The Development of Private Enterprise in Contemporary China: Institutional Foundations and Limitations*

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Abstract
This paper is an attempt to analyse the rapid development of private enterprises in the reforming era, with particular emphasis on the role of trust. We argue that trust in China, although family centred, has an extraordinary capacity to extend and be network-based. It is this capacity for trust and the shared family ethics and social norms that underlie it which provide new institutions for the growth of the private sector. The concept of trust therefore is further divided into three types, namely, trust in one’s own person, trust in interpersonal relations, and trust in systems.

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which correspond to three forms of capital, i.e. human capital, relational capital and institutional capital. Based on several reported cases of bankrupted private enterprises, the limitations of these institutions are discussed. These include some common problems that have surfaced among private enterprises, such as the high debt ratio of enterprises, familistic management and the weakness of personal trust.

The economic reform which started in the late 1970s has witnessed a dramatic development of private enterprise in the People’s Republic of China (PRC). Its rapid growth has not only surpassed the expectations of Chinese policy makers, it has also posed challenges to existing social theories. This is particularly true if the development of private enterprise in China is put into perspective with that in other reforming socialist countries, particularly in Russia and Eastern Europe. Compared with the “radical approach” as implemented in Russia and Eastern Europe, where the economies were reformed to follow closely the theoretical ideas of neoclassical economics, China chose a gradual, evolutionary approach with central planning and the state sector continuing to dominate the economy. Therefore, the radical reforms in Russia and Eastern Europe theoretically should have fared far better than the gradual approach followed by China. However, reality has proved otherwise. Not only has China achieved an unprecedented economic growth, but far-reaching social and political changes have also taken place, with continuity and stability during the reform era. Among all the changes, the development of the private sector commands the attention of scholars and policy-makers alike, and also prompts enquiry into the formation of the new institutions which are facilitating this extraordinary development within the constraints of a centrally planned economy. This paper is an attempt to analyse the institutional foundations of this development with particular emphasis on the role of trust.

It is widely believed that trust in China is confined only to family members or, at most, to broader forms of kinship, and that there is a dearth of trust among people who are not related to one another, which consequently prevents China from innovating organizationally and ultimately from developing modern corporations. In this paper, we argue that this is a misunderstanding of the nature of Chinese economic life, and that this misunderstanding has overlooked the capacity for trust, as well as ethical and social norms, that are well able to expand beyond family. Although trust in China is characterized as family centred, it also has an