

How state ownership hampered entrepreneurship in Chinese companies

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For state-owned companies in China, the significant detriment in employing innovation may be linked to the company's ownership structure, according to a new study on Chinese entrepreneurship by Chinese business experts at Rice University, the University of Hong Kong, Texas Christian University, Jilin University and Shantou University.

The researchers found that the more equity the state owned of a company, the less likely the company was to engage in strategic entrepreneurship (investing in research and development and other

innovations) to gain market share. This emphasis on strategic entrepreneurship in transition economies is critical as nations seek to revitalize existing state-owned companies. However, such efforts must be thought out and designed well, the authors said.

The findings are the result of the authors' study of 1,095 Chinese business-group-affiliated companies during a period of institutional friction in 1999; the researchers expected to find a potential conflict between emergent institutions encouraging strategic entrepreneurship and those still creating pressure for maintenance of the status quo. The authors examined how such institutional friction impacts firms' strategic choices regarding corporate entrepreneurship and innovation. The paper will be published in *Strategic Entrepreneurship Journal*.

"Although both formal systems designed to reward strategic-entrepreneurship activities and informal systems to develop new cultures are important in creating the desired strategic outcomes, their effectiveness is hampered by the embedded state philosophy," said Robert Hoskisson, one of the study's co-authors and the George R. Brown Professor of Strategic Management at Rice's Jones Graduate School of Business. "We believe that the results of this study provide insights for managers and policymakers in transition economies by highlighting the means and constraints that are available to encourage strategic entrepreneurship."

A transition economy is an economy that is shifting from a centrally planned structure toward a more free market. China is doing so very gradually. The former Soviet Union used the so-called "big bang" approach of very quickly privatizing state-owned firms, often through auction.

The researchers studied competing institutional philosophies measured through a company's founding leadership and ownership history and

through the impact of formal and informal controls emphasized in newly formed business groups and how they influence company actions. Formal systems were manifested in the use of objective financial control measures to reward and discipline member firms; informal control efforts to indoctrinate new values and norms were represented by the socialization and development of a strong group culture.

The authors found that the original institutional philosophy of state control and ownership remained a potent factor among the Chinese companies, while the new institutional philosophy in support of strategic entrepreneurship took place through business groups' informal and formal organization controls.

They also found that state philosophy caused rigidity and inflexibility for companies to react to the new institutional demands, thus weakening the positive effects of business groups' formal and informal controls on strategic entrepreneurship.

The authors advocated that managers and policymakers of state-operated enterprises need to be cautious about the consistency between the institutionalization of new organizational practices and governance and control of the firms. "Although the use of formal controls that rely on structuration to sanction and set norms for appropriate behaviors may be more effective in the short run, for long-term effectiveness, a supportive cultural change for an emphasis on strategic entrepreneurship is needed," the authors said.

Transition economies are a significant part of the world economy, the authors emphasized. "However, forward economic movement in such nations will require a greater understanding of strategic entrepreneurship in former state enterprises," they said. "This research has helped lay the foundation for a greater understanding, but more research is still required."

Provided by Rice University

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