

Why is China Cracking Down the Private Sectors?

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Division of Chinese Politics, Military and Warfighting Concepts

1. News Highlights

During Xi Jinping's tenure, it's not uncommon to hear the CCP oppressing private enterprises that had close ties with old party cadres and second-generation officials. Since the second half of 2020, the CCP began to take a series of obvious political actions against private

entrepreneurs in different sectors through judicial and administrative supervision, as well as leveraging media against them with political implications.¹ The context behind the tightened control over private enterprises and its causes are explained in this article to better understand the logic of how the CCP selects its "targets".

1. In November 2020, Sun Dawu (孫大午) and Yang Zongyi (楊宗義) (founders of Zhejiang Fuzhong Group) were taken away by the law enforcement agencies, while Li Huaiqing (李懷慶) (with the Chongqing Fuhua Pawn Company) was sentenced to 20 years for "inciting subversion of state authority". Since December 2020, the Ant Group, Tencent, Didi and other largest tech companies have been subject to new regulations (e.g. antitrust or data use) imposed by the authorities. Recently, private tutoring industry, online games industry and dairy industry have been under pressure. In its "Opinions on Further Reducing the Burden of Compulsory Education Students' Homework and Off-Campus Training" (known as "Double Reduction"), China's State Council instructed the tutoring industry to be registered as "non-profit" and are prohibited from public financing. At the same time, the online game industry was criticized by name through the *Economic Reference News* (owned by Xinhua News Agency) for harming young people physically and mentally, consumers were also alerted by the Xinhua News Agency of the over-marketing problem of formula milk that affected people's acceptance to breastfeeding. The opinions from official media caused the stock prices of the tutoring, game and dairy industries to take substantial impact for some time.

2. Security Implications

2-1. Beijing's response to the US “distinguishing CCP and Chinese people” policy

During the Donald Trump presidency, the Republican administration’s China policy began to take on a “distinction between the CCP and the Chinese people” principle, which prompted Xi Jinping to criticize publicly in response.² The new iteration of this policy began to develop in the first half of 2019 and was culminated in Michael Pompeo’s “Communist China and the Free World’s Future” speech at the Nixon Presidential Library. Pompeo stated that “the Chinese people are very different from the Chinese Communist Party, and we (the free world) must also engage and empower the Chinese people.”³

After 1978, the CCP regime moved from totalitarian to authoritarian. However, in comparison with the previous planned economy era, the CCP’s power to control society and ideology has weakened with the development of economic and social diversity. The US assertion of distinction between “the CCP” and “the Chinese (people)” and even the implication of “supporting the Chinese people” not only exposes the jeopardy in the CCP’s hold on power — the aforementioned weakness, but also reminds the CCP of the attempts to “advance China peacefully”. Therefore, the CCP will inevitably become more suspicious of the possibility of “collusion” between the people and external forces.

2. After the US publicized its 2019 policy of distinction between CCP and the Chinese people, it initially elicited reactions from China’s diplomatic system, and in 2020 it escalated to a personal response from Xi Jinping, “Anyone or any power that attempts to divide and antagonize the CCP and the Chinese people is absolutely not allowed.” — Xi Jinping, “Speech at the Symposium Commemorating the 75th Anniversary of the Victory of the Chinese People’s Wars Against Japanese Aggression and the Fascist Powers,” *Xinhua Net*; September 3, 2020.

http://www.xinhuanet.com/politics/leaders/2020-09/03/c_1126449917.htm.

3. “We must also engage and empower the Chinese people – a dynamic, freedom-loving people who are completely distinct from the Chinese Communist Party” . Michael R. Pompeo, “Communist China and the Free World’s Future,” US Department of State, July 30, 2020, <https://2017-2021.state.gov/communist-china-and-the-free-worlds-future-2/index.html>.

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Since the reform and opening of China, private enterprises have played an important role in bridging China and the world. Through enterprises, China has been able to import a steady stream of both tangible and intangible assets such as technology, capital, institutional frameworks and industrial standards from outside. However, with the unveiling of new US policy toward China, the “bridge” function performed by private enterprises has become a potential danger to the CCP. Even though mainstream academia has found no evidence that the Chinese bourgeoisie pose a real challenge to the CCP, it’s argued that their ties to the CCP are too intertwined and “embedded” from the political perspective.⁴ As a result, the CCP has further heightened its defense against the economic elites and emphasized the importance of the relationship and trust between the Party

and private enterprises.

In the “Opinions on strengthening the United Front in the private economic sector for the new age” (Sept. 2020), the CCP Central Committee for the first time explicitly pointed out that the diverse values and interests epitomized by private entrepreneurs are an issue that need addressing. In addition to strengthening the ideological guidance for private entrepreneurs, the CCP has also included “trust” for the first time in the policy of the United Front for Private Enterprises as the top priority.⁵ Although the guidance continues, the CCP keeps stressing that private entrepreneurs must be “trustworthy to the Party”. Under China’s party-state political system, private companies, no matter how well they maintain political or business relations with the CCP, can never be as powerful or well-protected as the state-owned enterprises. Therefore,

4. See the following sources for more details: Kellee S. Tsai, “Capitalists without a Class: Political Diversity Among Private Entrepreneurs in China,” *Comparative Political Studies*, Vol. 38, No. 9 (November 2005), pp. 1130-1158. McNally, Christopher A, and Teresa Wright, “Source of Social Support for China’s Current Political Order: The ‘Thick Embeddedness’ of Private Capital Holders,” *Communist and Post-Communist Studies*, Vol. 43, No. 2 (June 2010), pp. 189~198. Perry, Elizabeth J., “Studying Chinese Politics: Farewell or Revolution?” *The China Journal*, Vol. 57 (January 2007), pp. 1~22.

5. “The Guidance Outline for Starting a New Era in the United Front on Private Economy — the Central United Front Department Answers Reporters on ‘Opinions on Strengthening the United Front in the Private Economy Sector for the New Age’” , *People’s Daily Online*, September 16, 2020, <http://politics.people.com.cn/n1/2020/0916/c1001-31862713.html>.

the author believes that the key to distinguishing private entrepreneurs as “one of our own” or “an outsider” is whether they can be trusted by the CCP for what they “would do for the Party”.⁶

2-2. CCP's weaken private entrepreneurs to prevent “collusion”

As a result, we can observe from the recent news stories that the CCP is “assaulting” private enterprises in various industries on all fronts in every possible way. However, why does the CCP assault certain private entrepreneurs or industries through the bureaucratic systems across the judiciary, regulatory and official propaganda outlets? What is the political logic behind it?

This article offers two key observations:

1. Did private entrepreneurs develop their own value system different from the CCP’s based on their self-interest (instead

of the government’s)?

2. Do private entrepreneurs have the potential to establish a platform for “collusion”?

For instance, in case private enterprises take advantage of their capital as a tool to connect citizens, external forces and the influential veteran cadres to develop their own value systems or even political power outside the central government, they may become a threat beyond the grasp of the CCP. This might be the reason CCP uses its authoritarian power to cut off the potential collusion among private entrepreneurs while deepening their one-way reliance on the Party. On the other hand, the CCP also release a message that calls for private entrepreneurs to be “trusted by the Party”. In the following sections, the author will briefly explain the current situation by using the “Sun Dawu case” of different industries and the Internet leaders interrogated by the authorities as examples.

6. In November 2018, Xi Jinping said at the “Private Enterprise Symposium” that “the private economy is an intrinsic element of our economic system, and private enterprises as well as entrepreneurs are our own people.” Xi Jinping, “Speech at the Private Enterprise Symposium”, *Xinhua Net*, 1 November 2018. http://www.xinhuanet.com/politics/2018-11/01/c_1123649488.htm.

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1.The “Sun Dawu case”:

Sun Dawu, the founder of Hebei Dawu Farming Group, was sentenced to 18 years in prison by the Hebei Gaobeidian City People’s Court in July 2021 after being taken away by the public security authority last November (2020) for several “crimes”.⁷ Sun’s case involves his alleged “collusion” with private entrepreneurs and civic movements as a capitalist support to such movements with political ideas different from the government, which has become the biggest worry for the CCP. In addition to his public image as a grassroots entrepreneur, Sun is also widely known for his outspokenness. As the founder of one of China’s Top 500 companies, Sun has not shied away from dealing with liberal intellectuals and his willingness to support them. For example, Sun not only publicly mourned liberal intellectual Li Shenzhi in 2003, but also spoke out

on behalf of the human rights lawyers arrested by the CCP in July 2015 (known as the “709 Incident”). He also had a commission-representation relationship with one of the arrested lawyers, Xu Zhiyong, in a judicial case.⁸

2.To suppress emerging Internet startups:

In addition to strengthening the regulation of emerging Internet companies such as Alibaba, Tencent, Didi, Meituan and Kuaishou, the CCP suppressed them with two more considerations in mind:

First, to restrain their ability to collaborate with domestic and foreign private capital. Since these enterprises thrived during the Jiang Zemin and Hu Jintao era, they had benefited from considerable political and capital support from powerful leaders of that time; and thanks to the enormous potential of the Chinese market, they also received substantial investment from foreign

7. Sun Dawu was charged with crowd assault to state-owned institutions, obstructing public affairs, provoking public order, disrupting public production and operations, forced trade, illegal mining, illegal occupation of agricultural land and illegal solicitation of personal properties. “Sun Dawu sentenced to 18 years in prison and fined 3.11 million RMB in the first trial” , *People's Daily Online*, July 29, 2021. <http://society.people.com.cn/n1/2021/0729/c1008-32173871.html>.

8. Sun's voicing out on behalf of human rights lawyers may be due to the fact that Xu Zhiyong, the lawyer wanted by the CCP, was Sun's defense lawyer in 2003. “Chinese Entrepreneur Sun Dawu Sentenced to 18 Years for Eight Counts of Obstructing Public Affairs” . *BBC Chinese*, July 28, 2021. <https://www.bbc.com/zhongwen/trad/chinese-news-57085524>.

capitalists. For instance, SoftBank held over 20% of both Alibaba and Didi by 2021. It is worth noting that Alibaba, Tencent and Baidu have also invested in Silicon Valley since 2013. In this way, Chinese tech companies have not only benefited from private capital but have become part of the international capital circle as well. The capital, political, technological and human resources behind such “international alliances” could undermine the influence of the government if they are not brought under control.

Secondly, the CCP’s actions prevent the “new generation of non-public economists” in the emerging industries from becoming advocates of diverse values. China’s Internet giants have not only employed the country’s top university graduates, but also a large number of “returnees from abroad”.⁹

The social networks formed by the new generation nourish innovation of China’s tech industry, but they are also deemed to slip away from the Party’s control. They not only have the intellectual power and the potential to attract capital, but are also highly interconnected with the world’s tech networks. Once out of the Party’s control, the networks will continue to develop their own value preferences to easily become a “counterweight” for those in power and even a factor of political instability.

3. Trend Forecast

3-1. Private capital guided by the CCP to support designated industries

In mid-November 2020, Xi Jinping visited Nantong, Jiangsu Province, and pointed out that “since the reform and opening up of China, the Party and the

9. For more details on the brain drain in China's high-tech industries (mainly IT industry and semiconductor), see: Yu Zhou and Jinn-yuh Hsu, “Divergent Engagement: Roles and Strategies of Taiwanese and Mainland Chinese Returnee Entrepreneurs in the IT Industry,” *Global Networks*, Vol. 11, No. 3 (July 2011), pp. 398-419. Rui-Mei Hsiung, Guan-Rong Chen, and Yi-Ren Kuan, “Mechanisms of China's Cross-Border Innovation Networks: An example of the Patent Inventor Network of Semiconductor Companies in Mainland China,” in Lee, Tsung-Wing, and Lin, Tsung-Hung, eds, “*Unfinished Miracles: Taiwan's Economy and Society in Transition*” (Taipei: Institute of Sociology, Academia Sinica, 2017), pp. 496-539.

State have created favorable conditions for the development of private enterprises and the growth of entrepreneurs,” and urged that “private enterprises should learn from the best to support the country, assume social responsibility and help others to grow once they’ve become rich.”¹⁰ It is clear that the CCP is consciously sending the message that private enterprises must cooperate with the state to “invest wherever the Party tells them to”.

In April this year, Tencent announced that the group will promote the “Innovation for Sustainable Social Value” initiative not only by investing RMB 50 billion, but also by coordinating various products departments to support the development of basic science, education innovation, rural revitalization, carbon neutrality, elderly care, and digitalization

of public welfare projects.¹¹ Later, the partnership between Tencent and the GAC Group was also announced on the media day of the Shanghai Auto Show on April 19, 2021. The cooperation range from the establishment of a data platform spanning from production, manufacturing, sales to management as well as the acceleration of upgrades on the ecological and technological perspective of online taxi services.¹² According to Tencent, the investment strategy is in line with the two policy pillars included in “The 14th Five-Year Plan and Vision 2035”: first, to further develop the offline economy and promote the integration of advanced manufacturing and service industries; second, to fine-tune the current economic development model of “let some people get rich first” and to pursue “quality development” in the next phase to narrow

10. “Xi Jinping Stressed, During his Visit to Jiangsu, to Implement the New Development Concept and Construct a New Development Model to Promote High-quality, Sustainable Growth of the Economy and Society” , *Xinhua*, November 14, 2020.

http://www.xinhuanet.com/politics/leaders/2020-11/14/c_1126740143.htm

11. “Tencent Invests NT\$200 Billion to Promote ‘Innovation for Sustainable Social Value’. Ma Huateng: “It’s Just the Beginning” , *The Liberty Times*, April 19, 2021

<https://ec.ltn.com.tw/article/breakingnews/3504567>

12. “The GAC Group and Tencent Escalated Strategic Cooperation to Promote Platform Digitization and Ecological Development” , *Sina.com*, April 19, 2021.

<https://finance.sina.com.cn/tech/2021-04-19/doc-ikmxzfmk7696153.shtml>.

the gap between people's livelihoods and wellbeing.

Then another question emerged: apart from the fear of the CCP's autocratic power, why do private enterprises continue to follow the government's industrial policy? First, private enterprises must not only be ideologically aligned with the government, but more importantly, they must be able to earn the trust of the Party to ensure their long-term survival. Therefore, private enterprises that need to "demonstrate their loyalty" are expected to invest in "new strategic industries" as defined in "The 14th Five-Year Plan and Vision 2035" as well as on the revitalization of rural areas. Second, as the CCP still occupies the high ground in terms of domination of political power and state capital even after the economic transformation, private entrepreneurs are eager to seek political patronage in order

to maximize their own interests.¹³ Taking advantage of this motivation, the CCP released the following message in the "Opinions on strengthening the United Front in the private economic sector for the new age" (Sept. 2020):

"Optimize the structure of the private economic representative team via an appropriate inclination towards strategic emerging industries, advanced manufacturing industries, modern service industries and modern agriculture, etc." It shows that people in these industries are the talents the CCP expects to absorb in the future, and they will be given the right to represent private enterprises. That is, they may enjoy special political status in the future. It's understandable that it is economically rational for private enterprises to intentionally include these "strategic" industries in their investment plans in order to ensure political protection.

13. Although Wank believes that as market reforms deepen, the relationship between private entrepreneurs and the CCP is gradually moving toward a two-way dependency. But even though it is a symbiotic relationship, the private entrepreneurs still have an incentive to seek political protection for their own business development while they provide the resources the government might need as well. David L. Wank, "Bureaucratic Patronage and Private Business: Changing Networks of Power in Urban China," in Andrew G. Walder (eds.), *The Waning of the Communist State: Economic Origin of Political Decline in China and Hungary* (Berkeley, CA: University of California Press), pp. 153~183.

3-2. Conglomeration of private enterprises will be limited

According to the results of another round of conversations between financial regulators and Ant Group plus 13 other Internet platform companies in April this year, it was officially confirmed that financial services wrapped in the guise of tech innovation are prohibited as an act of “disorderly capital expansion”, and the next stage of administrative supervision will focus on divesting such companies from “illegal” financial services.¹⁴ Since 2019, the substantive controllers of large private enterprises, including Ma Huateng of Tencent and Zhong Shanshan, the founder of Nongfu Spring

Beverages, have stepped down from roles outside their main industries.¹⁵ This article suggests that the CCP financial bureaucrats may take the next step to prevent large private enterprises from becoming “conglomerates”.

In the process of capitalization, enterprises tend to form “conglomerates” to achieve economic scale and maximize profits. When a parent company combines several subsidiaries across different industries or the spectrum of a supply chain through cross-shareholding, a conglomerate is born. In East Asia, the most notable examples are the large enterprise groups found in Japan and South Korea.¹⁶ By minimizing internal

14. “Pan Gongsheng, VP of People's Bank of China, Answers Reporters' Questions on the Financial Authorities' Second Interview with Ant Group,” *Xinhua Net*, April 12, 2021.

http://www.xinhuanet.com/fortune/2021-04/12/c_1127321490.htm.

“Financial Authorities Jointly Interviews Some Enterprises Engaged in Financial Businesses on Online Platforms,” *Xinhua Net*, April 29, 2021.

http://www.xinhuanet.com/fortune/2021-04/29/c_1127393316.htm.

15. “Zhong Shanshan, China's Richest, Suddenly Resigned From Board Position, Wantai Biological Stock Price Plunged” , *Central News Agency*, January 14, 2021.

<https://www.cna.com.tw/news/firstnews/202101140351.aspx>.

16. Japanese plutocrats are called “keiretsu” , represented by large enterprises such as Mitsui, Mitsubishi, Sumitomo, Dai-Ichi Kangyo, Fuji and Sanwa; Korean plutocrats are called “chaebol” and are best known by Samsung, Hyundai and Lotte. The major difference between the two is that although a Japanese “keiretsu” is centered on the main bank for capital allocation, it's actually a “coreless” network, in which no single company can dominate the other group members. However, both have developed internal horizontal networks across companies in different industries and vertical supply chain networks within industries.

James R. Lincoln and Michael L. Gerlach, *Japan's Network Economy: Structure Persistence and Change* (Cambridge UK: Cambridge University Press, 2004), pp. 1~50.

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transaction costs and allocating capital efficiently, these groups quickly gain ground in the market while obtaining enormous political and economic influence. In South Korea, for instance, the “chaebols” (plutocrats) have an unparalleled position in the country’s economic development, but they have also become a problem: they are crowding out the country’s smaller enterprises and causing South Korea to be overly dependent on a handful of conglomerates for its economic growth.

In order to prevent large private enterprises from becoming conglomerates and gaining political and economic influence, the CCP is expected to limit the expansion of private enterprises. To move toward the objectives of “common prosperity” and “expanding the mid-level income group,”¹⁷ the CCP will not only invest in building a comprehensive social welfare and education system, but also force large private enterprises to yield more market space to small- and

medium-sized businesses. Moreover, in order to prevent from falling into the situation that the CCP must support the development of private enterprises, the extent of “disorderly capital expansion” of private enterprises must be limited. Lastly, to increase the reliance on the state and the need for political protection, it’s also necessary for the CCP to weaken the motivation and ability of private enterprises to expand their power.

17. “Promoting Common Wealth with High-Quality Development and Coordinating the Works of Preventing and Resolving Major Financial Risks,” *People’s Daily Online*, August 18, 2021.

<http://politics.people.com.cn/n1/2021/0818/c1024-32197312.html>.