State Elite Capitalism: How Transnational Financial Elites Managed Political Elite Conflict over State-Owned Enterprise Reforms in Post-Mao China

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Abstract

This article addresses a central puzzle in China's post-Mao economic reforms: why, amid intense political conflicts over state-owned enterprise (SOE) reforms, Chinese political elites ultimately endorsed a model of state elite capitalism—centered on state shareholdership through state-led corporatization and elite-led financialization—rather than privatization as seen in most other former socialist economies. Drawing on major SOE reforms in 1978-1998, (1) expanding enterprise autonomy (1978–1982), (2) tax-for-profit reforms (1983–1986), (3) the contract responsibility system (1987–1991), and (4) the liberal shift toward state shareholdership through state-led corporatization and financialization (1992-1998), the analysis reveals that three existing elite conflict theories—manipulative brokerage, situational conflict, and ideological divergence—effectively explain the adoption and dynamics of the first three reform models during 1978–1992. However, these theories do not fully account for the repeated failure of those models to generate a broad political elite consensus or achieve lasting success.

To resolve this gap, the article introduces a novel model of "transnational elite consensus" to explain the development of state elite capitalism. It demonstrates how transnational financial elites—through their expertise, global legitimacy, and interactions with Chinese policymakers—played a pivotal role in forging alignment among fragmented political elites. This transnational influence facilitated convergence on state shareholdership as a viable compromise, enabling the preservation of state control while incorporating market-oriented international norms.

The resulting trajectory diverged from China's economic reforms in ways that most other post-socialist states did not. Instead, it is a distinctive form of state elite capitalism: the state retained control over key enterprises through financialization under transnationally politically embedded bankers (TPEBs), including domestic and external advisors from the World Bank, Wall Street, and Hong Kong. This explanation highlights the interplay between elite politics and financial elite networks in shaping China's unique reform outcome, offering new insights into the resilience and adaptation of state capitalism in a reforming socialist economy.

Extended Abstract

China's post-Mao state-owned enterprise (SOE) reforms from 1978 to 1998 represent a profound and enduring puzzle in the study of economic transitions: why, in the face of protracted and intense conflicts among domestic political elites over the restructuring of SOEs, did Chinese leaders ultimately coalesce around a distinctive model of **state elite capitalism**—one prominently featuring a mix of state shareholdership in state-led corporatization, and elite-led financialization—rather than embracing the more radical, privatization-heavy paths that characterized neoliberal reforms in the majority of other former socialist economies during the same era? This outcome not only preserved significant state control over key economic assets but also integrated market-oriented mechanisms in a way that diverged markedly from global trends, highlighting the unique interplay of domestic elite politics (Zhang, 2021) and international influences in shaping China's reform trajectory.

To address this puzzle, the article draws on empirical evidence from four major SOE reform efforts spanning 1978 to 1998. These phases illustrate the evolution of SOE reforms: (1) the initial push for expanding enterprise autonomy (1978–1982), which aimed to loosen central planning constraints; (2) the tax-for-profit reforms (1983–1986), designed to standardize revenue extraction from enterprises; (3) the widespread adoption of the contract responsibility system (1987–1991), which sought to delineate rights and responsibilities through contractual arrangements; and (4) the pivotal liberal shift toward state shareholdership (Wang, 2015, 2019) via state-led corporatization and elite-led financialization (1992–1998), which entrenched a hybrid system blending state dominance with elite-led corporate governance.

The analysis demonstrates that three established theories of elite conflict—**manipulative brokerage**, **situational conflict**, and **ideological divergence** (Zhang & Shi, 2024)—provide robust explanatory power for the origins, adoption, and internal dynamics of the first three reform models during the period from 1978 to 1992. However, these frameworks fall short in accounting for a critical pattern: the recurrent failure of each of these early models to secure broad, sustainable consensus among political and economic elites or to deliver enduring economic success in SOE reforms. Each phase, despite initial promise, unraveled due to inherent limitations—such as unchecked bargaining in the autonomy phase, persistent distortions in the tax-for-profit system, and short-term behavioral incentives under contracting—that prevented the formation of a stable elite alignment.

To bridge this explanatory gap and resolve the overarching puzzle, the article advances a novel theoretical contribution: the **"transnational elite consensus" model**. This framework posits that **transnational financial elites**, operating through their specialized expertise, global institutional legitimacy, and direct engagements with Chinese policymakers, served as crucial mediators in resolving entrenched domestic elite fragmentation. By promoting state shareholdership as a pragmatic compromise, these elites facilitated a convergence that allowed for the retention of core state control while selectively incorporating market-driven elements, corporate governance principles, and

adherence to international financial standards. This process not only differentiated China's SOE reforms from the privatization-dominant strategies in other post-socialist states but also solidified a resilient form of state capitalism, wherein the state maintained dominant ownership stakes and strategic oversight over pivotal enterprises, all within a more formalized, corporatized, and financially integrated structure overseen by transnationally politically embedded bankers (TPEB; as conceptualized by Sun & Mallard, 2025). Key actors in this network included domestic economic elites and external advisors from the World Bank, Wall Street financial institutions, and Hong Kong-based capital market experts.

The "transnational elite consensus" explanation underscores the dynamic interplay between internal elite politics and external ideational and financial networks, offering fresh analytical insights into the mechanisms that underpin the persistence and adaptive evolution of state capitalism within a reforming socialist economy. Below, each reform phase is examined in detail, including the rationale for the relevant elite conflict theory, the reasons for excluding alternatives, the core empirical evidence, and a concluding summary. This is followed by an in-depth account of the World Bank's evolving perspectives, suggestions, and participation levels across the phases, which exemplifies the transnational dimension.

1. **Expanding Enterprise Autonomy Phase (1978–1982) → Best Explained by the "Manipulative Brokerage" Theory**
    - **Why Not Ideological Divergence or Situational Conflict?** During the initiation of this phase (1978–1979), ideological constraints from the "Two Whatevers" (两个凡是) doctrine lingered, yet high-level elites had already formed a basic consensus on the necessity of reform, minimizing fundamental ideological rifts. Similarly, while the economy teetered on the brink of collapse, the acute "fiscal pressure" as a situational driver did not yet dominate; the true fiscal crisis only became pronounced in the early 1980s. Thus, neither deep-seated ideological splits nor immediate contextual crises fully capture the phase's dynamics.
    - **Core Evidence:**
        - **Local Actors as Primary Brokers:** The Sichuan Provincial Committee, under Zhao Ziyang, functioned as a quintessential "grassroots broker." Rather than awaiting centralized directives, it proactively selected six enterprises for pilot trials, translating enterprise demands for "loosening bonds" (松绑) into actionable local policies and demonstrating innovative approaches to autonomy.
        - **Media as a Brokerage Instrument:** In 1979, the Ningjiang Machine Tool Factory published an advertisement in the People's Daily soliciting orders

outside the state plan. This strategic use of a national media platform—a "super broker"—directly disseminated the message of enterprise autonomy to society at large and key decision-makers, generating powerful demonstration effects and exerting upward pressure for broader adoption.

    - **Central Adoption and Transformation Process:** The State Economic Commission subsequently synthesized and refined experiences from Sichuan and other locales, converting them into nationwide policies such as the "Several Provisions on Expanding the Operational and Management Autonomy of State-Owned Industrial Enterprises." This exemplifies a classic brokerage sequence: local innovation (broker discovery) → central acknowledgment (broker integration) → national dissemination (broker amplification).

  - **Conclusion:** The expansion of enterprise autonomy was fundamentally a reform driven by local and enterprise elites acting as "brokers," who skillfully "marketed" and elevated grassroots innovations and demands into formalized national policies, leveraging networks and platforms to navigate and influence the political hierarchy.

2. **Tax-for-Profit Reforms Phase (1983–1986) → Best Explained by the "Situational Conflict" Theory**

  - **Why Not Ideological Divergence or Manipulative Brokerage?** The tax-for-profit initiative primarily involved technical fiscal adjustments, without delving into core debates over public versus private ownership, thus diluting its ideological intensity. While the Ministry of Finance played a leading role, this was not the result of individual or factional "manipulation" but rather a predictable response rooted in departmental mandates and responsibilities.

  - **Core Evidence:**

    - **Direct Trigger from Fiscal Pressures:** By 1982–1983, the prior autonomy expansions and profit concessions had led to the "two proportions" declining sharply—the ratio of state fiscal revenue to national income and central fiscal revenue to total fiscal revenue—creating a severe situational crisis that necessitated reform to stabilize government finances.

    - **Conflicts Driven by Departmental Functions:** The Ministry of Finance advocated for tax-for-profit to fulfill its statutory duty of safeguarding national revenue streams. In contrast, enterprises and the State Economic Commission system resisted or passively complied with adjustment taxes, prioritizing production quotas and worker welfare. These clashes stemmed not from differing ideological convictions but from the distinct positions, incentives, and performance metrics within the economic apparatus.

- **Micro-Level Situational Dynamics in "One Household, One Rate":** The adjustment tax mechanism, tailored to each enterprise's historical "base," vividly illustrated situational conflict at the grassroots level. Negotiations between Ministry of Finance representatives and enterprise delegates over base figures represented a direct, context-specific bargaining process shaped by immediate operational realities.

- **Conclusion:** The tax-for-profit phase emerged as an inevitable response to the acute situational pressure of declining fiscal revenues, with conflicts arising organically from the functional roles and interests of various departments within the economic chain, rather than from premeditated brokerage or abstract ideological battles.

3. **Contract Responsibility System Phase (1987–1991) → Best Explained by the "Ideological Divergence" Theory**
   - **Why Not Situational Conflict or Manipulative Brokerage?** Although elements of manipulative brokerage (such as Shougang's Zhou Guanwu engaging in lobbying efforts) and situational pressures (like the 1986 industrial downturn) were present and contributed to the system's promotion, these factors ultimately served as enablers or manifestations of a more profound underlying ideological contest, rather than defining the phase independently.
   - **Core Evidence:**
     - **Fundamental Debates on Reform Direction:** By the mid-to-late 1980s, elite factions crystallized into two major ideological camps: the "contract system faction," which believed that public ownership could be revitalized through contracts clarifying rights, responsibilities, and benefits without altering ownership structures, reflecting a faith in "two-rights separation" under socialism; and the "shareholding system faction," which argued that contracting failed to address short-termism and government-enterprise entanglement, advocating instead for property rights reforms to establish "clear ownership" as essential for modern enterprises.
     - **Ideological Labels and Advocacy Figures:** Prominent intellectuals embodied these divides, such as Li Yining, dubbed "Li Shares" for his promotion of shareholding, and Yang Peixin, known as the "father of the contract system," who authored works defending it. Their public debates transcended specific policies, escalating to broader ideological questions

about "whither China's reforms" and the envisioned future societal blueprint.

    - **Political-Level Ideological Contestation:** The high-level decision in 1987–1988 to universally promote the contract system represented an endorsement of one ideological strand, while the post-1989 reflections and hesitations on more market-oriented explorations like shareholding highlighted the dramatic political manifestations of these divergences.

  - **Conclusion:** At its core, the contract responsibility system phase involved heated disputes over the essence of reform—"whether to reform, what to reform, and how to reform"—which boiled down to clashing ideological visions and blueprints for China's socio-economic future. Situational and brokerage elements acted merely as catalysts or surface expressions of this deeper ideological schism.

4. **The Liberal Shift Toward State Shareholdership Through State-Led Corporatization and Financialization (1992–1998) → Best Explained by the "Transnational Consensus" Model**

Why the Earlier Elite Conflict Theories (Manipulative Brokerage, Situational Conflict, and Ideological Divergence) Fail to Explain This Phase

By the early 1990s, the prior models had exhausted their explanatory power for the decisive turn toward state shareholdership. Manipulative brokerage (e.g., lobbying by individual firms or local leaders) persisted in some forms but could no longer account for the systemic, nationwide convergence on corporatization and financialization, which required bridging deep, longstanding domestic elite fractures across ideological lines and departmental interests. Situational conflict—driven by acute fiscal crises, industrial slumps, or short-term pressures—had propelled earlier shifts (e.g., tax-for-profit amid "two proportions" decline or contracting during 1986 downturns) but failed to resolve the repeated breakdowns of those models or generate lasting consensus; the 1990s shift occurred amid relative stabilization post-1992 Southern Tour and 14th Party Congress, not a singular overwhelming crisis. Ideological divergence, while still simmering (e.g., lingering debates over property rights vs. public ownership), no longer dominated as the primary driver; the emerging model offered a pragmatic "third way" that depoliticized operations without full privatization, sidestepping the binary ideological clashes of the contracting era. These domestic-centric theories thus cannot explain why fragmented elites ultimately aligned on a hybrid state capitalism path that preserved core state control while embracing market mechanisms, corporate governance, and global financial integration—precisely where transnational influences filled the gap.

Core Evidence Supporting the "Transnational Consensus" Model

The phase's dynamics are best captured by the "transnational consensus" model, wherein transnational financial elites—through sustained expertise, global legitimacy, and direct policy interactions—mediated domestic elite conflicts and forged alignment around state shareholdership as a viable compromise. This process is vividly illustrated by the World Bank's evolving role across all reform phases, serving as a continuous transnational thread:

Expanding Enterprise Autonomy and Profit Retention (1978–1982) — Observer/learner: Restored seat in 1980, president's 1981 visit; cautious optimism on decentralization but critique of plan-bound limits; early 1985 report ("China: Long-Term Development Issues and Options") urged market principles beyond administrative tweaks; minimal participation (surveys, reports).

Tax-for-Profit (1983–1986) — Active fiscal advisor: Close ties with Ministry of Finance/State Economic Commission; supported shift to taxation for normalized relations but harshly criticized "adjustment tax" for violating uniformity and entrenching soft budgets/vested interests; suggested uniform corporate income tax + price reform; moderately deep involvement via surveys, technical assistance, seminars influencing scholars (e.g., Lou Jiwei).

Contract Responsibility System (1987–1991) — Sharp critic/detached observer: Specialized enterprise/financial studies; opposed contracting as "backward-looking" (historical bases) vs. "forward-looking" market competition; economists (e.g., Peter Harrold) highlighted reinforced negotiations, short-termism, neglect of investment/innovation, bank bad-debt risks from "profits guaranteed, losses not covered"; urged corporatization/shareholding, modern governance, competition, bankruptcy; superficial engagement (academic exchanges) with limited policy impact, as contracting was a political choice amid slumps/fiscal woes.

Shareholding Pilots and Modern Enterprise System (1988–early 1990s brewing, full adoption post-1993) — Deeply embedded promoter, augmented by Wall Street and Hong Kong elites: As contracting flaws mounted and post-14th Party Congress (1992) socialist market economy aligned with Bank views, the Bank became a behind-the-scenes architect. Firmly advocated shareholding for clear property rights, genuine separation, robust governance (not mere fundraising but structural overhaul, echoing "legal person governance structure"). Deep participation included: influential "China: State-Owned Enterprise Reform" report (circa 1996) diagnosing issues and proposing classified reforms, social security, stripping social functions—aligning with "grasp the large, let go the small"; technical assistance projects aiding restructuring/listings with international banks/accounting firms; Company/Securities Law workshops providing templates on shareholder rights, disclosure, independent directors (1993 Company Law drafting onward); profound role in 1990s social security frameworks, supporting layoffs via "China: Pension System Reform" report (1997) shaping pooled + individual accounts.

This was further reinforced by transnationally politically embedded bankers (TPEB; Sun & Mallard, 2025): Wall Street elites (e.g., Gao Xiqing and Chen Boming from "Joint Office"/联办 precursors, leading Company/Securities Law revisions and integrating into CSRC to drive reform implementation); Hong Kong capital market advisors (e.g., Hong Kong Stock Exchange Chairman Li Guowei advising Zhu Rongji during Shanghai mayor/party secretary tenure to establish Shanghai Stock Exchange; New World Securities—Hong Kong's largest investment bank—advising Li Hao [former secretary to reformist vice-premier Gu Mu] during Shenzhen mayor/party secretary tenure to establish Shenzhen Stock Exchange). Broader international capital provided decisive support: global banks (especially Wall Street majors) acted as primary sponsors, financial advisors, and cornerstone investors in SOE IPOs/listings; foreign mutual funds widely subscribed to these shares, gaining deep benefits and embedding global norms/liquidity into the process. This transnational network bridged domestic divides by offering globally legitimated "third way" expertise: state control retained, yet depoliticized via boards, share structures, listings, and international standards—addressing prior models' failures (discipline deficits, distortions, short-termism) without privatization's political risks.

Conclusion

The 1992–1998 shift crystallized China's distinctive state capitalism, where the state retained dominant ownership and strategic guidance over key enterprises within a corporatized, financially sophisticated framework. The "transnational consensus" model illuminates how global financial elite networks—exemplified by the World Bank's phased evolution from observer to deep collaborator, Wall Street/Hong Kong advisors' direct policy embedding, and international capital's IPO sponsorship/subscription—interfaced with domestic politics to forge elite alignment on this hybrid path. This transnational mediation enabled a unique adaptation that preserved socialist-state legacies amid market integration, diverging from privatization-dominant post-socialist trajectories and yielding broader insights into state capitalism's resilience in reforming command economies.