

**ENTERPRISE MANAGEMENT IN
CHINA'S TRANSITIONAL
ECONOMIES**

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Abstract

This paper is focused on changes in Chinese enterprise management during the transition from a centrally planned economy to a socialist market economy. It reviews the management evolution in the industrial sector during Mao's regime (1949-78) and the revolution of management system and practices since the post-Mao economic reforms (1979 onwards). The impact of the Maoist Chinese model and economic reforms on the evolution and revolution of Chinese enterprise management is analysed and its implications for international business are briefly discussed.

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INTRODUCTION

Since the People's Republic of China (PRC) implemented an open-door policy and commenced its economic reforms in the late 1970s, it has attracted business people over the world to tap into its underdeveloped market. Foreign direct investment (FDI) in China, for example, increased by an annual average of 215 percent during 1985-94 (World Bank, 1996: 27-28). Now China is ranked only second to the US as a global destination for FDI (Walker & Ridding, 1996). The escalation of FDI in China has resulted in more foreign managers being assigned to work in their parent firms' subsidiaries in China. This has thus raised questions about management practices in China. As Schermerhorn and Nyaw (1990: 19) have argued that "China's past holds too great a grasp on its present and future", it is necessary to understand the traditional management systems and practices before comprehending current management. This paper intends to examine Chinese management systems and practices in the industrial enterprises during both Mao's regime (1949-78) and the post-Mao economic reforms (1979 to date). The systematic examination reflects the impact of the Maoist model on the formulation of pre-reform enterprise management practices, and also highlights how the reforms have facilitated the management revolution. The paper concludes with a brief discussion on the implications of such changes for international business.

Enterprise Management During Mao's Regime (1949-78)

After the PRC was founded in 1949, a Maoist Chinese model was developed and maintained until the commencement of economic reforms in the late 1970s (Jackson, 1992; Harding, 1987; Selden, 1993). The three major components of this model, as summarised by Dernberger (1982), included a Stalinist 'big push' development strategy; a centralised or command economic system; and the radical principles of Maoist ideology. The Stalinist big push development strategy, or "a leap forward type of heavy-industry-oriented development strategy" as specified by Lin, Cai & Li (1996: 19), was adopted by the government in the early 1950s to achieve the goal of rapid industrialisation. However, the heavy-industry centred strategy was not in harmony with China's initial economic endowment, as China's scarce capital and poorly developed economy could not support the extremely capital intensive heavy industries (Lin et al., 1996; Naughton, 1996). To reduce the conflicts between the capital-intensive heavy industry and the capital-scarce economy, a command economic system was subsequently established.

The command economy in China was characterised by two prominent features: central planning and public ownership (Lee, 1987; Chen, 1995). Central planning before the reforms, as noted by Riskin (1987: 9), refers to a particular form of central intervention. The central government set priorities and carried them out administratively by distributing materials and finances to enterprises and ordering output from them, especially state-owned enterprises. The central planning thus enabled the government to exert strong and direct control over industry and management, while the enterprises acted as basic production units to fulfil state plans. Public ownership, on the other hand, including state ownership of the means of production (mainly in the form of state enterprises) and collective ownership, reflects the control of state institutions over enterprises (Pu, 1989; Hay, Morris, Liu & Yao, 1994). This control includes "the contractual power to determine who will comprise the management and their remuneration, and the right to determine the allocation of residual gains and losses" (Hay et al., 1994: 424). The ownership structure "allows the state to maintain direct-authority relations over most of its output" and "permits a command system to function unimpeded" (Naughton, 1996: 29). The nature of public ownership also moulded the enterprise into a basic social unit or a mini-society that had to take on various social responsibilities (Walder, 1986; Lin et al., 1996).

The adoption of the heavy-industry oriented development strategy resulted in the development of a command economic system. Under this system, the state ownership of most productive resources guaranteed the government control of resources, and a highly centralised planning apparatus enabled direct steering of resources to planners' priority uses. As a result, the state ownership structure was consolidated and state-

owned enterprises became dominant in the industrial sector (Lin et al., 1996; Naughton, 1996). In 1978, state ownership accounted for 77.6 percent of gross industrial product, with collectives accounting for the remaining 22.4 percent (Statistical Yearbook of China, 1993). In the context of such a centralised planning system and public ownership, the major features of management practices differed significantly from those defined in advanced Western market economies.

Hay et al. (1994) have noted that in the West, ownership and resource co-ordination that is conducted by management are more distanced from each other. While the ownership function of shareholders of a firm appears to be purely that of residual risk-bearing, the management is given full control of the operation of the firm. "The defining characteristic of management [in the West] is that it co-ordinates the contracts and the activities they specify, hence management is the immediate manifestation of the 'conscious power' which determines resource allocation, production, and distribution" (Hay et al., 1994: 424).

In contrast, neither the state institutions which effectively exercise the ownership function of enterprises in China nor the managers of the enterprises had sufficient incentive to be efficient because neither of them bore residual risk (see Hay, et al., 1994: 426 for the allocation of residual risk by state institutions). This was because central planners "created a system in which property rights were vague or non-existent", so they could have maximum discretionary control (Naughton, 1996: 30). Without assuming any risk and having no right to allocate residual profits or losses, Chinese managers did not have any incentive to pursue efficient, profit-maximising strategies in their production and distribution activities (Hay et al., 1994; Liew, 1997). Chinese enterprise managers were thus not in an environment that stimulated them to carry out their supposed duties in full capacity (in a Western sense) and the "problems of managerial autonomy and accountability" became characteristic of state socialist economies including China (Child, 1990: 142).

While management had different features in China due to the economic system and ownership structure, it was also affected directly by politics and Mao's ideology (Lee, 1987; Riskin, 1987; Walder, 1986). Jackson (1988: 338) has pointed out that "management and labour policies have, throughout the history of the PRC, been subject to changes in the ideological stance of the Party leadership". Before the founding of the PRC, enterprises in the revolutionary base area (also called the liberated area) were managed by a 'three-man team' (*san-ren tuan*) composed of the factory director, Party secretary and union committee member (Xia, 1992: 587; Ye, 1991). Given that any Chinese trade union was in practice subordinated to Party authority, "the main shifts in enterprise leadership have been between the primacy of management and the Party, reflecting shifts between economic and political criteria" (Child, 1994: 59). These shifts were clearly observed during Mao's regime even though "the unity of political and economic leadership and Communist Party primacy" was adopted as the first management principle in the PRC's first industrial management handbook (Kaple, 1994: 61). These leadership shifts demonstrate the profound and lasting impact of politics, economics and ownership structure upon management policies and practices.

To examine the impact of politics and the economic system on management systems and practices during Mao's regime, it is necessary to divide Mao's era (1949-1976) into four periods (see details about the four periods in Lee, 1987: 115) so as to review management system and practices in each period. The first was in the period of economic rehabilitation and socialist transformation (1949-57), during which the One-Man management system was installed with an emphasis on material incentives and regulatory controls. The second occurred during the Great Leap Forward (1958-61) when management practices were dominated by Mao's 'proletarian line' that stressed the commanding role of the Party, the importance of political ideology and the leading role of the workers. The third, which was during economic readjustment (1962-65), resurrected the practices and policies of the first period and witnessed the implementation of the Seventy Articles for Regulations in Industry. The final period was during the Cultural Revolution (1966-76), which revived Mao's dominance and ended up eliminating the 'bourgeois line' advocated by Liu Shaoqi. These four periods of management systems and practices are reviewed in detail as below.

One-Man Management

In the early 1950s, a new regulation, Industrial Management Mechanism (*gongye guanli jizhi*), was proposed by the Communist Party of China (CPC or the Party hereafter). This document relied heavily on the Soviet management model, with adoption of the "One-Man management" system being one of its ten principles (see

Kaple, 1994: 62 for the rest of the principles). The One-Man (also called 'one-director' or 'one-boss') management system was initially introduced to North-East China after the CPC took over the region in 1948. A key figure was Gao Gang, the Party leader in the North-East area and first head of the State Planning Commission. The North-East region was the base of China's heavy industry and was greatly influenced by the Soviets due to the large number of Soviet aid projects. Gao claimed that the One-Man management system would enable separation of the state apparatus from the Party organisation, i.e. the factory director would be granted exclusive power over production and administration whereas the Party committee would just supervise and ensure the fulfilment of the production plan. Gao also believed that the system made it possible to have individual responsibility, division of labour and increased motivation (see Lee, 1987: 26-9). The implementation of the One-Man management system was officially approved by the Party Central Committee in 1953 along with the commencement of the first five-year plan (Andors, 1977; Zheng, 1987). Riskin summarised this management system as, a combination of 'scientific management' and a hierarchical 'responsibility system' of leadership. The former entailed the formulation of precise work plans for all phases of factory operations, and their translation into minutely specified job tasks. The latter put one person in complete control of each unit and level of a factory, with supreme authority vested in the plant director (1987: 45).

Under this management system, the factory director "was given unified authority over all activities within the factory, and took overall responsibility for fulfilling state plans and for factory production, finance and administration" (Child, 1994: 60). This enabled the chain of command to go vertically from the factory director down to production team leaders. It was believed that the system would suit central planning which required effective channels of command and an organisational structure that allowed for the smooth upwards and downwards flow of information (Schurmann, 1968). The system was reported to be highly efficient and conformed to the laws of economic development (Zheng, 1987), and produced "unity of command" (Schurmann, 1968: 262). Consequently, piece-rate wages and a bonus incentive system became popular as they fitted the control requirements of One-Man management (Andors, 1977; Laaksonen, 1988). By the end of 1952 slightly over one-third of all industrial workers were paid this way, and by 1956 about 42 percent of all industrial workers belonged to a piece-rate incentive system (Laaksonen, 1988: 199). To summarise, the key feature of the One-Man management system was, as noted by Lee (1987: 44-5), its "authority orientation", i.e. a highly rationalised and centralised system and an organic state socialism with both material and non-material incentives.

However, One-Man management was not favoured by the Party organisations as their doctrine was "the Party apparatus should directly manage industry" (Lee, 1987: 31). The system was also resisted by many Party cadres as they believed that "this system led to a diminution in the functions of the Party committee" (Schurmann, 1968: 263). Because of this resistance and a differential "pace of political consolidation and economic recovery" (Lee, 1987: 31), the system was not universally implemented by the time it was abolished. At the Eighth Party Congress in 1956, One-Man management was condemned officially for violating ideological principles favoured by Mao such as the supremacy of the Party and politics, and neglecting democratic management (Lee, 1987; Riskin, 1987; Zheng, 1987). The system was further reprimanded by official articles for its "reliance upon a minority of 'experts', material incentives, and excessive and unnecessary regulations" (Lee, 1987: 63). In addition to political and ideological reasons, other factors contributed to the abandonment of the system, including lack of professionally trained managers, lack of objective measurement for performance, and blind copying of the Soviet model without considering different national cultures and traditions (Andors, 1977; Laaksonen, 1988; Schurmann, 1968). A new system of industrial management, 'Director Responsibility System under the Leadership of the Party' (DRSULP), was recommended in a report to the Eighth Party Congress to replace the One-Man management system. The Congress hence called for universal implementation of the new system in industrial enterprises. The new system emphasised the combination of the Party's collective leadership and individual responsibility, with the Party as the core of the leadership (Zheng, 1987; Schurmann, 1968).

Management under Collective Leadership of The Party and The 'Two-One-Three' System

The adoption of the director responsibility system under the leadership of the Party (DRSULP) system in late 1956 represented a shift from individualism to collectivism, and from "centralism" to "democracy" (Schurmann, 1968: 291). This meant that while the factory manager was still responsible for everyday

operations and administration, all major decisions were to be made collectively by the factory's Party committee. Apart from this lateral shift of authority from managers to the Party, decision-making powers were also shifted downward from managers to workers at shop floor level to achieve "democratisation of management" (Kaple, 1994: 65). After the PRC was founded, many enterprises instituted workers' committees under the leadership of the Party, such as the Factory Management Committee and the Factory Employees' and Workers' Conference, to democratise management. These committees had played only a minimal role under One-Man management as they were inconsistent with the Soviet model (see Kaple, 1994: 66-71). However, in 1957 under the DRSULP system, the Factory Employees' and Workers' Conference (hereafter called the Workers' Conference) was encouraged to be revitalised to carry out Mao's "mass-line" or "mass-oriented style of industrial management" (Lee, 1987: 60), which meant "mass participation in enterprise management and supervision" (Child, 1994: 62).

With the launch of the Great Leap Forward in early 1958, the management system in industrial enterprises underwent rapid transformation. The changes were consistent with the ideological emphasis of the movement on "combating bureaucratism, blunting the distinction between mental and manual labour, and encouraging mass participation in management" (Riskin, 1987: 120). The DRSULP system was maintained during the period of the movement (1958-61) as it embraced core elements of the Great Leap Forward's approach, such as Party's collective leadership, decentralisation and mass-line management.

The two major consequences of the DRSULP system were the growing domination by the Party, and the decentralisation of planning and decision-making (Laaksonen, 1988). First, under this system the Party committee demanded primacy in important decision-making areas, including employee matters and the factory's conformity to the central plan (Andors, 1977; Schurmann, 1968). The Party's direct control over employees (cadres and workers alike) on matters, such as "determining appropriate labour norms" (Laaksonen, 1988: 202), indicated a concerted political stance to ensure that employees followed the Party's and Mao's proletarian line (Andors, 1977). The Party's authority in formulating the enterprise plan in areas such as production quotas showed "direct Party influence on the entire course of enterprise economic activity" (Schurmann, 1968: 292). The Party's supremacy in both the politics and policies of enterprises resulted from the Maoist belief that the collective leadership of the Party committee could solve any problem, whether it be the co-ordination of authority and responsibility, the circumvention of bureaucratic tendencies, the implementation of mass line management, or improvement of the technical and professional abilities of Party committees' (Andors, 1977).

Second, decentralisation of planning and decision-making came along with the DRSULP system at "both the micro- (enterprise-) and the meso- (provincial and communal) levels of the Party" (Laaksonen, 1988: 203). As Liew (1997) has observed, there was an ongoing debate on the appropriate balance between central directive and regional initiative in the history of the PRC. "Decentralisation was the natural response to the increase in complexity in national planning brought about by the continuous increase in the number of state enterprises and range of products produced by an economy that was growing" (Liew, 1997: 56). In 1956 virtually all industry and commerce came under direct state control as a result of the completion of socialist transformation of ownership in all sectors. However, "planning and administration, in their highly centralised form, had become increasingly ineffective as the economy grew in size and complexity" (Riskin, 1987: 111). Consequently, Mao's strategy of "administrative decentralisation" was endorsed by the State Council in late 1957 (Riskin, 1987: 104). The authority of local government encompassed all aspects except the four mandatory goals, i.e. the quantity of main products, the total number of employees including staff and workers, the total wage bill, and profits (Andors, 1977). Meanwhile, the Party committee at the enterprise level also gained more power and responsibility over the operations of the enterprise, now handling quota planning, wages and incentives (Laaksonen, 1988; Riskin, 1987).

To implement Mao's large-scale mass-oriented management, a new management model was promoted at the height of the Great Leap Forward in late 1958. This new model was called "two participation, one reform, and triple combination", or the "Two-One-Three" management system (Lee, 1987: 62). 'Two participation' referred to the participation of workers in management and of cadres (i.e., managers or other white collar employees) in manual labour; 'one reform' referred to the reform of irrational rules and regulations; while 'triple combination' referred to technical work teams, consisting of workers, technicians, and administrative cadres to achieve "combination of leadership with the masses, labour with technique, and technical theory

with production practices" (Andors, 1977: 83). The Two-One-Three system was made official by Mao in March 1960 when he endorsed this practice in a report sent by Anshan Municipal Committee (Xia, 1992: 590). This system was soon included in the five principles of the Anshan Constitution that was regarded as the constitution for industry at that time (Andors, 1977).¹

The Two-One-Three system was directly contrary to Soviet industrial enterprise management, which, in Mao's view, "used restrictive rules and regulations to subordinate workers to management" (Riskin, 1987: 162). This system, according to Lee (1987: 69), evolved "from the conflicts between ideological purity and expertise, material incentives and non-material incentives, the mass-line and professionally oriented management, and regulatory control and a mobilisation approach". In this system, distinctions between managers and workers were erased by "making managers work and workers manage" (Schurmann, 1968: 288), and "worker-managers were elected by the teams for separate tasks and confirmed by the Party Committees at the factory level" (Andors, 1977: 82). Material incentives were severely criticised as they contradicted the political goals of socialism. The incentive policy during the Great Leap Forward was focused on political dedication to the building of socialism, and incentive was expected to "come from feelings of solidarity, mutual co-operation, and collective improvement rather than from individual competition and monetary rewards" (Andors, 1977: 125). Subsequently, the individual bonus was abolished and the percentage of industrial workers who earned piece-rate wages dropped from 42 percent in 1957 to only 5 percent in 1960 (Lee, 1987: 56; Andors, 1977: 86). The Two-One-Three system facilitated the end of highly centralised planning as small production groups planned their own daily work schedules and operations. The task of co-ordination and control over policy, operations, and politics was thus shifted to the Party committees (Andors, 1977; Riskin, 1987).

Management under collective leadership of the Party (DRSULP system) and the Two-One-Three system both pursued the policy of concentrating leadership into the Party's hands and dividing management among the masses (Schurmann, 1968). However, the DRSULP system still tried to separate political goals from the economic and technical tools of modernisation, and managerial staff were still heavily involved in everyday management work. The Two-One-Three system focused more on "the politicisation of the enterprise management policy" (Lee, 1987: 60) by overemphasising the Party's supreme control over "the whole gamut of industrialisation" (Andors, 1977: 95). With the collapse of the Great Leap Forward in 1961, Mao's favoured approach of social mobilisation and administrative decentralisation was discredited and these two management systems were replaced to some extent by management principles stipulated in the Seventy Articles in 1962.

'Expert-Oriented' Management – The 'Seventy Articles'

Early in the period of economic readjustment (1962-65), the government moved to reassert strong central control over the economy and resource allocation with regard to industry, commerce, finance, and labour. Re-centralisation of the planning system required regularisation of enterprise management, for which the Seventy Articles became the guide (Riskin, 1987: 158-9).

The adoption of the Seventy Articles was aimed to retreat from Great Leap Forward practices (Riskin, 1987), and "to negate the Great Leap Forward experiments and to return to One-Man management" (Andors, 1977: 129). Although the Soviet term 'One-Man management' had not been used since the late 1950s due to the Sino-Soviet conflict and the subsequent Soviet withdrawal of economic and technical assistance, the management system adopted in the Seventy Articles was similar to 'One-Man management'. Schurmann (1968: 297) has observed that "industrial management returned once again early in 1961" when the central government frantically called upon the discredited managers to rescue the country from its economic crisis. The Seventy Articles emphasised an "expert-oriented management" or "professionally oriented management" system (Lee, 1987: 94), and restored the professional managers and other technical experts to the positions they had occupied before the Great Leap Forward (Breth, 1977). The return of professional management marked a shift "from Party management to profit management" as noted by Laaksonen (1988:

¹ The five principles of the Anshan Constitution were: (1) to keep putting politics in command; (2) to strengthen Party leadership; (3) to rely on mass movements; (4) to institute the 2-1-3 system of management; and (5) to vigorously promote technical revolution (Selden, 1979:591-2).

204). This meant the emphasis was shifted from all-out production drives to economic efficiency with profits, costs, and labour productivity representing the important factors (Li, 1964).

According to Lee (1987: 85-9), the Seventy Articles provided comprehensive coverage of all major aspects of enterprise management including planning, technology, accounting and finance, labour and compensation, economic co-ordination and responsibility systems. The Articles defined the nature, objectives, and organising principles of the enterprise and its relationship with the supervising authorities and other enterprises. During the implementation of the Seventy Articles, industrial enterprises were renamed as 'economic organisations' rather than political organisations, and many dimensions of enterprise management became emphasised again, such as strengthening the power of the factory director to keep the state and Party separate, restoring the office of chief engineer to establish the technical management system, returning partially to the piece-rate wage and a limited bonus system, and promoting the employment of contractual and seasonal workers (Lee, 1987: 88-9). With the restoration of system and order following the re-establishment of specialised functional departments in enterprises, factory directors regained their leadership role with supervision from the Party committees, whilst direct worker participation in enterprise management declined (Riskin, 1987). The re-emergence of independent managerial authority witnessed a reduction in the role of the Party committee to such an extent "that it was confined solely to 'political activities'" (Breth, 1977: 83).

The Seventy Articles were implemented intensively from late 1961 to 1966, even though Mao had reservations about the document and never gave his support to the articles² (Lee, 1987). Profitability became a more important indicator of enterprise performance in the early 1960s (Riskin, 1987; Schurmann, 1968). Ma Wenrui, the Minister of Labour at the time, wrote in 1964 that the most important task for management was production so as to achieve modernisation, because, he argued, once the system of ownership was changed from private to public, the principal cause of class conflict in modernising industrial society was eliminated (Andors, 1977: 136). However, adoption of the Seventy Articles and expert-oriented management and the argument for modernisation did not defeat Mao's ideological principles such as 'supremacy of the Party' and 'politics in command', because Mao and his followers never acknowledged any major mistakes made during the Great Leap Forward.

Cheng (1963) has noted that the communiqué of the 10th plenary session of the Eighth CPC Central Committee published in September 1962 only admitted that during the Great Leap Forward, "some of our work is not well done. For instance, because of the incompetence of the leading cadres, production teams, some factories and some business establishments have produced less or become unwelcome to the masses" (see Cheng, 1963: 156). Mao's leadership and ideology were still regarded as being completely correct and the 'three red banners' advocated by Mao (i.e. the general line for socialist construction, the Great Leap Forward, and the people's communes) were not explicitly challenged by anyone except a small group of Party leaders headed by Peng Dehuai (see Lee, 1987: 66-8 for details of the criticism raised by Peng and the subsequent political purge of Peng).

Riskin (1987: 179) has pointed out that after the Great Leap Forward, some of the leadership strongly advocated "stability, routinisation, professionalism, and economic liberalisation; ... a shift in attention from revolutionising the relations of production to developing the forces of production". These ideas, however, were not only rejected by Mao but also regarded as objects of 'class struggle' between the bureaucratic class and the working class (Lee, 1987 Riskin, 1987). Lee (1987: 115) has suggested that the struggles between the two classes or two lines in the industrial sector were actually the "two fully articulated and contradictory views of enterprise management before the Cultural Revolution".

The Maoists advocated that 'politics in command' rather than economic laws were the means of increasing production, while the bureaucratic or anti-left line called for "a return to systems, order, discipline, production, and Party leadership" (Riskin, 1987: 193). Between 1963 and 1965 the Maoists launched a

² After the Great Leap Forward, Liu Shaoqi was appointed as the State Chairman of the PRC in 1959. Then Mao Zedong voluntarily withdrew from the first line (i.e., to stay at "second front") while Liu Shaoqi and other CPC leaders such as Deng Xiaoping, the then Party General Secretary, and Bo Yibo, the then Vice-Premier, became the "first-front" leaders in charge of the economic readjustment (see Lee, 1987: 89-93 and 118-9).

number of mass political propaganda campaigns such as 'Learning the thought of Mao Zedong' and 'Industrial enterprises to learn from Daqing'. These ideological campaigns were aimed at "creating a personality cult of Mao and preparing the working people for uncritically and blindly following his command" (Bharadwaj, 1995: 37). The campaigns were also part of the Maoist counterattack on the trends following the Great Leap Forward. By 1964, "the Party's leadership in the economy and in industrial enterprises was as strong as it ever was, if not stronger" (Andors, 1977: 134). Mao's view on revolutionary industrial management was also fully developed. This included the re-emphasis of the role of politics in enterprise management and the claim that revolutionisation should precede modernisation (Andors, 1977; Lee, 1987).

As a result of Mao's ideological and political influence, there were two contradictory tendencies during the economic recovery period. One was to undermine or negate the Maoist radical methods by adopting the Seventy Articles to rationalise enterprise organisation and management; the other, to preserve some Great Leap Forward policies and practices such as the 'Two-One-Three' system (Andors, 1977; Riskin, 1987). For example, cadre participation in manual labour or physical work received less emphasis with the implementation of the Seventy Articles, but was maintained and later emphasised by Maoists when Mao launched a campaign for every industry to learn from the Daqing model during the period 1963-66 (Lee, 1987; Riskin, 1987). In 1964, cadre participation in labour was regarded as one of the keys to revolutionisation (Andors, 1977). In addition, the triple combination of workers, technicians, and administrative cadres from the Two-One-Three system was continued during this period, even though the triple combination groups became "less concerned with making policy and more concerned with providing information for the policy makers as worker participation in management changed and as cadre participation in labour changed" (Andors, 1977: 120).

In early 1965, Mao requested that the Seventy Articles be revised because of the incompatibility of this document with his ideology. However, Deng Xiaoping, the Party General Secretary and Bo Yibo, the Vice-Premier, who were in charge of this revision work, tried to "keep to the original version as closely as possible" (Lee, 1987: 92). Bo Yibo stressed that the applicability of the principles of managerial work and the leadership system in the Seventy Articles meant no fundamental changes in the document would be made (Lee, 1987: 92). By late 1965 the revised Seventy Articles were issued by Bo Yibo to key enterprises at central and local levels to solicit responses, and the new version of the document was to be implemented in 1966. However, implementation did not occur, as the Cultural Revolution was launched in May 1966 by Mao, due to "in large part the effective resistance of much of the Party and government leadership to Mao's call for the renewal of class struggle" and his leftist ideology (Riskin, 1987: 180).

'Revolution Committee' Management

During the Cultural Revolution, the expert-oriented managerial systems were condemned for "putting too much emphasis on professional work and undue reliance upon control and supervision" (Lee, 1987: 114). The Seventy Articles were considered to be revisionist and were intensely criticised for advocating management control over workers by rules and regulations, granting control of production by technical experts regardless of their political attitudes, encouraging material incentives by restoring a bonus system, and weakening the Party's control over enterprises (Andors, 1977). Mao Zedong himself believed that leadership in a majority of factories "was not in the hands of genuine Marxists and the masses of workers before the Cultural Revolution. Thus, such enterprises, publicly owned though they were in form, were in reality controlled by opponents of socialism" (Riskin, 1987: 190). Maoists declared that Mao's policies for industry - i.e. the leading role of the workers, the importance of political ideology, and the commanding role of the Party - were not followed and carried out except during the period of the Great Leap Forward (1958-61). They also claimed that industry in the PRC had been governed by bourgeois management policies, such as expert-oriented management and emphasis on profit and material incentives, from 1949 to 1957 and from 1962 to 1966 before the Cultural Revolution started (Lee, 1987).

As the Cultural Revolution became a mass movement and spread to industrial enterprises in late 1966, the previous expert-oriented or "bourgeois technical authorities" management was replaced by so-called "rebel leaderships" composed of workers and cadres who were "directly involved in full-time production, [and were] active critics of the factory leaders" before they seized management power (Andors, 1977: 163-5).

During the seizure of power in enterprises, some enterprises experimented with commune-type organisations, with leaders being elected by workers and the Party being substituted by rebel leadership (Lee, 1987).

Nevertheless, the loss of both the Party and state control inherent in the direct democracy of the 'commune' model was too much for Mao, who opted instead for the establishment of revolutionary committees consisting of a triple alliance of rebel workers, military representatives, and 'revolutionary cadres' (Andors, 1977; Riskin, 1987). The reason for bringing military representatives (i.e., officers and soldiers from the People's Liberation Army [PLA]) into the management team was because "during ideological turmoil the PLA became a source of administrative coherence and symbolic legitimacy" (Andors, 1977: 172) and played the role of a political broker between the rival factions within industrial enterprises to restore order and keep enterprises in operation. In 1969, the Party's leadership was restored and became the nucleus of the revolutionary committee (Andors, 1977).

The establishment of revolutionary committees proceeded unevenly from early 1967 to mid-1968. Revolutionary committees at enterprises were characterised by a "charisma-inspired, mass-oriented style of industrial management" (Lee, 1987: 97). Large numbers of workers were appointed to the committees and took on managerial positions at the factory level (Andors, 1977). However, many committee members "were not sufficiently competent and experienced to handle day-to-day managerial functions" (Lee, 1987: 113), because their selection had been based only on their political background. Many workers appointed to the committees did not have previous management experience (Andors, 1977). Laaksonen (1988) has also observed that the selection of new managers was based more on ideological suitability than appropriate qualifications or experience.

Revolutionary committees at all levels were required to "practice unified leadership, eliminate overlapping jurisdictions, streamline organisational structure, and maintain closer ties with the masses" (Lee, 1987: 113). Ideological education preceded other operational duties, because Maoists claimed that "politics and production were to be inseparable. Politics was to be applied to production, shaping human relationships, defining purposes, and providing incentives for hard work" (Andors, 1977: 224).

The other major responsibilities of the revolutionary committees included technical and financial control, compensation and incentives, macro-management and economic integration (Andors, 1977: 216-24). The technical and financial control in many enterprises was exercised by the triple combination of administrators, technical persons (e.g., technician or accountant) and shop-floor workers, a grouping inherited from the Two-One-Three system. This management practice witnessed a greater decentralisation of control functions to the production units and participation both up and down the line, i.e. worker participation in management and cadre participation in labour. The political motive behind the practice, as pointed out by Laaksonen (1988: 222), was to "avoid creating a new elite or social class" and to reflect the Maoist emphasis on "the participation of the masses". Nevertheless, many human resource practices, such as wage scales and welfare distribution, underwent little change except the abolition of all material incentives including bonus and piece wages (Harding, 1987; Riskin, 1975).

As for macro-management and economic integration, there were two major features according to Andors (1977: 222) - despecialisation and decentralisation. Despecialisation resulted from Mao's emphasis on self-reliance, which aimed to allow each locality, region, or enterprise to rely on its own resources for development (see Riskin, 1987: Chapter 9). It encouraged enterprises to become comprehensive units that made maximal use of the materials and intermediate goods needed to achieve its main production line. As a result, enterprises were often either 'small but complete' or 'large and complete'. According to a "Country Study" conducted by the World Bank in China in 1983, nearly all enterprises visited had built a significant proportion of their equipment for themselves. A textile factory, for example, had a foundry and a forge for making spare parts, and extensive, well-equipped machine shops that could repair even their own maintenance machines (World Bank, 1983: 161). The pursuit of such 'completeness' or self-reliance resulted in the 'community' or 'miniature society' type of industrial enterprises that were characterised by overstaffing and low efficiency (Harding, 1987; Laaksonen, 1988; Riskin, 1987). The decentralisation during the Cultural Revolution was combined with various administrative and governmental levels of economic despecialisation. This meant a multi-layer system of relatively more independent localities and enterprises was created than would be usual in a vertically integrated economy.

The efficiency of the revolutionary committee management system was challenged in the policy papers drafted by the State Planning Commission in 1972 when Mao endorsed the ex-Premier Zhou Enlai for carrying out national economic tasks.³ The policy papers listed deficiencies in the enterprise leadership system (i.e., the revolutionary committees) as one of the main problems to be remedied (Lee, 1987: 118). The problems in industrial management were also addressed in a policy paper by Deng Xiaoping in 1975 when he became Acting Premier. The paper was entitled 'Twenty Points' (or 'Certain Questions on Accelerating the Development of Industry') and was regarded as a reprint of the discredited Seventy Articles. It focused on management at the enterprise level, emphasising the management needs including the need for regulations and systems, the need to strengthen enterprise leadership and improve employee motivation (Lee, 1987: 125-9). However, the revolutionary committee management with its focus on politics and Mao's ideology was maintained until an initial reform in enterprises started and the factory-director-responsibility system was introduced in mid-1977 after the fall of the 'gang of four' and Deng Xiaoping's return to power.

In summary, under the highly centralised planned economy and state dominant ownership structure, management systems and practices possessed distinct features that could be generally described by Naughton's (1996: 57) analogue, "the bird in the cage", or Lin et al.'s (1996: 51) terminology, "puppet-like" enterprise management. This is because regardless of whether managers were given autonomy for their operations as in the 'One-Man' management practices or deprived of such autonomy as in the Cultural Revolution, they were constantly confined by a centralised command economic system. Under this system, the state "set the norms of economic activities to be followed by enterprises" (Hsu, 1991: 76), that is: ... all required factors of production were allocated to enterprises by the state, all their products were submitted to the state, all their production costs were settled by the state, and all their profits were remitted to the state. There was no link between the expansion of an enterprise and its economic efficiency, or between its workers' income and their contribution (Lin, et al., 1996: 61).

The system imposed a highly restrictive and rigid set of constraints over the behaviour of managers, and deprived them of any authority "to shape the enterprise into a unique or idiosyncratic organisation to match the output, market, or personality of that unit" (Naughton, 1996: 107). In addition, the Party was the ultimate arbiter of important decisions due to the supremacy of the Party and politics (Naughton, 1996). All these factors ultimately deprived managers of their autonomy and resulted in a 'puppet-like' or 'birds-in-the-cage' management style.

Enterprise Management after the Commencement of the Reform Process (1979 Onwards)

The Third Plenary of the 11th Central Committee of the CPC, held in December 1978, was regarded as a historical turning point and a milestone in Chinese history as it initiated a major program of reform of the Chinese economy. The meeting "started all the processes which put an end to the excesses of the 'extreme left' policies over two decades and which finally led to the emergence and consolidation of the policies of reform and opening" (Talas, 1991: 67). The two main components of the command economy - central planning and public ownership - were targeted for reform (Dong, 1992; Talas, 1991). Dong Fureng (1992: v), a well-known Chinese economist, specified the two major aspects of the economic reform as operational reform and ownership reform. Operational reform aims to replace the mandatory central planning system with a market-oriented system. Ownership reform, on the other hand, has two aims. The first is to reform the existing ownership structure that is predominated by public ownership so as to encourage other types of ownership. The second is to reform public ownership *per se* so as to establish a new form of public ownership which stimulates economic growth.

During the era of economic reforms, China has experienced a series of rapid changes unprecedented in its post-revolutionary history. These changes, including a restructured economic system and rapid growth of various forms of ownership, have set the stage for significant changes in management. While China is in the transition "from plan to market" (see Liew, 1997) and the reforms have since "substantially upgraded China's old-style 'command economy' to a new 'socialist market economy'" (Goodall & Warner, 1997: 569), a number of issues arise. First, to what extent have traditional management systems and practices been changed? Second, what is the

³ Mao's support for economic development was endorsed after the Lin Biao incident. Lin Biao officially became Mao's successor in 1969 but was killed when he fled to the Soviet Union in September 1971 after an abortive coup against Mao (Harding, 1987:51; Lee, 1987:115-18).

impact of reforms on changes in enterprise management? This section seeks to answer these questions by highlighting and examining major changes in the management practices since the reforms.

The fundamental changes in management practices began to take place in the late 1970s and the early 1980s with the adoption of different systems of management responsibility. Two critical issues emerged when implementing these systems: first, who should take responsibility for the enterprise, the enterprise Party committee or the director (the chief executive officer in Chinese enterprises); second, whether the responsibility should be primarily political or economic and, if economic, how it should be specified (Hay et al., 1994). The two issues rightly reflected the problem underlying the puppet-like management. In other words, should the Party's supremacy still be kept intact in enterprise management? Should politics still take precedence? What responsibility should a director have over production and operations? What were appropriate indicators of management performance? To address these issues, and in effect to solve the problems of the puppet-like management, a number of different management systems have been tried since beginning of the reform. Three major systems are examined in chronological order in this section. This account demonstrates that every change in the management system is closely linked to reforms at micro and macro levels, including reforms of the tax, price and resource allocation systems, subsequent emergence of different types of ownership, and changes in government roles in enterprise management.

Factory Director Responsibility System (FDRS) (1984-86)

Along with the abolition of the revolutionary committees in the late 1978, executive bodies were established in most enterprises consisting of a Party committee and a working committee, with the latter under the leadership of the former. Meanwhile, a tentative system of division of responsibility was tested, with the factory director⁴ under the leadership of the Party committee (Tung, 1982). Nominally this system was similar to the DRSULP (director responsibility system under the leadership of the Party) used in the mid-1950s, but it granted enterprises "a certain degree of autonomy and a partial claim to newly created revenues" as a result of adopting the profit retention system (1979-81) and the profit contract system (1981-83) (Lin et al., 1996: 138-40).

As the enterprise at this stage was controlled by the collective group represented by the Party committee rather than the factory director, there was no clear delineation as to who should assume responsibility for production operations, especially for any losses caused by a wrong decision (Child, 1987; Hey et al., 1994). This collective system diffused responsibility for enterprise performance and was criticised by Deng Xiaoping when he stated that, "Nominal responsibility of the committee for decision-making means no responsibility, or nobody to be really responsible for decisions" (Zhang 1987, in Hay et al., 1994: 20). Lockett (1990) also observed that by the early 1980s the role of the Party committee in management was perceived as problematic because of the ignorance of committee members towards technology, economics and management of the enterprise. The implementation of this system indicated a strong impact of Mao's ideology that the Party should direct and control everything, and that the Party's unified leadership should be practised over all economic institutions including enterprise business operations (Hey et al., 1994; Kaple, 1994; White, 1993).

From the early 1980s, state enterprises faced increasing competition due to the entry of non-state enterprises that became more competitive on the market. In order to improve the performance of enterprises, post-Mao reformers tried to separate the functions of the Party committee and factory directors by reducing the influence of the Party committee and curtailing its rights to making decisions about production (Lin et al., 1996; Mackerras, Taneja & Young, 1994; White, 1993). These changes were endorsed by the policy document on 'China's Economic Structure Reform' adopted by the Party Central Committee in October 1984. The policy recognized the significance of division of labor in modern enterprises, emphasized a subsequent necessity of establishing a highly efficient system to direct production and conduct operations and management, and declared that the contingencies of modern industry required the director or manager to assume full responsibility (Child, 1987). The factory director responsibility system (FDRS) was introduced and implemented on an experimental basis in six cities in the autumn of 1984, and later extended to the whole country (Child, 1987; Mackerras et al., 1994).

⁴ 'Factory' and 'factory director' were more frequently used than 'enterprise' and 'enterprise general manager' before the issue of the 'Enterprise Law' in 1988.

The FDRS was intended "to identify and hence structure the distinctive executive powers of management and to distinguish these from the rights and functions of state ownership and of the Party" (Child, 1994: 296). Under this system, ultimate managerial authority was vested in enterprise directors who were responsible for enterprise production, sales, pricing, purchase of materials, use of funds, handling of assets, structural establishment, personnel and labour, wages and bonuses, and inter-unit operations (see Laaksonen, 1988: 240-1 for example). The Party committee was no longer involved in economic decision-making within the enterprise, and was relegated to a nebulous supervisory and co-ordination role. It was to ensure that state policies and laws were adhered to and the state quotas were fulfilled, and to assist the director to improve productive performance. It was also responsible for carrying out political and ideological work among employees (Naughton, 1996; White, 1994; Wong, Heady & Woo, 1995).

Since the introduction of the FDRS, the government has passed several laws and regulations in its efforts to institutionalise the system. In 1986, the State Council issued the Regulations on the Work of Factory Directors in State-owned Industrial Enterprises, which gave directors final operational authority although they were still required to consult on major decisions with a management committee composed of the Party secretary, heads of the trade union and other functional departments (Byrd, 1992). In 1988 the Seventh National People's Congress adopted the Enterprise Law that not only legitimated the leadership position of directors but also legalised the functions and powers assigned to the director. Directors were appointed for one- to three-year terms, at the beginning of which they were required to set out both long- and short-term targets of their enterprises, and reappointment depended partially on their achievement of goals (Mackerras et al., 1994; Zhao, 1995).

Factory directors' autonomy with respect to production was facilitated by the government's reduced role in planning and controlling as well as by the fiscal reforms in 1984 that replaced profit remittance to the state by taxes on profits. According to the 1984 Enterprise Bill of Rights, all managers had the authority to establish their own production plans provided that they fulfilled mandatory state plans. Based on a survey conducted in 1990, Naughton has revealed that "the proportion of managers actually having such authority increased gradually from only about a quarter of total enterprises in 1984 to two-thirds by 1988 and almost 90 percent by 1990" (1996: 207). Additionally, with the fiscal reform, absolute ceilings on bonus payments were eliminated and replaced by a progressive bonus tax (Naughton, 1996). This offered managers more flexibility to decide on the amount of bonuses, and how to distribute them to reward high performers and to widen differentials between mental and manual, skilled and unskilled work (Child, 1994).

The FDRS specified clearly who within the enterprises should exercise decision-making, and it was the first time a unitary management system had been officially accepted since the adoption of the Soviet One-Man management in the 1950s (Child, 1987). However, some serious problems were identified within this system. Lo (1997) has observed an asymmetry between benefits and responsibility of factory directors as there was a persistent tendency for investments and bonuses to expand. The investment hunger of enterprises was caused by the fact that directors would receive further benefits if they succeeded but risk very little if they failed. The bonus expansion occurred mostly through "wage emulation" rather than productivity improvement (Lo, 1997: 109).

Hay et al. (1994: 21-2) have also pointed out some issues that were not resolved by the system. First, the definition of 'responsibility' was vague and its interpretation was flexible, i.e. what was the content of responsibility – was it administrative, political or economic? Second, lack of strong motivation and commitment to meet profit targets was identified as a marked weakness. The system allowed the pay of a director to exceed the average level of workers by only one to three fold, and the mechanism for determining managerial pay remained unclear (Byrd, 1992). Third, responsibility was 'one-way', i.e., the director was responsible to the higher authority, but this did not prevent intervention by the higher authority that did not take any responsibility for the consequences of its interventions. Child (1994) attributes this problem to solidly formulated structures of central planning and hierarchical administrative control that could not be easily removed. Because of these unsolved problems, especially the unsatisfactory performance indicators such as falling enterprise profits and contracting state budget revenue (Lo, 1997), the FDRS was replaced by a new contractual management system in 1987.

Contract Management Responsibility System (CMRS) (1987-94)

The contract management responsibility system (CMRS) was applied generally throughout China in 1987, and it proved to be very popular and became the longest surviving incentive system and managerial mechanism in the industrial sector until the mid-1990s (Chai & Docwra, 1997). What were the main objectives and practices of the CMRS? How did the system function? Did the CMRS achieve better results than the FDRS? What contributed to its replacement in 1994? Each of these questions is addressed respectively in this section.

With the implementation of the FDRS, the government delegated more decision-making powers to enterprises, with the intention of enabling them to compete freely on the market. This was difficult in practice at that time due to dual-track prices. Because enterprise profits were often not determined by its management performance but rather by its access to inputs with low prices, or permission to sell more products on the market, or its ability to increase profits by rent-seeking, competition remained unequal between enterprises (Lin et al., 1996; Naughton, 1996). In order to create equal conditions for all enterprises, the government took into account each enterprise's business conditions and environment by negotiated individual contracts for each enterprise (Ishihara, 1993). The CMRS was introduced and swiftly became the general practice among enterprises, especially state ones. By 1990 more than 90 percent of enterprises came under the CMRS (Jackson, 1992: 109). This system restored targets for profit delivery, and established a more explicit link between enterprise performance and the payment of bonuses to workers (Hay et al., 1994).

Contracts used in the CMRS were negotiated between the enterprise, usually represented by its director, and its supervisory agency, and involved the specification of items such as the amount of profit to be remitted, investment and technical innovation targets and the tying of wage bills to total profits (Fan, 1994: 149). Under the CMRS, an enterprise was contracted to complete certain production tasks for the state, and to submit to the state tax payments and a mutually-agreed specified portion of its after-tax profits. All profits after tax in excess of this specified portion could be retained by the enterprise to use for expansion, to pay bonuses or to provide collective welfare benefits. If an enterprise failed to meet agreed targets, then the shortfall had to be made up from its own funds (Tisdell, 1993). This practice was also called "two-guarantee and one-linkup system" (*liangbao yigua*), that is, the enterprise should guarantee the state delivery of a certain amount of profit, guarantee the completion of certain planned tasks such as technical renovation, and link the growth of its wages bill to enterprise efficiency indicators (Chai & Docwra, 1997: 163; Chen, 1995: 63; Hay et al., 1994: 25).

The duration of a contract averaged three to five years, and this was intended to alleviate the problems caused by ratchet effect⁵ (Fan, 1994; Naughton, 1996). It was believed that long-term contracts could avoid continuous re-negotiation for targets and "would establish a quasi-legal guarantee for the enterprise manager's autonomy over a somewhat longer period" (Naughton, 1996: 213). Shirk has argued that the duration of a contract was actually not an issue due to one of its distinct features – "lack of risk" (1993: 323). According to Shirk, a long-term arrangement could in theory put enterprises under greater financial risk and might even create personal liability for managers during periods of price reform when there were severe fluctuations in the market. Nevertheless, in practice, the definition of contract used in the Chinese context was different from the one used in the West, in that the contract did not have "real teeth" and was just "an overall agreement" between two parties (Chen, 1995: 57). Enterprise managers could always renegotiate their contracts to compensate for any external factors that reduced their revenues, because they in fact carried no risk (Byrd, 1992; Chen, 1995) – they actually "contracted only for profits and not for losses" (Shirk, 1993: 315).

Many researchers (e.g., Byrd, 1992; Chen, 1995; Child, 1994; Hay et al., 1994; Lo, 1997) believe that because of the implementation of the CMRS, enterprise managers became more independent from the higher level authority, had more focused managerial objectives and a more business-like orientation, were more responsible in their investment behaviour, and were encouraged to reform their payment systems. Liew (1997) has provided evidence of productivity improvements achieved by state enterprises under this system. However, while this system was effective in ensuring greater stability in state revenue collection and in increasing workers' income, it focused mainly on profitability rather than on development such as technical renovation and enterprise

⁵ 'Ratchet effects' refer to the situation where good performance in one year could be penalised by higher targets for planned profits in subsequent years when using historical data to fix new targets (see Byrd, 1992: 3; Naughton, 1996: 213).

expansion (Chai & Docwra, 1997; Ishihara, 1991; Lo, 1997). This was partly due to the lack of emphasis by the state on such long-term strategies and partly due to the availability of soft loans from the state. The soft loans, in particular, encouraged managers to avoid using their discretionary funds for long-term investment at their possible personal expense (e.g., bonuses forgone) (Tisdell, 1993). Apart from this short-term behaviour, the system had other weaknesses such as individually based negotiation and vulnerability to external influence. Shirk (1993: 322) used the term "particularism" to describe the problem caused by enterprise-based negotiation. As the tax rate was individually set rather than being uniform in the system, bargaining between the parties to the contract was still an option and any budget constraint imposed on the enterprises could thereby be softened (Chai & Docwra, 1997; Fan, 1994; Jackson, 1992; Wong et al., 1995). Furthermore, negotiations covered issues ranging from the contract terms to what to do if the enterprise failed to reach its profit target (Wong et al., 1995). Although Lo (1997) has argued that bargaining under the CMRS was mainly around financial performance rather than inputs allocation and outputs delivery as it was under the central planning system, some researchers believe individually-based negotiations were incompatible with the goals of enterprise reform (Jackson, 1992; Wong et al., 1995). Because contracts varied within different enterprises, industries and localities, the contracting method became too arbitrary to discriminate between capably and poorly managed enterprises (Shirk, 1993).

Furthermore, managers were still vulnerable to external influence from bodies such as the Party and government departments (Chen, 1995; Naughton, 1996; Tisdell, 1993; White, 1993). For example, under the CMRS, managers were designated as the legal representatives of enterprises and were responsible for the fulfilment of tasks set in the contract (Lo, 1997). However, the Party secretary was not prevented from direct participation in enterprise management, and political consultation was often required for managers to receive support from the Party secretary (Tisdell, 1993). This became more obvious after the Tiananmen incident in 1989, when an absurd slogan was put forward, "The manager is the centre, and the Party Committee is the core" (Chen, 1995: 75; Naughton, 1996: 279). The centre and the core referred to the top position and the slogan indicated that the Party Committee should still have an important role in enterprise management. In 1990 the Party Central Committee set specific guidelines for rebuilding the Party apparatus in enterprises and detailed the issues that the Party secretary should examine (Naughton, 1996: 279).

Chen (1995: 66-8) has summarised views in a debate revolving around the CMRS when it was first introduced regarding the distribution of power and interests between the government and the enterprises. According to Chen, there were three different views of the system. The proponents believed that the scheme could be used to serve two purposes: keeping public ownership and gaining enterprise autonomy; and offering enterprises more incentives through profit-sharing. The opponents argued that the system did not provide a rational approach in determining the profit targets, which was partly because the targets were based on previous rather than potential performance and partly because of the bargaining process. This shortcoming would subsequently damage the interests of the government. Furthermore, they claimed that the system induced short-term behaviour and excluded other alternatives for enterprise merger or bankruptcy because of the signed contract. The third view proposed that the system was not an ideal choice for the reform, but was workable and acceptable during a transition period, as it was too early and risky to introduce a shareholding system. While the arguments provided by the first two views actually recognised the major merits and defects of the CMRS, the third view predicted the downfall of the system.

By 1994 state enterprises had continued to be out-performed by other types of enterprises and incurred heavy financial losses which increased from 36.7 billion yuan in 1991 to 48.26 billion yuan in 1994 (Hay et al., 1996: 215; Lin et al., 1996: 145). The declining profitability reflected the ineffectiveness of the CMRS, such as its "arbitrariness in the distributional relations between the state and the enterprise and related incentive problems" (Xu, 1996: 370). In order to enforce budget constraint to increase enterprise's independence and competitiveness, it was believed that all enterprises should be pushed into the market rather than to be protected by the state (Lo, 1997). In 1994, the state implemented a new tax system with a uniform tax, which aimed to equalise the tax burden among different types of enterprises so as to equalise competition. Consequently, the foundation for the contract system was abolished and the CMRS was replaced by the modern enterprise system through corporatisation and shareholding.

Since the early 1990s the increasing financial losses incurred by state enterprises and the subsequent fiscal burden imposed on the state prompted further reform of state enterprises, which was considered by the government "to be the key to the reform of the economic system" (Liew, 1997: 85). Wood (1994) has argued that to rearrange the pattern of state ownership by introducing a shareholding system could help change the direction of many enterprises, making them predominantly profit-seeking rather than having a number of objectives (e.g. social and political). Some researchers also believed that state enterprises' lack of viability could be attributed to the ambiguity of their property rights, and the shareholding system would be the most effective measure to deal with such problems (Lin et al., 1996).

The program to establish a modern enterprise system through corporatisation and shareholding was formally recommended in the 'Decision on Issues Concerning the Establishment of a Socialist Market Structure' adopted by the third plenary session of the 14th Party Central Committee in November 1993 (Liew, 1997: 86). This Decision summarised the four major features of the modern enterprise system and pointed out the two major benefits of corporatisation. The four features as defined in the Decision included, "clearly-established ownership (*chanquan qingxi*); well-defined right and responsibility (*quanzhe minque*); separation of enterprise from government administration (*zhengqi fengkai*); and management in a scientific way (*guanli kexue*)" (*Beijing Review*, November 22, 1993: 14).

Chen Qingtai, Vice-Minister in charge of the State Economic and Trade Commission, has described the four features in more detail (Chen, Q. T. 1995: 67). First, under the modern enterprise system, state enterprises would be transformed into corporate entities to operate independently and compete freely on the market. The investors or shareholders of an enterprise would be represented by the board of directors, who would have control of residual rights including the right to appoint and remove managers, and would pressure managers towards profit-oriented behaviour. Second, enterprises would be instituted as required by the Corporate Law. While the government has limited liability to the enterprise based on its investment, the enterprise would have utilisation right, return right and alienation right.⁶ Third, there would be a distinction between the functions of government and enterprises. While enterprises have operational rights to gear up its production to market demand, they would be gradually divested of their social service obligations to the government administration. Hence the government would need to establish a diverse social security system to deal with unemployment, pension and other types of social welfare. Finally, management must be modernised by developing advanced managerial skills such as strategy development, effective leadership and organisation structure, marketing, and human resource development.

As for the benefits of corporatisation, the Decision stated that, first, it would clarify the assignment of property rights so as to separate government administration from enterprise management, and thus allow the state "to get away from its unlimited responsibility for enterprises". Second, corporatisation would encourage the infusion of new capital into state enterprises by other state corporations as well as by private and foreign investors. Therefore, it was "conducive to raising funds and diversifying risks" for the state sector (*Beijing Review*, November 22, 1993: 15). The program to set up a modern enterprise system was facilitated in 1994 with implementation of the new tax system, downfall of the CMRS and promulgation of the Corporate Law.

In the past, as enterprises were classified in terms of their ownership, the government had to formulate laws for different types of enterprises, such as the Law on State-Owned Industrial Enterprises and the Law on Sino-Foreign Joint Ventures, to suit such a classification. Under the market economy, all enterprises are required to be independent legal entities without administrative dependence, and thus enjoy total equality (*Beijing Review*, May 13, 1996: 17). In accordance with this requirement, the Corporate Law was formulated and issued to provide a uniform legal framework for various forms of shareholding companies (Wong, 1993). According to the Corporate Law, state enterprises could be incorporated as either limited liability companies or share holding

⁶ The definition of these three rights is "the right to utilize the assets (utilization right), the right to possess the fruits (and responsibility for the negative outcomes, such as damages and debts) of that utilization (return right), and right to transfer these rights to another agent through gift or sale (alienation right)" (Putterman, 1996: 87).

companies, which allowed them to issue shares to legal persons (the enterprise themselves), to employees or to the public depending on the type of company (Deng, 1998).

The experimentation of converting state enterprises to a stock system was initiated in the late 1980s, and in the early 1990s large, modern and profitable state enterprises were increasingly converted into modern corporate forms of various types, including limited liability companies and joint stock companies (Naughton, 1996; Wong, 1993). Shares issued at that time, as observed by Naughton (1996: 298-9), were quite different from those in the West. First, most shares were only issued to the enterprise's own workers as a means of raising funds and some served as bonds because returns were guaranteed. The shares did not bear any rights of ownership and few shareholders were given management privileges. Second, shares issued to the public were held overwhelmingly by government bodies. For example, of all Shanghai joint stock corporations at the end of 1992, 62 percent of the share value was held by the government, 24 percent was held by legal persons (predominantly other state enterprises), 7 percent by domestic individuals, and 7 percent by foreign investors.

Since 1994, establishing a modern enterprise system through corporatisation has become a new trend. At the end of 1994, 100 enterprises, 18 cities and 56 enterprise groups were selected by the State Council to test this system, and in 1996 it was reported that positive results were achieved through this experiment (*Beijing Review*, June 17, 1996: 14-16). According to the report, the 100 experimental enterprises had achieved an overall increase of 15.5 percent in their total capital assets, 11.67 percent increase in their sales revenue and 12.6 percent in their realised profits by the end of 1995. The 18 pilot cities had made progress in capital increment, technical renovation, the transfer of redundant workers and promoting mergers (for detailed results, see Chen, Q. T. 1995: 66). Similarly, the 56 experimental enterprise groups had readjusted relations between parent and subsidiary companies based on property rights outlined in the Corporate Law, and could hence function as owners of state-owned property. Based on these results, the modern enterprise system was introduced nationwide in 1996 and its establishment in the whole industrial sector was expected to be accomplished during the ninth five-year plan period (1996-2000) (Chai & Docwra, 1997: 169).

While the previous contract management responsibility system tried to improve the management of individual enterprises and relied on the reform of enterprises themselves to change operational incentives, the modern enterprise system has aimed at revitalising the entire national economy by introducing corporatisation, regrouping via merging and acquisition, and even bankruptcies (*Beijing Review*, January 20, 1997: 12; Xu, 1996: 370). The results from the initial experiment with the modern enterprise system have indicated that corporatisation of existing state enterprises helps to clarify property rights and operation rights. Under the shareholding system, the dual rights are separated when the manager is appointed by and responsible to the board of directors who are concerned mainly with the return on investment (Xu, 1996). Although Wong (1993: 33) regarded it as "a sort of Chinese way of privatising state enterprise", the shareholding system has been used not only to raise capital, but more importantly, to preserve state ownership while modernising the internal governance and incentive structure of enterprises to make them compatible with a socialist market economy (Chai & Docwra, 1997).

Although corporatisation or joint stock form has become a popular mode of the modern enterprise system as it achieved a very high degree of separation between ownership and control, some researchers believe it is still not effective under the conditions of market imperfection and an ineffective discipline mechanism (Lin et al., 1996). For example, while a free labour market has emerged, enterprises cannot retrench their surplus employees at discretion because of an incomplete social security system (Zhan, 1997). Recently 300 large and medium state-owned enterprises have been given preferential treatment in the form of tax concession, subsidised loans and depreciation allowance retention because they have been selected by the government to be groomed into mega-enterprises to withstand foreign competition after China's entry into the World Trade Organisation (Chai & Docwra, 1997). Just as these enterprises have privileges, many loss-making enterprises still rely on the government subsidies or soft loans for their survival (Zhang, 1996).

Wu Jie, the deputy head of the State Committee of System Restructuring, has noted that some government administrative departments have been restructured into corporations without changing their functions. They have still kept both ownership and operation rights of enterprises under their control (Wu, 1996). As policy-induced losses or profits still exist, there lacks a mechanism by which to objectively appraise the performances of enterprises and their managers (Lin et al., 1996). Thereby a successful implementation of the modern enterprise

system relies on deepening reforms in other areas, including the government's control over enterprise business operations such as the appointment of senior managers of large-scale enterprises (i.e. the Party-controlled nomenclature system), the divestment of state enterprises of their heavy social responsibilities, and establishment of detailed legislation for implementing the Corporate Law (Wu, 1996; Zhang, 1996).

In 1996 Premier Li Peng admitted in his report to the National People's Congress that state enterprises had "considerable difficulties in production and operation with their management and operation systems not yet adapted to the requirements of a socialist market economy", and emphasised that the modern enterprise system should be established in most large and medium-sized state-owned enterprises by the end of this century (*Beijing Review*, April 8, 1996: Documents: 3-8). In 1997 at the Party Central Committee, the General Secretary Jiang Zemin stated that China would continue its economic restructuring and implementation of economic development strategies from the late 1990s to the first decade of the next century. These strategies included the development of diverse forms of ownership with public ownership in the dominant position, the implementation of the joint stock system in enterprises, and acceleration of state-owned enterprise reform. The joint stock system has been especially advocated as a useful means to separate ownership from management and to help raise the efficiency and productivity of enterprises (*Beijing Review*, October 6, 1997: Documents).

DISCUSSION AND CONCLUSION

As previously discussed, the operational reform has witnessed shrinkage of the old centralised planning system, but an increasing role of the market in the economic system, ranging from control over prices to resource allocation. Meanwhile, the ownership reform has resulted in a rapid growth of enterprises in the non-state sector and more intensive competition in the market. The economic reforms and subsequent changes in government roles in enterprise management have granted real autonomy to enterprises and hence made a deep impact on management practices. This paper, through an extant literature review, has detailed the evolvement of management from before the post-Mao reforms and reviewed the fundamental changes in management practices since the late 1970s. Management systems and practice during the transition has reflected the strong impact of the Maoist Chinese model and economic reform on Chinese enterprise management. Such radical changes in enterprise management also hold implications for international business.

It has been over two decades since China instituted its economic reforms, and the subsequent impressive economic growth has witnessed an unprecedented enthusiasm for establishing foreign invested enterprises (FIEs) in China, including foreign joint ventures and wholly foreign-owned ventures. By the end of 1996, China had absorbed total foreign direct investment (FDI) of US\$ 171.8 billion with 281,298 projects (*People's Daily*, 19 December 1996). Employment in FIEs has increased from 550,000 employees in 1986 to 8,820,000 in 1995 (*China Labour Statistical Yearbook*, 1996). FDI has tended to take the form of an international joint venture with a state-owned enterprise as the local partner (Child, 1993; Perkins, 1996), hence imposing upon its foreign partners its the Chinese management practices that are a legacy of the pre-reform days (Beamish, 1993). Therefore, the study of Chinese enterprise management "promises not only to provide information of direct relevance to those who are active in that economy, but also to illuminate the relevance of Western thinking on management" (Child, 1994: 2). An understanding of China's past and present management practices will be of benefit to Western managers who are currently operating or contemplating commencing operations in China. This is because the knowledge would enable them to understand the changes that have occurred and the difficulties faced by local managers in accepting non-traditional or Western-style management practices.

Although the development of economic reforms has strongly indicated that the Chinese economy has been "growing out of the plan" and is now concentrated "on the market track" (Naughton, 1996: 8), the reforms are far from complete and "the marketisation of the Chinese economy" will be further implemented (Dernberger, 1997: 13). In this situation, the government's emphasis on implementing the modern enterprise system and its strong desire for enterprises to "become corporate entities and competitors adaptable to the market" (*Beijing Review*, October 6-12, 1997: Documents: 20) have become driving forces for further reform in management practices. China is now pushing hard to be readmitted into the World Trade Organisation (WTO), which, in turn, will accelerate market-oriented reform, as China has to make its economy compatible with the WTO's market economy principles. Hopefully, Chinese enterprise management practices will converge towards those commonly practised in advanced market economies.

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