The Performance of SOEs in China: An Empirical Analysis of Ownership Control through SASACs

Professor Sea-Jin Chang
Corporate Governance of Asian firms

- Family firms
  - Family as a controlling shareholder
  - Family owners and management
  - Family business associations and service providers (e.g. FBN, private banking)

- Listed firms
  - Listed firms in groups
  - Investors & NGOs
  - Industry associations (e.g. SID, ACGA, CIMA, CFA, etc.)
  - Service providers (e.g. KPMG, SGX etc.)
  - Regulatory agencies and governments (e.g. SGX, MAS, OECD)

- Government linked listed companies
  - Government owned enterprises
  - Government linked listed companies
  - Governments
  - Sovereign wealth funds (e.g. Temasek, SASAC)

- Dispersed Ownership
  - State as a controlling shareholder
For more information, the 2014 report can be downloaded from CGIO website: https://bschool.nus.edu.sg/cgio
GLCs in Singapore

- Government-linked companies (GLCs) represent 37% of the stock market value in 2013.

- Two representative SWFs are Temasek and GIC.
Temasek Holdings

Legend:
- GLCs
- GLREITs

Sources: 2012 Annual reports of GLCs and GLREITs.
Investment Performance

Growth
Temasek’s portfolio market value increased 300% over the past 20 years.

Active Investor
Temasek invested S$159 billion and divested S$100 billion over the last decade.

Shareholder Return
Temasek’s 20-year Total Shareholder Return (TSR) was 2.5 times MSCI Singapore in 2012.

International Portfolio
Non-Domestic Ownership of Assets increased 22% over the last decade.

Comparison of Governance Practices: GLCs vs NON-GLCS

Board Independence
GLCs have **higher** percentage of independent directors on their boards.

![Percentage of independent directors](chart)

**External Board Appraisal**
GLCs hire **more** external consultants to conduct board appraisals.

![Number of external consultants](chart)

**Chairman Independence**
GLCs have **higher** percentage of Boards led by an independent/non-executive chairman.

![Percentage of independent chairmen](chart)

**Risk Governance**
GLCs are **more likely** to have a Board Level Risk Committee.

![Percentage of risk committees](chart)

Note: Analysis based on data from CGIO’s GTI 2009-2013.
A billion dollar question: Can the Singapore model be replicated in China?
THE PERFORMANCE OF STATE OWNED ENTERPRISES IN CHINA:

An Empirical Analysis of Ownership Control through SASACs

SIA JIN CHANG | SANDY YUAN JIN

Current CIMA - CGIO report on SOE reforms in China
SOE Reforms in China

Since its “Reform and Open Door Policy” of 1979, the Chinese government sought to reform its staggering state sector.

- The Company Law was enacted in 1993. SOEs transformed into limited liability firms or joint stock companies, with state ownership converted to shares.
- The SOE reform in 1995 with slogan, “Keep only large firms and let small ones go”.
- Private firms were legalized in 1997.

- SASAC (State-owned Assets Supervision and Administration Commission of the State Council) was established in 2003, modeled after Temasek.
  - Central SASAC controlled 197 (106 as of 2016) key companies. Provincial governments created their own local SASACs.
Ownership Structure of Chinese SOEs


- Information on top 10 shareholders of these firms in the CSMAR database.

- The Company Law defines an immediate shareholder with more than 50% ownership or with enough voting rights to significantly affect company decision making.

- The ultimate shareholders are owners of these immediate shareholders.
The proportion of SOEs among listed firms has been declining...

Figure 1: Number of SOEs 2003 - 2013
Surviving SOEs are large, representing more than 50% of market capitalization.

Figure 2: SOEs' Market Capitalization 2003 - 2013
Typical Ownership Structure

Figure 3. The Ownership Structure of Shenzhen Properties & Development in 2013

100%

Ultimate Controller

Immediate Controller

In average, 2.6 layers of ownership in listed firms

Shenzhen SASAC

Shenzhen Investment Holdings Company Limited

Shenzhen Properties & Resources Development (Group) Ltd.
Ownership Stakes of Immediate Controllers

Figure 9: Average ownership stake of immediate controllers
Composition of Immediate Controllers

A large portion of immediate controllers are SOEs
Ownership Stakes of Ultimate Controllers

Year:
- 2003: 39.78%
- 2004: 35.96%
- 2005: 34.12%
- 2006: 30.56%
- 2007: 30.80%
- 2008: 31.48%
- 2009: 32.58%
- 2010: 34.62%
- 2011: 35.09%
- 2012: 35.58%
- 2013: 35.70%
Composition of Ultimate Controllers

Local and central SASACs are ultimate controllers in more than 30% of listed firms, but they are not their immediate controllers. In other cases, ultimate controllers are governments or SOEs.

Figure 10: Composition of ultimate controllers
Comparison between Temasek and SASACs

**Temasek**
- Temasek is a commercial company, under the Singapore Company Act, paying taxes and dividends as well as having its own board.
- Its sole shareholder is MOF but the Ministry guarantees the integrity of board. Singapore separates the government’s shareholder role from its regulatory and policy making functions.
- Run by a professional management team. Makes commercial decisions.
- Temasek directly involves with appointing CEOs and Boards.

**SASACs**
- State assets are much larger. SASACs own listed firms indirectly through SOEs.
- SASAC is a government agency, an arm-length regulatory body representing the government.
- Run like a government branch. CEOs and board members of SOEs have political titles and ranks.
- Designate their functions as Bureaus. All staffs are government officials.
- CEOs of SOEs are appointed by the Party’s Central Committee, not by SASACs.
Financial Performance of Listed Firms

Financial performance of publicly listed firms in China

<table>
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<th>Dependent variables</th>
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<tr>
<td><strong>Immediate controllers</strong></td>
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<td>Local SASACs</td>
<td>-0.328</td>
<td>-0.080</td>
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<td>SOEs</td>
<td>-0.980**</td>
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<td>Governments</td>
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<td>-0.329**</td>
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<td>(0.800)</td>
<td>(0.094)</td>
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<tr>
<td>Financial institutions</td>
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<td>0.376**</td>
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<td>(0.741)</td>
<td>(0.087)</td>
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<td>Individuals</td>
<td>0.834**</td>
<td>-0.296**</td>
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<td>(0.189)</td>
<td>(0.022)</td>
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<tr>
<td><strong>Ultimate controllers</strong></td>
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<td>Local SASACs</td>
<td>-0.358</td>
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<td>Central SASACs</td>
<td>-0.790*</td>
<td>0.180**</td>
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<td>SOEs</td>
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<td>Individuals</td>
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<td>(0.302)</td>
<td>(0.035)</td>
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SASAC ownership does not improve firm performance
### Control variables

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<tr>
<th>Variable</th>
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<tr>
<td>Firm size</td>
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<td>(0.051)</td>
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<td>Firm age</td>
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<td>Fixed asset intensity</td>
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<td>(0.367)</td>
<td>(0.367)</td>
<td>(0.043)</td>
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<td>Intangible asset intensity</td>
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<td>-7.175**</td>
<td>0.219*</td>
<td>0.300**</td>
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<td>(0.844)</td>
<td>(0.845)</td>
<td>(0.099)</td>
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<td>Leverage</td>
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<td>(0.158)</td>
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<td>Constant</td>
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<td>(1.210)</td>
<td>(1.268)</td>
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- **Year fixed effect**: Yes
- **Industry fixed effect**: Yes
- **Observations**: 19039
- **Number of firms**: 2501
- **Adjusted R-squared**: 0.153

Note: Standard errors in parentheses. ** p<0.01, * p<0.05, + p<0.1
Conclusion

- Unlike the Singapore case, SASAC affiliated companies are underperforming, although not so poorly as those under direct state ownership.

- Future SOE reform in China should focus on reducing layers in pyramid ownership structure so that SASAC can function as active shareholder.

- Temasek is run like a private investment firm with own Board and CEOs, and hires people from private sector. SASACs are mainly staffed by bureaucrats. SASACs do not get involved with CEO appointment of portfolio companies.

- Clean government, transparency, and meritocracy would be needed.

- Make SOEs compete with others. See examples like Temasek vs. GIC. SMRT vs. Comfort, Singtel vs. Starhub.