

ECONOMIC FINDING

Special Deals from Special Investors: The Rise of State-Connected Private Owners in China

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The share of registered capital of connected private owners in China increased by almost 20 percentage points between 2000 and 2019, driven by increased investment from state-owned firms in joint ventures with private owners, and by increased investment from private owners with equity ties to state owners.

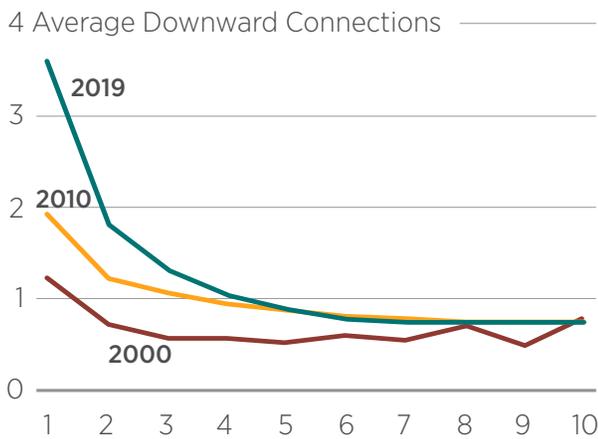
New private firms in China benefit heavily from investor relationships with state-owned firms or private owners that have equity ties to state owners. To document the importance of “connected” investors, the authors employed administrative registration data on the universe of Chinese firms from 2000 to 2019. These data provide information on the owner of every Chinese

firm, which the authors used to identify firms with connected investors defined as state-owned firms, or private owners with equity ties to state-owned firms.

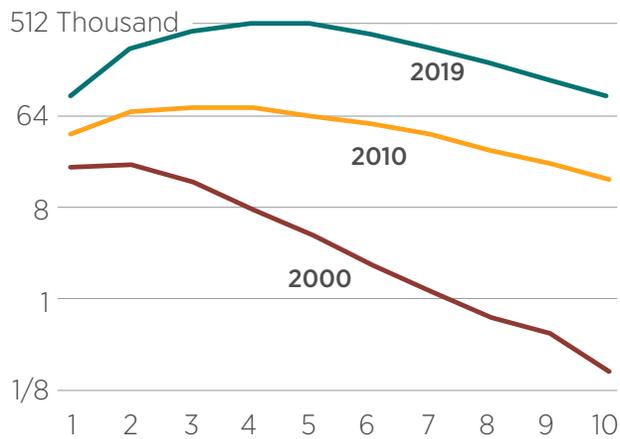
This ownership information reveals two key facts. First, there is a clear hierarchy of private owners in terms of the closeness of their equity links with state owners. In 2019, state owners had equity stakes in the firms of about 100 thousand private owners. These private owners are the largest in China and also hold equity in the companies of other, typically smaller, private owners. In turn, these private owners also invest in other, even smaller, private owners, and so on. At the very bottom of the hierarchy are owners that are up to forty steps away

Figure 1 • Expansion of Connected Private Owners (2000 - 2019)

Downward Connections per Owner



Number of Connected Private Owners



Distance to State Owners

Note: Left panel shows the average number of downward connections per private owner by distance to the state from 2000 to 2019. Right panel shows the total number of connected private owners by distance to the state from 2000 to 2019.

from the state owners at the top of the hierarchy and that do not invest in other owners. The very smallest private owners thus do not have any equity ties, direct or indirect, with state owners.

Second, the hierarchy of private owners with connected investors is a relatively recent phenomenon. In 2000, private owners with connected investors only accounted for about 16% of registered capital. By 2019, private owners with connected investors owned about 35% of all registered capital in China. The 19.5 percentage point increase in the share of connected private owners from 2000 to 2019 contributes a significant part of the increase in the share of all private owners over this period.

The growth of this hierarchy of connected owners is driven, in a proximate sense, by two related trends, broadly described here and in greater detail in the authors' paper. First, in 2000, only 12% of state owners had joint ventures with private owners. By 2019, about a quarter of all state owners had such joint ventures. The result is that the number of private owners with joint ventures with state owners increased from about 20 thousand in 2000 to more than 100 thousand by 2019.

Second, private owners associated with the state also now undertake more investments with other private owners. For example, the 20 thousand private owners with joint ventures with state owners in 2000 themselves had joint ventures with less than 1.5 other private owners in that year. In 2019, the 100 thousand private owners directly connected with state owners were themselves the "connected investor" for 3.5 other private owners on average. The result is that the number of private owners invested by the directly connected private owners (i.e., two

steps away from the state) increased from 23 thousand in 2000 to more than 300 thousand by 2019.

By 2019, the assets of connected private owners accounted for 35% of total assets in China, or about 45% of total assets of all private owners. At the same time, the share of connected state owners, the owners at the "top of the food chain" of the connected sector, was merely 21%, or 60% less than the share of connected private owners.

The authors estimate that the expansion of connected private owners may be responsible an average annual growth of 4.2% in aggregate output of the private sector between 2000 and 2019.