Nabeshima and Dwight Heald Perkins, *Under New Ownership: Privatizing China's State-Owned Enterprises* (Washington DC: World Bank Publications, 2006). Much of this and the preceding period have also been covered in the recently published Weber, Isabella M. *How China Escaped Shock Therapy: The Market Reform Debate*. Routledge, 2021.

7 David Zweig, "China's Stalled 'Fifth Wave': Zhu Rongji's Reform Package of 1998–2000", *Asian Survey* 41, no. 2 (2001): 243–244.

2000s: Governance experimentation

From the late 1990s to the early 2000s, the central government listed partial stakes in many of the largest SOEs (described further below). As China also shifted its growth driver from exports to domestic investment, SOEs dedicated to infrastructure boomed, with provincial and local SOEs focusing more and more on infrastructure.[8] Notable examples were provincial power and road utilities and special-purpose vehicles created by municipalities. In the aftermath of the global financial crisis, the country's large state-owned banks were directed to lend to such infrastructure-focused SOEs as the means to deliver China's giant stimulus to the economy. Some industrial SOEs were also encouraged to 'go out', ie, to invest abroad, which saw (among others) the first wave of large-scale Chinese investment in and construction of African infrastructure.

2010s: Seeking 'dynamic state capitalism'

Since 2013 Xi Jinping's government has emphasised a model that generally relies on the market but with the state in a leading role. The state is 'trying to get more out of SOEs and trying to use them to get more out of the private sector'.[9] The method has been to expand mixed ownership, in which SOEs attract minority private investments but also make their own investments in private sector firms.[10] Some large SOEs have been combined and given an explicit orientation to compete in global markets. Some, such as State Grid and the high-speed rail maker CRRC, have emerged as potential global leaders in their industries. At the same time, as a legacy of the post-2009 stimulus, many provincial and local SOEs have come close to defaulting on their debt – and some have in fact begun to default.

Chain reaction

Each stage of this evolution depended on the one before it. The mass rationalisation of the 1990s would not have been possible without at least some portion of the SOEs getting into shape to survive in the 1980s. The governance experiments of the 2000s would not have been possible without the rationalisation going on around them. The attempt to create 'dynamic state capitalism', with globally competitive giants, would not have been possible without the prior governance experiments and the at least partial improvements in performance that followed. Each stage also required that sufficient people harmed in the phase before were compensated at least sustainably enough that the subsequent phase was not derailed by intense and widespread opposition.

8 Chong-En Bai, Jiangyong Lu and Zhigang Tao, "The Multitask Theory of State Enterprise Reform: Empirical Evidence from China", *American Economic Review* 96, no. 2 (2006): 353–357.

9 Tooze, "Reading China's State Capitalism".

10 Xiaoqian Zhang, Mingqiang Yu and Gaoquan Chen, "Does Mixed-Ownership Reform Improve SOEs' Innovation? Evidence from State Ownership", *China Economic Review* 61 (2020): 101450.

> China did not wait until it could conduct an ideal reform all at once. It saw reform as a continuous task, solving what was possible in each phase

Regular change of such magnitude is made possible by some of the unique features of Chinese governance, which may not be replicable in African contexts. Yet, importantly, China did not wait until it could conduct an ideal reform all at once. It saw reform as a continuous task, solving what was possible in each phase, in a way that created more possibility in the next stage. The lesson for African policymakers here is not to spend five years agonising over a perfect reform, see it bogged down for another five, then ensure no further reform is politically viable by providing only weak support for those harmed. It is instead to continually move the ball forward, achieving results while preserving or expanding the political base for the next step forward.

Behind the regular change, some common principles can be discerned.

Among those, the most prominent, and perhaps the most useful, is the continual attempt to utilise market competition under the shadow of state ownership.[11] Another is the deliberate seeking of checks and balances, including the introduction of ones from outside the state. These two principles may often fall short of their goals, and both have a significant dependence on China's size and political economy. Nonetheless, they are central to how China governs its SOEs and hence deserve special scrutiny.

Competition within state ownership

Nearly every SOE in China is subject to competition, primarily from other SOEs. It is rare for an SOE to hold a monopoly, except in industries that are natural monopolies regardless of ownership, such as rail lines. Competition exists even in power transmission: China has two grid operators, State Grid (the larger) and China Southern Power Grid. There are five different centrally owned power generation SOEs, and many provinces own one or more as well. There are three major SOEs in telecoms, four in banking, and multiple construction and equipment SOEs, again just at central level, with many more being provincially owned.

There are two caveats to this rule. One is that, while SOEs may compete with each other on the same ground, they tend to compete with private enterprises on an uneven playing field, being favoured in their access to bank loans and other inputs. As a result, private enterprises try to avoid SOE-dominated sectors. For example, they enter solar panel production instead

11 Similar to the general Chinese governance method of 'experimentation under [the] shadow of hierarchy', for which see Sebastian Heilmann, Lea Shih and Andreas Hofem, "National Planning and Local Technology Zones: Experimental Governance in China's Torch Programme", *The China Quarterly* (2013): 896–919.

of traditional power generation equipment, or find specific niches within such sectors, such as running private freight warehouses along major rail lines. Sometimes, however, local government can encourage private entrants to discipline a large local SOE – for example, the city of Changsha is home to two of the world's largest construction equipment makers, Zoomlion (an SOE) and Sany (private), and tries to limit the state tilt towards Zoomlion.

A second caveat is that, when one or more SOEs are competing globally, they may be merged into a single national champion to compete with giant multinational corporations more effectively. This has occurred, for example, in high-speed rail. Such consolidation, however, happens after intra-SOE competition.

Why have multiple, overlapping entities, competing under the same owner? Because competition enlists the market in support of the state to monitor SOE management.[12] When an SOE of significant size is broken up into two separate SOEs, they have the same policy burden and restraints as the original. How the two SOEs then perform relative to each other demonstrates the quality of their respective management, and whether that management is performing or shirking. Since neither SOE is then vital to the state, discipline mechanisms can become credible. If the management of one SOE performs badly, it could be removed and the SOE restructured, with its twin picking up its responsibilities during the restructuring period.

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The effect of such competition is strengthened by its intersection with China's system of government promotion.[13] Promotion among Chinese Communist Party officials is overseen by the party's 'Organisation Bureau'. The senior managers of SOEs are all party members, and a strong performance running an SOE is often the springboard for later promotion to senior positions in government. Conversely, poor performance relative to peers limits a career. Evaluation and promotion is applied to provincial governors, too, and within departments. As a result, governors have a strong incentive to ensure adequate performance of the SOEs owned by their province, as do the heads of the provincial-level SASACs.

The promotion system, combined with competition, also provides a backstop for the budget constraints on SOEs. As in most countries, the SOEs formally must break even,

12 Lin, Cai and Li, "Competition, Policy Burdens", 422–427.
13 Heilmann, Shih and Hofem, "National Planning", 896–919.

aside from capital injections for specific investments, and formally will not be bailed out. In practice, if a very large and consequential SOE is on the edge of bankruptcy, and it cannot be absorbed by another SOE without a large injection of funds, then this budget constraint will be violated. The promotion system will then exact an extremely high price from the management of the failed SOE, and managers know this.

That indicates the necessary condition for this principle to work. An 'Organisation Bureau' in the Chinese form may not be strictly necessary, but it is necessary that managers face credible consequences if their SOE performs significantly worse than a competitor SOE. If the SOEs have so many other political tasks that none of them can succeed, consequences for any specific managers will not be credible. If managers believe workers will suffer while they themselves will just get new and comfortable jobs in other SOEs or private firms, then competition will have no consequences. Bonus schemes are unlikely to work, either for their political consequences or because, as in private companies as well, the schemes will simply be gamed.

Therefore, there must be just enough distance between short-term political needs and SOE governance that not all the entities will be badly managed, and managers must be exposed to consequences if their SOE performs worse than its peers. On the other hand, the clearer that relative performance is, and the easier division is, the lighter these conditions can be. It seems likely that only a robust governance system should attempt competition among network entities, like transmission lines; but where assets and outcomes are easily comparable, as with power plants or highways, the principle may be much easier to apply.

The work of governance: IPOs, SASAC

The large central SOEs have significant political weight (as large companies have in all political systems). That endangers the effectiveness of any formal system for managing them, even with competition: a pair of large SOEs in telecoms or rail could very well organise to capture their regulator (as private telecom companies do in many markets). A very large SOE, with a large budget and providing important goods and services, will also be a tempting target for political capture from above. The risks of capture from above and below reinforce each other: political actors and SOE management may collude to each other's benefit, using the weight and importance of the SOE to impose terms on other parts of the system, such as the fiscus and regulators.

China's attempts to mitigate these risks have evolved over the decades of the reform era. Sometimes those attempts failed, as with the oil and gas sector and with railways in the early 2010s. In large part, however, the constraints have held. The general principle of competition helps, as central SOEs with too much power have been broken up into functional or geographic units or new competitors created for them. The 'Organisation Bureau' is also independent and can rotate management personnel among SOEs within a sector (just as provincial leaders are rotated to prevent regional power bases).

An additional check, or attempted check, has been the public markets. Zhu, China's reformist premier in the late 1990s, was clear about the deficiencies of the SOEs and that, even as premier, he did not have sufficient political weight to force change upon them by himself.[14] Zhu and other reformers hoped that the process of getting ready for an initial public offering (IPO) would speed the professionalisation of SOE management. The expectation was that public shareholders would then provide ongoing constraints on SOE management and continuous pressure for further improvement.

The listing wave began with China Telecom (later renamed China Mobile) in 1997, although some of the banks and other financial firms had listed in Hong Kong somewhat earlier (known as 'red chips'). The firms that were listed from 1997 were constructed out of ministerial departments, through extensive reorganisation, often shortly before the listing. PetroChina, for example, was created out of departments in a ministry employing 1.5 million people. More than 1 000 accountants, lawyers and consultants worked for 18 months to create a new company that would be listed (called the 'ListCo').

Once the ListCos were constructed, their investment case rested on growth and margin expansion through the gradual removal of old inefficiencies. That case had to be presented in the language of global markets: based on financial statements audited by one of the big global auditors; with business units organised on recognisable lines; and run by managers with the incentives and authority to pursue growth and efficiency within those units. The bankers, consultants, lawyers and accountants brought in to prepare for the listing both helped transform the old entities into the ListCos and prepared the ListCos' narrative in the form and language of global capital.[15]

The investment cases also needed external validation. That was sought from two sources. One was to list on a leading global stock exchange with difficult listing requirements, usually the New York Stock Exchange. The second was a strategic investor in the same industry. For PetroChina, that meant BP; for China Mobile, Vodafone. Listing on a quality exchange, with a strategic investor, meant that experts in governance and in the industry had to some degree vouched for the core of the investment case: that the company was recognisably governed, and capable of at least a serious attempt at executing against the opportunity in front of it.

The amount of remaining state control was relatively less important. It was clear at the time that the Chinese state was not going to give up majority state ownership. Since then, investors have not punished the SOEs for that remaining ownership. China Mobile's listing was explicitly compared to that of Deutsche Telekom, which had been privatised a few years before. The total returns to shareholders since China Mobile's listing paint a

14 Hank Paulson, *Dealing with China* (London: Hachette UK, 2015); Zweig, "China's Stalled 'Fifth Wave'"; Yusuf, Nabeshima and Perkins, *Under New Ownership*.

15 The effort to turn the organisational pieces into what global investors would recognise as coherent and investable companies was immense. Elite consultancies saw entire teams resign when projects finished, burned out. On some deals, the investment banks threatened to walk out repeatedly. The units pieced together had often not possessed basic management information systems or accounting procedures.

clear picture, even when compared to the purely private AT&T (Figure 3).[16] Chinese state-owned banks' share prices may have underperformed those of US banks, but they have significantly outperformed those in Europe, which are privately held.

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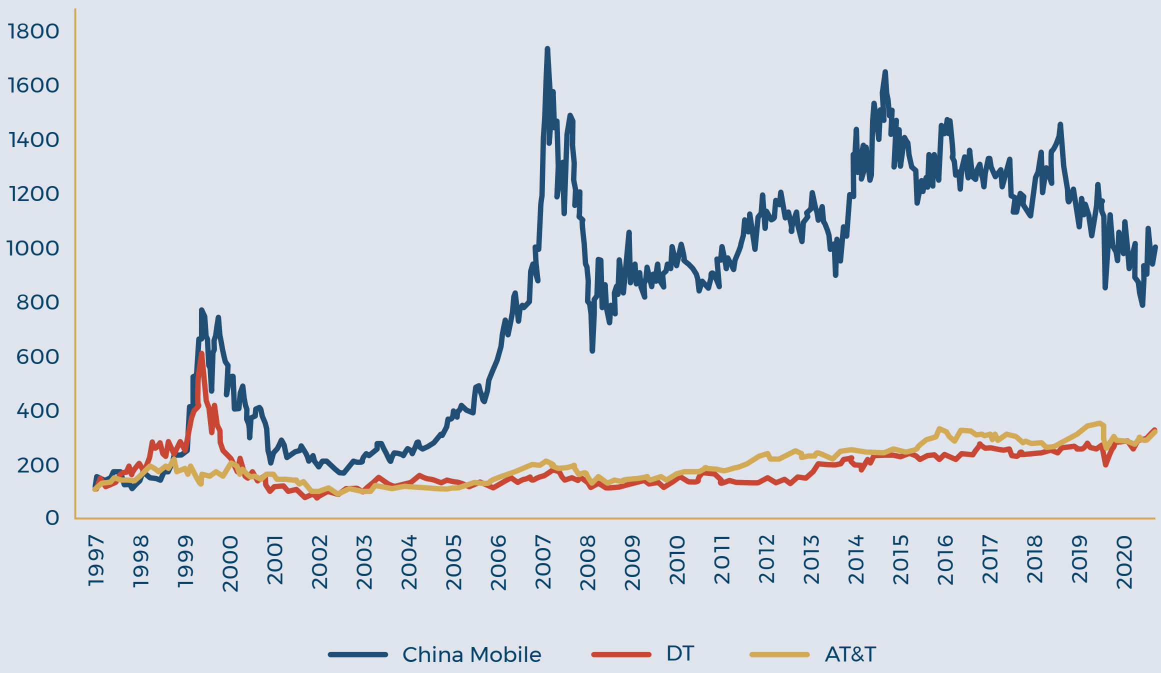
Figure 2 Total return to shareholders (indexed to 100)



Source: Author's calculation using public financial data on share prices, splits and dividends

That is not because the Chinese state has been passive in its ownership. In the years after the initial IPOs, state intervention revoked the share options awarded to managers when it became clear how wealthy the options would make those managers. Several SOEs also extended, sometimes by many years, the severance packages granted to workers. The state has realised that the public markets exercise less effective control over listed companies than sometimes advertised. As a result, more and more weight has been placed on the

16 Mobile markets have grown similarly, to the same size today in total revenue.

mechanisms of internal guidance and oversight, through the promotion system and through the holding entities, SASAC and the CIC.[17]

The remaining state stakes in the publicly listed SOEs are managed by either the CIC, for the banks, or SASAC, for the remainder. Both the CIC and SASAC have significant political weight, reporting directly to the State Council, China's cabinet. Both concentrate on the corporate governance of the companies they oversee, including active review and engagement with their boards. When it first recapitalised the Industrial and Commercial Bank of China, Central Huijin (the CIC's first incarnation) appointed six to seven full-time equity board members to help its reorganisation. SASAC repeatedly summons the heads of central SOEs to account for strategic decisions they have made, and has review and veto power over their investment plans.

Such power would make both SASAC and the CIC tempting targets for political capture. Take over SASAC, and, in theory, all the patronage power and procurement of the SOEs would be at one's command. In some cases, they have been used to send orders to the companies they oversee to act in ways that serve politics. Notably, the State Council ordered the state-owned banks via Central Huijin to massively increase lending in the aftermath of the 2008 global financial crisis. Overall, however, neither the CIC nor SASAC has been captured for patronage and procurement diversion in this way (even if individual SOEs have). There is no firm evidence on the reason for this (unsurprising, given the opacity of Chinese politics at so senior a level), but several factors seem important.

SASAC and the CIC report to the State Council as a whole, not to a single person or minister. An attempt to capture them from above would have to capture most of the cabinet

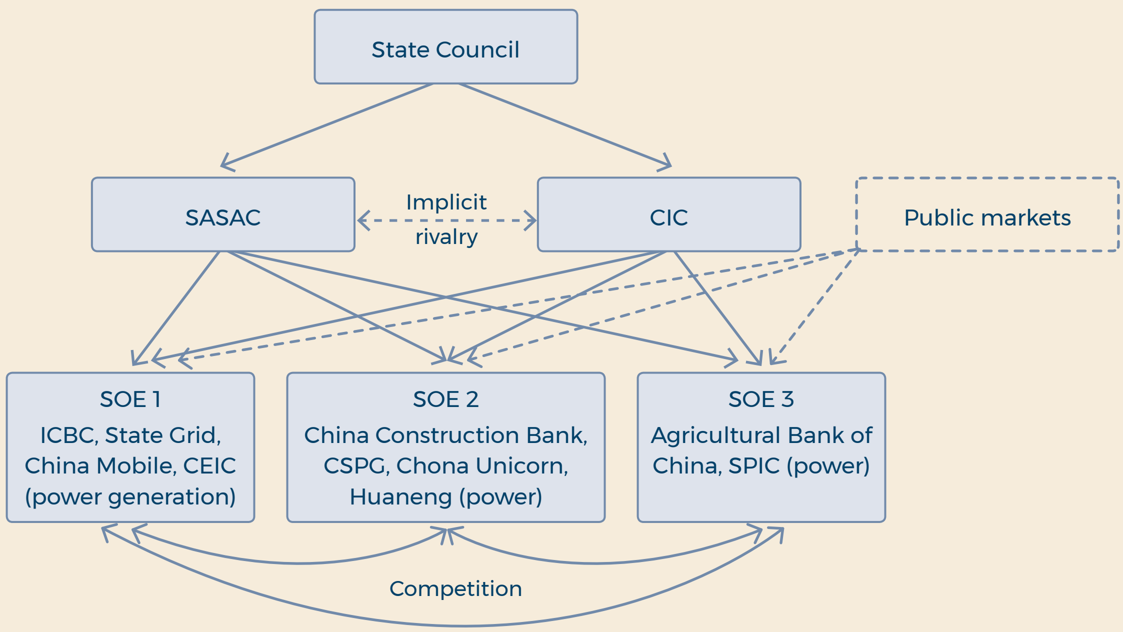
SASAC and the CIC report to the State Council as a whole, not to a single person or minister. An attempt to capture them from above would have to capture most of the cabinet, not just the appointment power of a single position or other single leverage point. In addition, the breadth of their oversight and the size of China mean an attempt at capture from below would have to assemble a dauntingly large coalition. The existence of both the CIC and SASAC, while they have different mandates at present, also means that if one were captured and had a sharp deterioration in performance, the other might make a bid to take over part of its portfolio.

17 Li-Wen Lin and Curtis J Milhaupt, "We Are the (National) Champions: Understanding the Mechanisms of State Capitalism in China" (Columbia Law and Economics Working Paper No. 409, Peter A Allard School of Law, University of British Columbia, Vancouver, 2013); Dominic Barton and Mei Ye, "A Chinese View of Governance and the Financial Crisis: An Interview with ICBC's Chairman", *McKinsey Quarterly*, March 2019.

Finally, SASAC and the CIC are prestigious and have attracted highly qualified personnel. In their early years both drew heavily on the elite reformist networks among top-ranked officials, as well as members of the Chinese diaspora returning home. They offer higher salaries than normal government institutions, at least at the mid-tiers. At senior levels, their leaders in fact earn less than many of their juniors because they are part of the elite Party personnel system, which has fixed grades. They are motivated to join, and to stay, by what they can do. They may give up some (or perhaps a great deal of) material gain for the prospect to contribute. It is unlikely that they would do so if SASAC and the CIC were less autonomous and empowered, or more encumbered.

A schematic of the oversight system is given in Figure 3. It is important to remember the sheer scale and variety of SOEs in China, and that their evolution has come in waves – in some sectors having barely begun. But the pattern overall is that competition on the ground, among SOEs, supports monitoring and governance by SASAC and the CIC (as well as public markets), and those organisations in turn mitigate the ability of the SOEs to capture the system around them. Those factors may, in part, be why China's five large power generation SOEs have each built more generation capacity than all of Africa in the last two decades, and why China's state sector is both larger, and has grown faster, than all of India's private sector (or of India's entire economy).

Figure 3 The SOE oversight system in China



Source: Author

Conclusion: Lessons and recommendations

As noted in the introduction, much of China's experience with SOE reform will be hard to replicate. Yet careful attention to how China has put its attributes to work provides at least some lessons that may be useful in African contexts.

Capacity: State capacity to initiate and manage entity reorganisation is crucial. It has come to seem almost a matter of course in China to divide or reorganise an SOE with 100 000 employees and billions of dollars of assets. Of course, there are difficulties beneath the policy documents, and reorganisation can happen too often, but the process occurs repeatedly. In most other governance systems, a single reorganisation takes years just to produce a consultant report.

The Chinese state's ability to move around large-scale organisations did not descend from the heavens. It has been constructed and is now a routinely used muscle of governance. One source of that capacity is diffused experience. During their career, every senior leader and senior official across China's government has likely overseen or been part of a restructuring process at least once. Another source is the consciously constructed ability to use external knowledge effectively. It may have been bruising for those inside it, but managing more than 1 000 professionals over 18 months to deliver almost on time is a feat. In the 1980s and 1990s, China consciously built the ability to manage development agencies, particularly the World Bank.[18] It built a similar ability to manage sources of commercial expertise.

African governments can construct a similar capacity, even if in ways suited to their own institutional make-up, and with many spill-over effects. The general capacity to manage external knowledge and technical advice can be put to work with elite consultancies and banks as well as traditional development agencies. It might be particularly useful for African countries today in engaging with China itself. The capacity building in question is not a matter of a workshop or appointing a minister with an elite CV, but requires the construction of highly skilled permanent teams with the right reporting lines and the right internal structure.

Compensation for harm: The people harmed by SOE reform must be compensated in durable and concrete ways. They must be given assets and income opportunities. Lip-service commitments to retraining are not credible. Spin and sophistry that they will not be harmed is even worse. Chinese workers were given their homes as their private and unencumbered assets, and a new ministry was created to find them jobs. Laid-off managers found a wealth of policy instruments enabling them, legally or sometimes illicitly, to turn their skills and connections into new firms and opportunities.

18 Pieter Bottelier, "China and the World Bank: How a Partnership Was Built", *Journal of Contemporary China* 16, no. 51 (2007): 239–258.

Such action requires some capacity for coordination, but that should not be overstated, or used as an excuse. Much of the peak SOE reform period looks coherent only in hindsight; specific actions were extremely uncoordinated in many instances and political contestation was intense. The system privileged energy over efficiency. But the energy was within an overall strategic conception that treated asset-based and income-earning compensation for those harmed by reform as a top-level priority. A few training programmes do not cut it.

Institutional design: The details of institutional design matter. It is not very helpful either to say that regulatory agencies will always be captured or to pretend that capture is easily mitigated. It is necessary instead to do the work of considering in detail the appointment power over an agency, its reporting lines, its internal balances and external checks, and the trade-offs of efficiency and robustness. That is an art more than a science, requiring a great deal of experience with the reality of how formal processes and informal power interact. It is not a job for outsiders, no matter their pedigree, but must be led by people with the necessary lived experience.

The meta-capacity to manage reorganisation, first-level priority for those harmed, and attention to the nitty-gritty of institutional design and its interaction with power: if these three lessons are not learned, replicating almost any aspect of Chinese reforms may do as much harm as good. For example, setting up an equivalent of the 'Organisation Bureau' to independently manage the evaluation and promotion of senior SOE managers will likely just be captured, and become a source of patronage and corruption. Bringing in advisors will result in much expense and wasted time. Dividing SOEs up into competitors may result in even more inefficient cartels. State building must precede the reform of state ownership if it is to be done at scale.

Tactical opportunities: Opportunities for state building and reform at scale are rare, and some lessons can still be learned for more tactical and incremental change.

Where there are obvious and low-hanging opportunities to increase competition among SOE managers, seize them. The obvious candidates here are in power generation, road transport and construction, where assets are easily separable and regulation can make performance easily comparable. In Africa, one subtle strategy may be to mandate infrastructure SOEs to pursue investments in other markets on the continent, and then use comparative performance across them to monitor performance. This will require a substantial enough presence in other countries, or across the continent, for management performance to be comparable. It may become more feasible if the African Continental Free Trade Area leads to greater integration, especially in connective infrastructure.

In addition, when pursuing a partial IPO of an SOE, seek a listing on a quality global exchange and the investment of a global leader in the industry. Doing so will make a substantive improvement in governance and management more likely, even if local exchanges (as is now the case in some African markets) have significant capital. An SOE partially listed on a local exchange, with its shares mostly owned by local banks or local financial institutions, will find it much easier to undercut attempts at oversight.

Finally, avoid having SOEs report either to their sectoral ministries or to a single ministry. Doing so will make capture from above or below likely. Create a highly capable intermediary, exempt it from standard government staffing constraints at its mid-tiers, and have it report to an entity (preferably cabinet) rather than a person. If possible, create two such entities, with different poles and bases of power. In an African context, that might mean having one entity report to a parliamentary committee (for example, that on finance or an infrastructure sector), and the other to cabinet as a whole.

Most of all, if a window opens for reform, and at least some preconditions are in place, take full advantage. When the window opened in China in the late 1990s, the SOEs listed were among the giants. While the seed of capacity must exist first, if it does, large-scale reform and listings conducted at a rapid, though not irresponsible, pace can provide a forcing device that helps spread capacity and signal direction.

The ultimate lesson is to see the question of SOE governance as an evolving system. China's SOEs have been in a 'reform' phase as often as not, and its system of SOE governance is in flux as often as it is stable. In many countries, SOEs will be among the largest entities in an economy and providers of critical public goods. Their governance and reform are enormously complex with enormous stakes. Approaching such a subject with simple ideas and preconceptions is a recipe for the kind of failure witnessed across regimes of dogmatic privatisation and dogmatic state ownership, or even those that simply lurch from one desultory stake sale to another. Systems of such scale and consequence require the hard work of continuous learning and evolution in practice, more than empty battles of rhetoric.

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Cover image

Night falls on the Beijing Central Business district buildings (ispyfriend via Getty Images)

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