Corporate Governance in Today's China:

China's Political Regime and Economic System

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Abstract
Corporate governance holds an important place in any advanced market economy. In the case of China, we have watched the country's dramatic rise from the "economic opening" in 1979 under Deng Xiaoping to its current position as the world's second-largest economy. The gradual building of new institutions and new ways of governing economic activity in the market has been a crucial part of China's successful transition. Over the last four decades of reform and transformation the institutional environment shaping corporate governance has evolved into a robust system governing corporate actors in China today. While the 1980s and 1990s could be characterized as periods of close administrative governance and control by the state, these periods were also the era in which China was setting in place systems of governance that would allow corporations to be governed by a system of laws and rules, the "modern enterprise system" [*xiandai qiye zhidu*]. These periods would see new laws and regulations such as the Labor Law, the Company Law, the Joint Venture Law – laws and regulations that governed the ways in which corporations operate in the rapidly growing economy. In the 2000s, under the leadership of Hu Jintao and Wen Jiabao, it looked like the government was stepping back from direct administrative fiat, allowing this rule of law system to govern the economy. However, in the decade since President Xi's inauguration in 2013, we have seen a dramatic reversal of these trends, what might be called a rule *by* law system, where the government relies on new aggressive regulations that make it increasingly difficult to operate in China. In this new legal regime, local governments demand economic partnership in building strong local economies in exchange for positive rulings on corporate compliance with the new legal regimes. Through an analysis of the cases of Apple, Foxconn, and Alibaba, we show the ways in which corporate governance in China today depends, once again, on close relations with local governments.

Corporate Governance in Today's China

In this chapter, we examine the issue of corporate governance in today's China. The building of a stable corporate governance infrastructure has been an ongoing process over China's forty-plus years of economic reform. As with all of China's major institutional transformations over the four decades since the "Economic Opening" in 1978-79, the process has been gradual and experimental. However, over the course of the reforms, the institutional environment shaping corporate governance has evolved into a robust system governing enterprises in China today. Nevertheless, the system of corporate governance in China today lives in the shadow of the heavy hand of the state, the monitoring agent that stands as the gatekeeper for participation in China's massive and expanding economy. Influence is sometimes subtle and often hidden from view, but the power is real. The institutions of corporate governance are among the key tools the government has to compel corporations to contribute to society and economic development in ways that the government sees fit. As the entities with the power of administrative fiat to govern corporate entities, the governmental bodies can – and do – use that power to push corporations to contribute to economic development and social order in ways that match the government's goals.

In the pages that follow, we explore four trends that shape corporate governance in today's China. First, this discussion must be placed in the context of China's governance evolution over the last four decades. The eras of Deng Xiaoping, Jiang Zemin, Hu Jintao, and Xi Jinping have all been quite different, and the notion of corporate governance has varied significantly with each era of leadership. Second, we point to and discuss the key "formal" institutions that have been set in place in the building of what was once called "the modern enterprise system" (*xiandai qiye zhidu*) and how that system has evolved over the course of the reform era. Third, and most importantly, we discuss the "informal" aspects of how corporate governance *really* works in China today. The governance of the economy in the decade under Xi Jinping has been much different than it was under his predecessors, and, in many ways, we have returned to a system that depends deeply on informal influence and control within the context of emerging formal institutional controls. Finally, we discuss the ways in which China's Environmental, Social, Governance (ESG) as well as its global ambitions have reshaped corporate governance in today's China. To illuminate these dynamics, we rely on case analyses of three well-known corporations, Foxconn, Apple, and Alibaba.

Our core arguments in this chapter are this:

- First, the Chinese government at all levels – central, provincial, municipal, district, township, village – is focused on economic development and maintaining social order through the economic development process. Over the last four decades, China has built an institutional framework that has fundamentally transformed the ways in which corporations are governed in China. This reform process has not been guided by the market-driven radical break from the past seen in other transitions from plan to market, but, rather, by a gradual, experimental process in which the Central Government in Beijing has introduced new institutional forms that govern the ways corporations operate.
- Second, this formal (gradual) institutional process has evolved in complex ways both temporally but also spatially. The temporal dynamics can roughly be mapped onto the reform era periods that are tied to the major leaders of each epoch. Thus, in terms of the evolution of corporate governance, the eras of Deng Xiaoping, Jiang Zemin, Hu Jintao,

and Xi Jinping are quite distinct, and we illuminate the rough outlines of those differences here. Spatially, China is a very diverse marketplace. While we often think of China as a one-party authoritarian system operated out of Beijing, this is only partially true. We argue that the dynamism of the Chinese reform process is fundamentally tied to a very decentralized system in which provincial, municipal, and township leaders are incentivized to experiment with and innovate around the implementation of new regulations to achieve economic goals. Our favorite metaphor for this argument draws on Andrew Walder's (1995) brilliant analysis of "local governments as industrial firms," where local officials are managers of a business division that has Key Performance Indicators they need to achieve, and their career advancement depends on whether they can hit these KPIs.

- Third, while there has been a powerful stepwise process of building formal institutions around economic reforms in general and corporate governance specifically, the last decade has seen a re-emergence of the informal controls of corporate governance. The current administration's return to – or perhaps reinvigoration of – a Rule *by* Law system of governance has meant that corporate leaders need to attend to the informal aspects of governmental relations. Strong relations with government officials are necessary for positive outcomes in the assessments around corporate governance.
- Fourth, two major global initiatives have also shaped how corporate governance continues to evolve in China today. The world's Environmental, Social, and Governance (ESG) movement has also touched China, and the movement has had a significant impact on how corporations are governed in China today. In addition, China's global ambitions with companies like Alibaba and under the Belt and Road Initiative (BRI) have also shaped how corporate governance plays out for firms going abroad but also have implications for their operations back home in China.

To develop these conclusions, we use a multi-method approach for the research and analysis presented here. In the discussion of corporate governance, it is of course essential to track the major formal institutional changes that have been set in place throughout China's reform era. There are a number of studies that have done this work, including Clarke (2003), Jiang and Kim (2020), Guthrie (2012), Guthrie and Wang (2015), Guthrie et al. (2015), and many others. We add to this work with a discussion of the changes in the last decade in particular. While citing and acknowledging many of the key institutions that have come to shape corporate governance in China today is important, in our experience, what readers want to know is how these institutions work in practice. Accordingly, we rely on interviews and ethnographic work gathered through years of advising companies negotiating with suppliers and municipalities in the Chinese market. Chien, Gao, and Long are all based in China and have worked with, advised, and led companies navigating the Chinese market for many years. In addition to his academic work on the topic, Guthrie has also advised several US corporations operating in China. In the analysis presented below, we rely on the authors' firsthand knowledge of corporations navigating China's system of corporate governance. In addition to our analysis of the formal corporate governance institutions and how the governance environment has changed over time, we use three case studies to illuminate the key points we put forward here. The three case studies presented here are Foxconn, Apple, and Alibaba/ANT Group. One final note on methods: where the data come from firsthand ethnographic experiences of the authors in working with various clients and employers, we have been careful to ensure that no firsthand data employed here violated

informal confidences or formal Nondisclosure Agreements (NDA). For two cases, Foxconn and Apple, which we rely on extensively here, we have ensured through legal representation that our analysis here does not violate the authors' NDA agreements.[1]
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Building New Institutions of Corporate Governance in China's Reform Era
As economic and political reforms swept across the world in the second half of the 20th Century, many scholars have studied and prescribed transitions from plan to market. Scholars studying and advising the governments of the former Soviet Union and Eastern Europe advocated for "shock therapy" – a rapid freeing of prices and trade liberalization. Broadly, this group operated from core ideas found in neoclassical economic theory that markets will effectively organize economies through a basic adherence to market signals to consumers – individuals and organizations – through supply and demand. However, markets need to be given the freedom to do so, and rapid liberalization needed to take place to set these economies on a path to successful economic transition from plan to market. Reviewing the work of scholars like Janos Kornai and Jeffrey Sachs, Guthrie et al. (2015) have described the model in the following way:

> During the 1980s and '90s, economists and institutional advisors from the West advocated the rapid transition to market institutions as the necessary medicine for transforming communist societies. This line of reasoning is well-known, with prominent figures producing many important theoretical and empirical assessments of the transformation process of many planned economies. The argument here was that private property is a necessary institutional foundation of a market economy and, thus, communist societies making the transition to a market economy must privatize industry and other public goods. Private property, the argument goes, is the most efficient way to create the incentives that are necessary for a healthy, functioning market economy. Thus, privatization is seen as the cornerstone of economic efficiency and, by extension, profitability. The radical members of this school argued that rapid privatization – the so-called shock therapy or big bang approach to economic reforms – was the only way to avoid costly abuses in these transitional systems.

Over the decades since its economic opening in 1979, China's path has been very different. In China's reform era, the country has gradually built new institutions that have governed the transition from plan to market. With guidance from the center, China has adopted a gradual measured process that begins with broad, sweeping changes from above, as Beijing lays the groundwork for the institutional frameworks that govern the economy and society. However, these broad, sweeping institutional changes are often vague and experimental, and they have always stopped short of radical change such as rapid liberalization programs advocated by the

[1] While the ideal and correct methodological approach would be to obtain all formal agreements to employ data and observations in future writing, this was not possible in all cases. The authors of this chapter have had long careers as corporate advisors, corporate advisors, researchers, and academics (in the case of Guthrie), and the process of obtaining up-front subject agreements was not always possible. One of the company case studies, Apple, is famously private, maintaining extensive and deep NDAs and would not openly agree to up front approval of the case. When Guthrie joined Apple, while the company preferred that future writings would never include Apple, both parties acknowledged this was not possible. Thus, as Guthrie's legal counsel worked with the Apple legal team, the NDA agreement was written in such a way that personal experience and information could be used as long as it did not violate company secrets or private conversations. Guthrie's legal counsel has worked with the Apple legal team in the years since 2019 (the year he left the company) to ensure that the spirit of this agreement was being met.

likes of Kornai and Sachs. These broad institutional changes have also created the space for gradual, incremental, and experimental institutional innovations of the local markets – provinces, municipalities, and townships – below (Guthrie 2012).

Concerning China's reforms, several scholars have examined the ways in which the country has defied these prescriptions and, in doing so, become a new model, a paragon, if you will, of economic transition from plan to the building of a vibrant market economy (Naughton 1995; Walder 1995, 1997; Guthrie 1997, 1998, 1999, 2001, 2005, 2012; Guthrie et al. 2002; Guthrie et al. 2020a, b, 2021a-j). Two core ideas unify all these analyses of China's reforms. First, as the Central Government resisted prescriptions for rapid privatization and general liberalization, it is a mistake to interpret this resistance as a lack of interest in building a viable and even vibrant capitalist market economy. Indeed, China has made the transition to a vibrant market economy, but it has done so through a gradual and experimental process of institution building. Second, the system has been radically decentralized, placing a great deal of experimental and innovative power in the hands of provinces, municipalities, and townships.

Here again, there has been temporal variation across the decades of reform since China's economic opening in 1979, and the institutions that would emerge to govern the economy. These variations roughly map onto the leadership of each period. In the Deng Xiaoping era (1979-1989), the key area of focus could be summarized by the idea of opening the economy and putting people to work. When Deng Xiaoping ushered in the reform era, a conservative estimate would place over 700 million citizens living in abject poverty. China needed cash and people and localities needed the freedom to generate income and revenues through an emerging private economy. The 1980s saw the emergence of economic categories of household businesses (*getihu*) and private enterprises (*siying qiye*). Today, more than 400 million Chinese citizens, or about 30 percent of the population, work in these organizational forms.

If there was focus on corporate governance over these new organizational forms, they would come at the end of the 1980s and pick up momentum in the 1990s, the era of Jiang Zemin (see Guthrie [2012] for detailed discussion).[2] Laws like the *Enterprise Bankruptcy Law* (1986), the Independent Accounting System (*duli hesuan*), the *Enterprise Law* (1988), the Company Law (1994), and the Labor Law (1995) would lay the foundation for the regime of corporate governance that would emerge. In these early years, there was a close connection between the emerging institutions of corporate governance and the local governments that were monitoring the organizational adherence to following these rules. Provinces, municipalities, municipal districts, and townships were all close monitors of the ways in which organizations in their jurisdictions adhered to these new institutional rules.

Beyond these new legal regimes, perhaps the most critical institutional change for corporate governance that would emerge organizationally came in 1988, when the State Council established the State-Owned Assets Management Bureau under the Ministry of Finance to govern and coordinate the management of all the country's state-owned assets. Over the course of the 1990s, several reforms oriented toward corporate governance were passed: "unified guidance, decentralized management" (*tongyi lingdao, fenji guanli*); "national unity, classified

[2] There were corporate and economic laws passed over the course of the 1980s, such as the Patent Law (1985), but the real institutions of corporate governance, which is the focus of this chapter, really began in the late 1980s.

monitoring, and autonomous operation" (*guojia tongyi suoyou, zhengfu fenji lueguan, yinye zizhu jingying*), which implied unified ownership by the state, separate supervision by local governments, and independent management by the enterprises themselves. This period could still be described as close monitoring of the local governments and the organizations under their jurisdictions. According to Guthrie (2012), things really began to heat up in the corporate governance space during this time period:

> In 1998, Zhu Rongji merged the State-owned Asset Management Bureau System into the Finance Ministry System. Then, in 1999, the State Council passed key decisions that emphasized the strategic restructuring of the state sector. Between 1999-2003, in order to better managing state-owned assets, the State Council gradually announced several documents to set up a specific department to supervise and administrate the state-owned assets and some relevant documents to further emphasis on the responsibilities of this department. As a result of the 16th CPC National Congress *Government Reform Plan* [*jichang gaige fangze*] the State-Owned Assets Supervision and Administration Commission (SASAC) was formally established (after more than a decade of gradual development). The supervision scope of SASAC is the assets controlled under central state-owned enterprises. Assets owned by local state-owned enterprises are managed by local SASACs, which were set up and governed by provincial and municipal levels governments. Thus, the system of separately owned, separately supervised was set up among central SASAC and local SASAC. Today, SASAC is the most powerful state organization managing across industries in China.

Also relevant for corporate governance in China today are the founding of the Shanghai and Shenzhen stock exchanges. On December 19, 1990, the Shanghai exchange opened its doors a little over a two decades into China's transition to a market economy. The Shenzhen exchange opened shortly thereafter. A series of regulations followed. These included "The Opinions on Standardizing the Joint Stock Limited Companies" and "the Provisional Regulations on the Administration of Issuing and Trading of Stocks." Shortly thereafter, the *Securities Law of the People's Republic of China* (PRC 1999) was adopted in 1998 at the Ninth National People's Congress and took effect in July of 1999, thus institutionalizing the legal basis for the standardized operation of listed companies. In 2001, the Central Government passed *The Tentative Measures for Decreasing State Shareholding* (PRC 2001).

Yet, as China has been systematically constructing the institutions of a publicly traded economy, even in the area of public ownership of listed companies, we must acknowledge the complexities of enterprise-state relations in the Chinese model, as the government's receding from control over publicly listed state enterprises has, like every other institutional change in the Chinese economic reforms, been a gradual process. The companies listed on China's domestic stock exchanges are becoming "privatized" in some ways. A typical ownership transformation for a state-owned enterprise would allow the state to retain between 30 and 40 percent of the company's shares; between 30 and 40 percent of the shares are designated for institutional shares; the remaining 30 percent of shares are designated for public consumption as free-floating shares.

For organizations that emerge from the state sector and work toward distribution by selling shares operate in a complex system where local state offices still carry a heavy responsibility of governance and control. Figures 1 and 2 (originally published in Guthrie et al. 2015) show the complex web of organizational relationships that define corporate governance in China today. We see a system in which state offices maintain a close and influential role even in publicly traded firms, including formerly state-owned firms that have gone public. Fully private firms do not require the same ownership structure in terms of the distribution of shares, but there is still the close monitoring and relationships with local state offices that are depicted in Figure 2.

Figure 1: Ownership of Publicly-Traded Firms

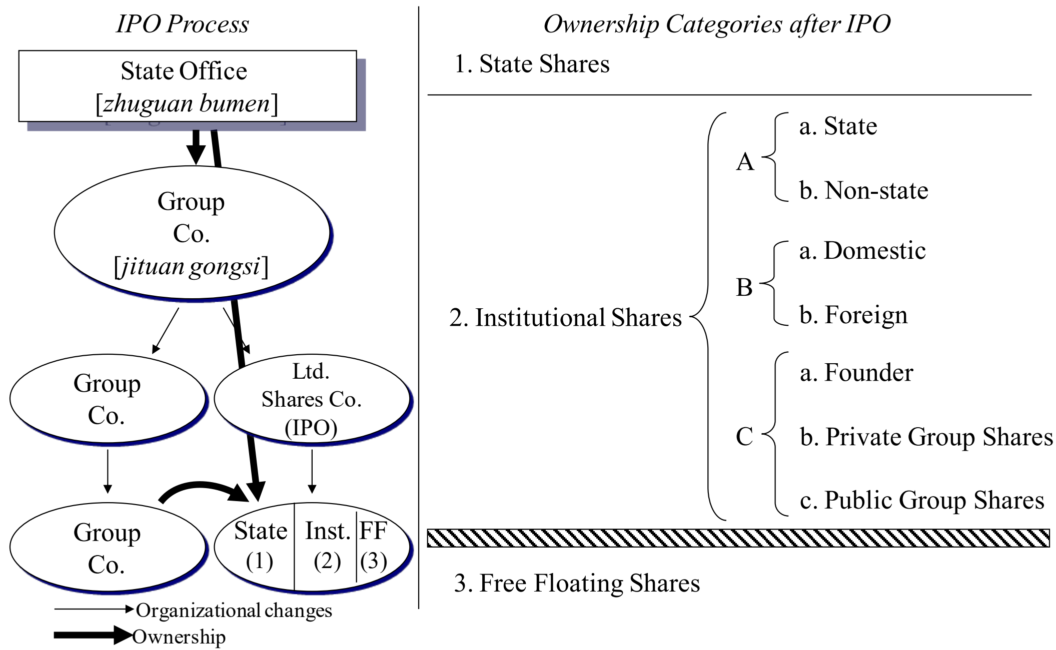
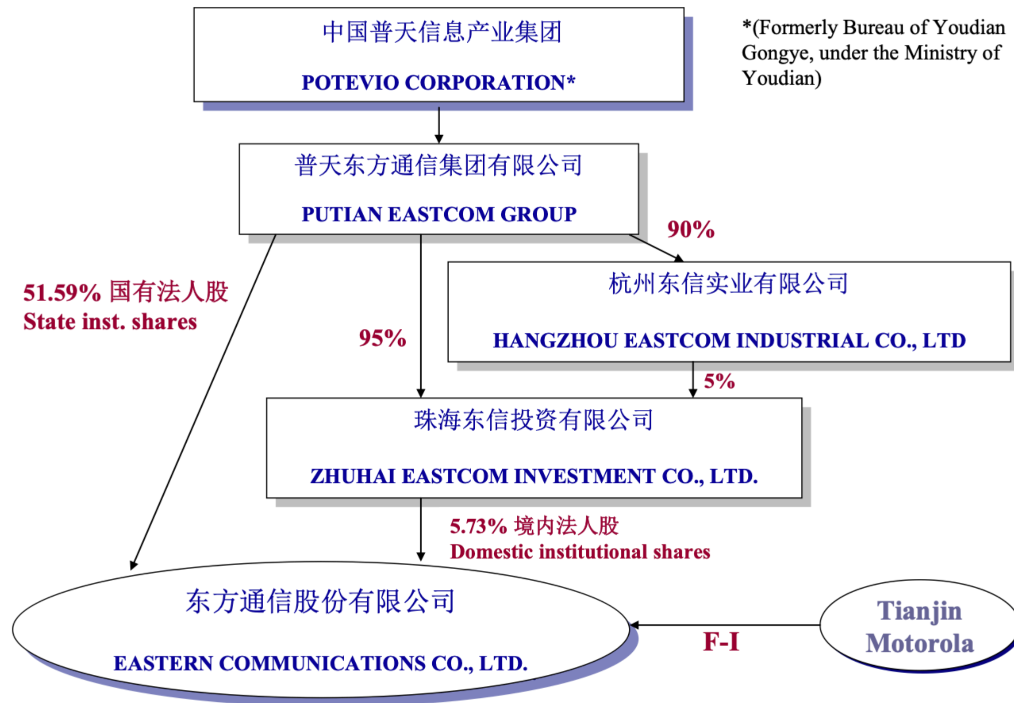


Figure 2: Ownership of Eastcom



In the private sector, we saw the continued rise of corporations like corporations like Huawei and the emergence of powerful entities like Alibaba and Tencent. While organizations such as these were privately held and thus increasingly under the governance control of individual and institutional shareholders, they were still heavily under the informal influence of the local municipal jurisdictions in which they resided, in these cases Shenzhen (Huawei and Tencent) and Hangzhou (Alibaba). Local governments to which all corporations – private, state-owned, or joint stock companies – oversee the implementation of all national corporate governance laws that govern corporate behavior.

Corporate governance in China is not only about the formal institutions that govern corporate action and the local governments that adjudicate corporate behavior in their localities, it is also about local economic development. There are strong incentives (KPIs) tied to economic development, and these local incentives create the conditions for favorable governance conditions. As we have noted previously, economic development in China is fundamentally shaped by government guidance and centralized control. There is a lot of strategic planning going on in five-year plans, ten-year plans, and twenty-year plans, as well as many centrally driven institutions of corporate governance (many of which are described above). While we often think of the Chinese government as an authoritarian, protectionist, and centralized party in Beijing, that is only one side of the government. Local governments are the engines driving China's growth. Indeed, the Chinese government is an extremely decentralized and entrepreneurial system of district and township governments. The mayors of China's municipalities, districts, townships, and villages behave like corporate CEOs, focusing on Key Performance Indicators (KPIs), pursuing foreign investment, and advancing their careers through

the financial and economic achievements in their districts and townships. But local governments do not do it alone. They do it through close coordination with China's private sector and with foreign investors from abroad. Thus, again, there are strong incentives to create favorable regimes of corporate governance.

The final era in the transition period is the current era, the era of Xi Jinping. Under President Xi, we have seen a re-emergence of the informal side of corporate governance emerge. During this period, we have seen the passage of several different laws that influence how corporations operate. Take, for example, the Labor Dispatch System (2014), which was an amendment to the Chinese Labor Law. The new Regulations on Labor Dispatch (Interim Regulations) were issued by the Ministry of Human Resources and Social Security and became effective on March 1, 2014. Dispatch labor is the system by which migrant laborers, the so-called floating population, are moved around the country to work at factories where there is a spike in the need for labor. The Labor Dispatch Interim Regulations decreed that companies were limited to ten percent of their employees as dispatch labor. Yet, many firms have a much larger portion of their workforce as being among the dispatch labor force. In other words, it was a new regulation that would make it impossible for firms to comply. As a result, many firms were compelled to curry favors with local officials so that their violations of the new regulations would be ignored. In the era of President Xi, we have seen many cases such as this: regulations set in place that make it impossible for corporations to comply and thus incentivized to work closely with local officials to find some wiggle room in the enforcement of the law. Institutions and a continued consolidation of the Party's direct hand in corporate governance have continued during this period. For example, in 2021, the Central Enterprise Unit issued the document "Opinions on Strengthening the Party's Leadership in Improving Corporate Governance by Central Enterprises (关于中央企业在完善公司治理中加强党的领导的意见). The key point here is that, over the last decade, we have seen the re-emergence of the Party as playing a much closer role in the monitoring of corporate governance behavior of major corporate players than we saw in the era led by Hu Jintao.

Case Studies 1 & 2: Foxconn in Zhengzhou, Apple in China

As is hopefully clear in the above discussion, there is an intimate dance between the corporations themselves – be they Chinese State-Owned Enterprises, Joint Stock Companies, private corporations, or foreign-invested corporations – and local district and municipal governments, which are primarily interested in economic development. These local governments have the power of administrative fiat to approve or disapprove of how the corporations are behaving and contributing to society. The rules and approval processes of corporate governance become the tools local governments (and in a few select cases the national government) must force corporations to show up and contribute to society the way they want them to. Thus, corporate governance is about compliance and the ways in which corporations implement and follow the rules set forth by the Chinese government. However, it is also one of the key mechanisms the government has to force corporations to contribute to society in a way that they see fit.

In this section, we introduce two case studies of how corporate governance operates in China today. The first case is that of Apple and Foxconn in Zhengzhou. Together Apple and Foxconn work with about 1,600 local Chinese suppliers, so this story is really about the engagement with local governments over the operations of their Chinese suppliers. Thus, like in Figure 2 above,

we see a complex web of organizational relationships with state (municipal) offices, foreign investors, and Chinese corporations.

On May 25, 2017, Zhengzhou made the transition from the solid ground of Tier 2 Chinese city to the hallowed land of Tier 1. In China, cities are ranked based on several criteria that place them into Tiers 1-6. While the Chinese Government releases no specific data on how cities are ranked, the financial magazine, Yicai Global, tracks these rankings and assesses them based on GDP, per capita GDP, commercial resources and the extent to which a city serves as a commercial hub, administrative level, and commercial dynamism. As of 2017, Zhengzhou now sits in this category of the top cities in China. But how did it get there?

In March of 2012, Tim Cook visited an iPhone production plant in Zhengzhou City on his first trip to China as the CEO of Apple. Before its investment in Zhengzhou, Foxconn had invested in 22 cities in mainland China, including 12 factories. How did Zhengzhou as a late arrival to this party become a leading player in this important industry? Foxconn is the world's largest provider of electronics manufacturing services and Apple's biggest contract manufacturer. Foxconn's investment in mainland China began in Shenzhen in 1988. Before the Zhengzhou plant was completed, Shenzhen had been Foxconn's largest production base, and currently, Shenzhen still retains Foxconn's China headquarters and R&D center.

In 2008, the relationship between Shenzhen and Foxconn began to weaken, as a number of problematic issues strained the relationship between Foxconn and the Shenzhen municipal government. Shenzhen's rising wages were eroding Foxconn's profits. A series of employee suicides occurred at the Foxconn factory in Shenzhen leading to a significant rise of scrutiny by the Shenzhen municipal government. Under the pressure of the financial crisis, Foxconn was criticized for having a tax contribution significantly lower than the industry average. And Shenzhen's new corporate favorites like Huawei and BYD were generating higher output per area unit. Although the Shenzhen government was still working with Foxconn, anyone with a discerning eye could see that Foxconn's life in Shenzhen was becoming difficult. In other words, the company's inability to deliver as a strong corporate citizen strained the relationship between Foxconn the company and its corporate governance overseer.

Henan Province started courting Foxconn as early as 2007, under the leadership of a task force lead by the Mayor of Zhengzhou. However, Foxconn did not show much interest in Zhengzhou at the time. Early reports revealed that the company's initial impression of Henan was not good: a poor province that could supply a significant migrant labor force, but little more. However, after 2008, Foxconn's founder and CEO, Terry Gou, finally made up his mind to begin to move Foxconn's production base inland. Foxconn searched widely, negotiating with local governments one after another, intentionally or unintentionally creating a situation of "too many monks and too little gruel." Gou, who had been somewhat embarrassed by the negative press in Shenzhen, became a key protagonist for inland provinces – cities that entered his vision were Chengdu in Sichuan, Taiyuan in Shanxi, Wuhan in Hubei, Zhengzhou in Henan, and Chongqing and Tianjin, which are both provincial-level cities.

At the time, Foxconn seemed to prefer Tianjin, and Zhengzhou was viewed as a backup. Zhengzhou finally won the competition because of its lower overall costs, which is critical to the

electronics contract manufacturing industry where gross profit margins usually hover around 10%. Zhengzhou is located in Henan Province. Henan has a population of over 100 million people and a large supply of low-cost labor. In 2010, Foxconn had 800,000 employees in mainland China, nearly one-fifth were from Henan. Zhengzhou is the largest transportation hub in China, with high-speed rail lines running in eight directions. Starting from Zhengzhou Airport, a 1.5-hour flight can cover two-thirds of major cities and three-fifths of the population in China. The introduction of Foxconn became a governor's project, Henan Province gave Foxconn favorable conditions in terms of government co-investment, cheap land and tax incentives. Though never revealed, it is estimated that it cost Henan about 12 to 15 billion yuan or $1.8-2.3 billion for Foxconn's Zhengzhou project.

In the project contract signed at the beginning of July 2010, Foxconn proposed a stringent schedule to test the execution capability of the Zhengzhou government. The Foxconn factory is in the Zhengzhou Airport Economic Zone. A state-owned construction company in Zhengzhou arranged for 2,000 workers to work in three shifts 24x7, the renovation of standard factory buildings of 62,500 square meters was completed in less than a month. Because the available plant area was not big enough, a textile company that had been in the Zone for a long time was "persuaded" to move out immediately by the Zone management. The special cables and air compressors required by Foxconn's plant were not available in the market, the government therefore stopped subway construction in Zhengzhou and transferred the same equipment and products to ensure Foxconn's needs. On August 2, Zhengzhou Foxconn officially went into production. It took only one month from the initial investment agreement to the landing of the first batch of parts.

The Zhengzhou municipal government's ability to deliver on a speedy launch of Foxconn's production was impressive. Starting in mid-September, more than 6,000 construction workers were working day and night on a large construction site in Zhengzhou Airport Economic Zone, five kilometers north of the airport runway. The twelve-month project was completed in four months. At the end of 2010, a state-of-the-art factory building with a total construction area of 600,000 square meters was completed. Then, a labor army of 100,000 strong, recruited with the support of the government, joined assembly lines in the new factory, where popular iPhones went through final assembly and then shipped to all parts of the world by air. Today, the mega plant of Zhengzhou Foxconn has over 200,000 employees, hosts over 90 production lines, and conducts final assembly for about half of the world's iPhones.

The Foxconn project has brought Henan Province's electronic communication equipment manufacturing industry, a new industry to the province with annual sales that now exceed 300 billion yuan. The project has brought Zhengzhou a new title – iPhone City. Before Foxconn landed in Zhengzhou, Henan hardly produced mobile phones. In 2014, Zhengzhou Foxconn exported 72.12 million mobile phones with a value of 127.6 billion yuan or $20.7 billion, making it China's largest export company. In 2016, the number of mobile phones made in Henan reached 259.2 million, of which 257.5 million were produced in Zhengzhou. In the same year, the output of non-Apple mobile phones surpassed Apple mobile phones for the first time. Foxconn now has factories in 8 cities in Henan Province, most of which are business units supporting Zhengzhou Foxconn.

In addition to economic benefits, Foxconn has also produced tremendous social value. Foxconn has exerted a subtle influence on Henan, a large agricultural and populous province with an urbanization level of only 40% ten years ago. Most of Zhengzhou Foxconn's employees are migrant workers, and their lives have been changed by Apple and Foxconn. After being baptized by local urbanization and modern assembly lines, they have promoted the urbanization and industrialization of Henan Province.

Although Foxconn has increased Zhengzhou's exports by many fold, its contribution to Zhengzhou's GDP may be lower than we might imagine. It is estimated that Foxconn adds about 30-billion-yuan GDP to Zhengzhou, less than 3% of Zhengzhou's total GDP. Foxconn has contributed more than 100-billion-yuan GDP to Henan, while the province's total GDP exceeds 5.4 trillion yuan in 2019. Is Foxconn important to Zhengzhou? Very important. While it might be a stretch to say that, without Foxconn, Zhengzhou's economy would collapse, but there is little doubt that the economy has transformed in fundamental ways through this relationship.

There is another part of this story that has to do with labor. In China's powerful manufacturing economy, one of the critical forces is the massive migrant labor force, about 250 million people moving around the country providing a "seasonal" labor force spread across China's integrated supply chain. For years, the so-called floating population has fueled the Chinese manufacturing miracle. But, in some ways, they have also been second-class citizens of sorts because of China's household passport laws. The interesting thing to consider here is how Zhengzhou has dealt with this population in the years since Foxconn started making iPhones in Zhengzhou in 2010. With this influx of workers, Zhengzhou would be transformed into Apple City. As noted above, in Zhengzhou, Foxconn has built more than 4 million square meters of factory buildings, more than 2.5 million square meters of blue-collar apartments, and employed more than 200,000 people.

Most of Zhengzhou Foxconn's employees are migrant workers, and their lives have been dramatically changed by Apple and Foxconn in a number of ways. First, Foxconn provides a legal and stable employment environment. Foxconn signs labor contracts, pays salaries in full and on time, pays social insurance and housing funds, and conducts regular occupational health checks. Working at Foxconn, many migrant workers have achieved stable employment for the first time since entering the city, and, for many, it is their first formal job in their lives. Second, stable income provides the material basis for migrant workers to live in the city, support their basic living and consumptions. At Foxconn, the average income of migrant workers is basically the same as the average annual salary income of local urban private sector employees. In 2019, the average salary of employed persons in urban private units in Zhengzhou was $7,445. Third, the living facilities and working environment provided by Foxconn help migrant workers to form urbanized living habits. Blue-collar apartments provide air-conditioning, water heaters, separate bathrooms and 3rd party property management; migrant workers from different places communicate in Mandarin instead of dialects; whether they work or go out, they must follow the instructions and the guidelines of public signals.

All of these dynamics help migrant workers integrate into urban life in terms of employment, adaptation, and cultural and psychological recognition. When the household registration system reform enables migrant workers to have a household passport (*hukou*) in the city where they live, it is natural for migrant laborers to become true urban residents. Based on our research, more and

more Zhengzhou Foxconn migrant workers have adapted to urban life and want to stay longer if possible. Some migrant workers have bought housing in Zhengzhou; some children of migrant workers are studying in schools near the factory. The urbanization of migrant workers is a crucial part of China's urbanization strategy and an important way to increase the residential consumption in the city where they are located.

So here we have a case of a tight partnership between a Taiwanese manufacturing giant and the Zhengzhou local government. But this is not just a story of the relationship between Foxconn and Zhengzhou. Foxconn is the final assembly producer for several electronics giants producing products like mobile phones (e.g., Huawei, Apple, Xiaomi, Oppo, Vivo). But this final assembly plant is only the tip of the iceberg for the Henan economy. Apple, for example, works with over 1,600 Chinese suppliers, many of them located in Henan province. Thus, the Henan and Zhengzhou relationship with Foxconn has been a boon for the local economy.

Nevertheless, this is more broadly a story of local economic development in China, and it is one that is intimately tied to corporate governance. The Zhengzhou government has done an exceptional job of attracting foreign capital, building a manufacturing ecosystem, weaving together public services for new residents through public-private partnerships. The Zhengzhou Foxconn project is a win-win – Foxconn has made Zhengzhou successful and vice versa. The project of Apple and iPhone City in Zhengzhou has been a key part of the growth of Zhengzhou as an economic center of China. But this has been a broadly defined effort of transformation by an entrepreneurial local government. We have seen this in China before, and Zhengzhou is but one of many examples of local economic development. This is the story of entrepreneurial municipal and provincial governments, competition over and partnerships with powerful foreign investors, public-private partnerships, and the dynamic use of a powerful migrant labor force. It is the story of the rise of a new Tier 1 Chinese city.

It is not difficult to see the ways in which the incentives around building close corporate ties might influence corporate governance relations with the overseeing governmental body overseeing Foxconn and many of its suppliers. An additional data point in this example is closely related to and deeply intertwined with the Zhengzhou-Foxconn dynamics depicted above: Apple. We would remind readers here that one of us worked for Apple as the head of Apple University in China, which included advising the Apple Executive Team on the company's negotiations with the Chinese government (see, e.g., Guthrie 2018).

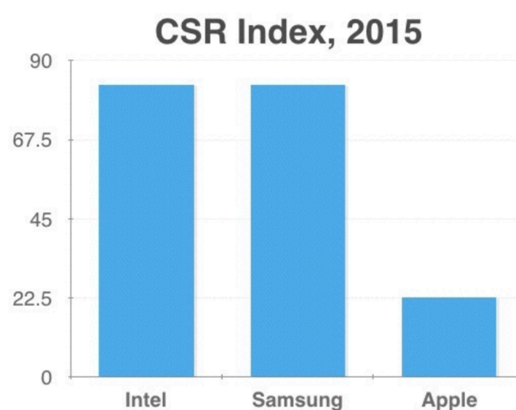
So where does Apple fit into this discussion? Despite the popularity of Apple's products in China, in 2013, the company seemed to increasingly be under attack by the Chinese Central Government. The first shot across the bow came on Consumer Day, March 15, 2013 (the first Consumer Day over which Xi Jinping presided). On the nationally televised show, Apple was accused of "unparalleled arrogance," as a "greedy firm that treated locals as second-class citizens." Thus, starting in March of 2013, there has been a steady stream of signals that the current regime will not continue to allow foreign companies – particularly in technology and related sectors – to continue to operate under the freedoms they enjoyed from 2002-12. The direct threats to this operation will not be explicit or clear, as such explicit threats are against World Trade Organization (WTO) rules. However, the new legal regimes plus the growing

difficulties Apple is experiencing plus the collective response of the majority of other major competitors in the technology space suggest that the threats are real.

In November 2015 and 2016, the State-Owned Assets Supervision and Administration Commission (SASAC) and the Chinese Academy of Social Sciences (CASS) released reports on the extent to which the top 100 global corporations give back to China. The report focused on CSR, and many publications (sina.com, tencent.com, *The South China Morning Post*, and many others) noted Apple's poor showing in the assessment compared to our peers – in 2015, Apple scored 22.5 on a scale of 1 to 100, where companies like Samsung and Intel scored 80+ (Apple scored similarly, 25.3 in 2016). However, the more damning articles looked beyond the CSR assessment to a broader assessment that is common with respect to Apple's operations in China – Apple is that foreign company that does nothing in the way of partnerships here, relies on cheap Chinese labor to assemble its products, and makes money hand over fist in China, and contributes little to Chinese society.

In the most glaring example, the popular blogger, Wang Chao, whose blog was picked up widely by the likes of Tencent and Sina, took the report and issued an excoriating analysis comparing Apple's presence in China to that of Samsung. At one point, Wang asserted, "Apple [has] never invested much in China other than in advertising. Until now, Apple only has offices in Beijing and Shanghai, with a growing number of retail stores. Its revenue, on the other hand, has skyrocketed from 1 billion USD to 38 billion USD in the past five years... It goes without saying how important China is to Apple. As time passes, China may become the most important market other than US, so Apple's attitude toward China, seeing it only as a sales destination is not sustainable."

Figure 3: Results from CSR Study Conducted by SASAC and CASS



Then in April 2016, Apple was forced to shut down iTunes and iBooks after China's online media regulator, the State Administration of Press, Publication, Radio, Film and Television, required the closings. This action came seven months after the operations were opened. The shutdown was linked to China's new Cybersecurity Law (2015), which bars foreign-owned companies from publishing content online in China. This move reflected China's ongoing

determination to “safeguard China’s information security” while also allowing the central government to supervise the majority of Internet content in the country.

So here we have a puzzle: Apple was probably China’s single largest foreign investor, spending more money in China than any other foreign company in the world; Apple has probably spent more on social causes like environmental sustainability and education than any other MNC; and, yet the company is regarded by important organizations like SASAC and CASS as contributing little to Chinese society. What was going on?

The answer could be found in the fact that the current regime had returned to the kind of expectations that were explicit in the 1990s (pre-WTO accession) – if MNCs are not helping to uplift Chinese partners technologically, they would not be welcome in China. As China aspires to transform itself from a manufacturing juggernaut to a hub of indigenous technological innovation, technology transfer, knowledge sharing, and management practice are perhaps *the* most important aspects of how foreign firms are viewed in China, particularly in the technology sector.

Very quickly, we saw announcements of joint ventures from Cisco, Hewlett Packard, Dell, Microsoft, Qualcomm, IBM, and Intel. We have not seen such a flurry of JV activity as this since the 1990s – and perhaps never in such a compressed timeframe. Many of these announcements came with much fanfare and bluster, however, reading between the lines and knowing some of the behind-the-scenes details of what was required in these deals (for example, the giving up of source code in the cases of IBM and Microsoft), we can be sure that these relationships came under a certain amount of duress.

Unfortunately for Apple, the organizational structures the company operates by in China did not match the government’s conventional view of what a deep partnership in China looks like. Apple has among the deepest penetration of any foreign company operating in the China market and deep penetration in the supply chain, yet we do not have the same company infrastructure as many of the other big players in China. Among our organizational entities in China – Apple Computer Trading (Shanghai) Co., Ltd. (151); Apple Procurement & Operations Management (Shanghai) Co., Ltd. (166); Apple Trading (Shanghai) Co., Ltd. (186); Apple Electronics Products Commerce (Beijing) Co., Ltd. (183); Apple Solutions Consulting Services (Beijing) Co., Ltd. (205); Apple Technical Services (Shanghai) Co., Ltd. (207); and the Beijing R&D Center (212) – none signal the type of commitment or partnership that the Chinese government has come to associate with technology transfer.

In pre-WTO-accession China, the government’s point of view was very clear: if you want access to China’s internal market, you must find a partner (or several) and help them to become better – largely through technology transfer but also through knowledge spillover in the area of management practice. For example, one of Apple’s competitors, Samsung, which has been operating in China since the early 1990s, has partnerships (either as WFOEs or JVs) with 39 Chinese entities. These types of relationships are explicit “cooperative partnerships” (*hezuo huoban*) [合作伙伴], and they are not just viewed favorably by the Chinese government. They are a form of protection against government interference.

Apple suppliers were also feeling the pressure. At the time, Apple worked with about 1,600 Chinese suppliers, yet the company did not have any formal cooperative partnerships with these firms, indeed, it did not have formal "cooperative partnerships" with any of its supply chain partners. This system worked very much in favor to Apple's presence in China in the 2000s – 2001-2013. However, with President Xi's ascendence, a signal was sent to Apple – recall the Consumer Day call out to Apple (detailed above), which occurred the day after President Xi's inauguration. It took some time, but eventually, Apple got the memo.

Over the next few years, scrutiny not only of Apple but also of any Chinese supplier that worked with the American technology giant came under the scrutiny of the Chinese government. The scrutiny was general, but corporate governance was most often the institutional vehicle. Within short order, if a Chinese firm was known to be working with Apple, local government officials were using the mechanisms available to them to deepen the signal they were sending to the powerful corporate player operating within China's borders. And remember, in the post WTO-accession era, China was no longer allowed to demand a quid pro quo for market access. However, if they used the institutions of corporate governance to make operation difficult for Apple's supply chain partners, Apple would eventually take notice.

Take, for example, the new Labor Dispatch System (Interim Regulations), which were put into place (March 1, 2014) just two weeks before Apple's Consumer Day call out. Under this new regulation, a given Chinese organization was only permitted to allow ten percent of its labor force from the Dispatch (migrant) Labor System. Guthrie – who was employed by Apple at the time to advise the company on China affairs – recalls one conversation with a member of the Apple legal team as the Apple official tried to make sense of the new regulatory regime. The official expressed consternation, saying that these new rules seemed impossible within the current system, stating that some of Apple's suppliers employed upwards of eighty percent of their manufacturing labor force through the migrant labor force. The Apple official went on to explain that this was crucial, because of the seasonal production of Apple products. Citing one example, the company's relationship with Foxconn, the official explained that, in the months prior to the launch of a new iPhone, the requirements for labor assembling these Apple products would increase precipitously, sometimes quintupling in labor force volume. However, the Apple official explained, this would only be for two months out of the year, and then production of apple products would drop back to normal levels for the remaining ten months of the year. If Foxconn had to employ and pay those laborers on labor contracts for the full year, the entire economic model would break down. As Guthrie listened to this member of Apple's legal team, he carefully explained that goal might not be compliance; rather the goal was to send a signal to Apple that the company needed to build closer relations with the local governments in the areas in which they were operating. If Apple proactively offered new sources of collaboration and contribution, a lack of compliance with the new Labor Dispatch Regulations might be overlooked.

More laws were produced that would make Apple's operations in China difficult. In 2015, the Chinese government passed the new Cybersecurity Law, which barred foreign-owned companies from publishing content online in China. Within short order, Apple's iTunes store in China was shut down. Suddenly, the Chinese government had the tech giant's attention. Within months, the Apple executive team was on a mission to show the Chinese government – both the Central

Government and the provincial and municipal government where the company's key suppliers were located – just how committed to China Apple is and continues to be. A new organizational structure was put in place that would work closely with the Pudong District Government, and a new Vice President level leader relocated from Cupertino to Shanghai to work directly with the central and local governments. R&D Centers were built in Shanghai, Shenzhen, Beijing, and Suzhou; Data Centers were built in Guizhou (where Chen Miner was governor); white papers were written, and presentations made to government officials all over China telling the story of the tacit knowledge that Apple operations engineers deliver to the 1000+ manufacturers in their supply chain. Suddenly, Apple was showing up and contributing to Chinese society and economic development in a way that pleased the Chinese government. And, amazingly, the new governance institutions – those very institutions that would make it impossible for Apple's Chinese suppliers to operate in the way they had – suddenly receded from the conversation. Business went back to the way it had been before 2013.

This is a corporate governance story, but it is a governance story shaped by the economic interests of the local and national governments operating in a post-WTO accession era. The Chinese government had in place the governance institutions, which, if enforced, would make it very difficult for Chinese suppliers in Apple's manufacturing supply chain to serve the tech giant. However, if Apple delivered for China what the government wanted, these institutions of corporate governance would remain unenforced. There would be no quid pro quo for market access – the Chinese government never asked for the R&D Centers or Data Centers. But these organizations were funded and built, and the Chinese government rewarded Apple by turning a blind eye to suppliers' violations of corporate governance institutions. It was an amazing transformation and dance between the Chinese government and the world's most powerful and valuable technology company.

Case 3: The Case of Alibaba and ANT Financial

Let's look at one more case, the case of a wholly Chinese corporation, Alibaba. Founded in 1999 by entrepreneur Jack Ma as a China-based B2B marketplace site. The Internet e-commerce site would become profitable within three years and would quickly become a leader and powerhouse in a short period, launching technology innovations such as Taobao, Alipay, Alimama, Lynx and others. The company's Initial Public Offering on the New York Stock Exchange in 2014 would become the largest IPO in history. In 2014, Alipay would lay the groundwork for the founding of ANT Financial (which would eventually be renamed the ANT Group). In October of 2020, ANT Financial was set to deliver for the second time for an organization under Jack Ma's leadership the largest IPO in world history – a projected $34 Billion IPO. In an amazing twist, the IPO was quashed by the Chinese government. So, what happened?

Many large technology companies seem to believe they are saviors, transforming the world economically and socially, democratizing access to commerce, and "enriching people's lives," as one of the world's largest technology companies often says. There is a sense that, in their pursuit of solutions to lead the world into a new economic age, critics are neither qualified nor capable to challenge them, because these companies are the future, and they are special. One of the consequences of this disposition is that regulation and supervision of these companies have been a challenge. This is true in both the U.S. and China, where regulation is a double-edged sword.

On one hand, since these behemoths reflect the competitiveness and innovation of a country, regulation could restrict a nation's economic vitality and growth. On the other hand, the dominance of these giants has brought some negative effects to the economy and, of greater concern, the social fabric. To regulate or not, that is the question.

After long hesitation concerning Chinese big tech, the Chinese regulatory authorities finally pulled out their sword and swung it at the Ant Group (ANT), an Alibaba company that was on track to become the largest IPO in history. On the evening of November 3, 2020, just 36 hours ahead of a scheduled debut in Shanghai and Hong Kong, the Shanghai Stock Exchange (SSE) surprised the market by announcing that it would suspend ANT's listing in its STAR Market. About an hour later, ANT announced its Hong Kong IPO was to be shelved as well. The suspension of ANT's listing plan sent a strong signal that the Chinese Government would have a say in what was happening in China's financial markets. ANT retains its status as the world's largest Unicorn. (A Unicorn is a privately held company worth more than one billion USD, and ANT is the most valuable Unicorn in the world by far.)

First, however, it is important to give a high-level discussion of what we think has happened here. As we have discussed previously, it is important to remember that there is a close alliance between the Central Government, local governments, and the private sector – they all work together in the economic development of Chinese society. This is not a free market, but it is a collective market. There is a close alliance between President Xi Jinping's administration and big tech, as the government is relying on companies like Alibaba and Tencent to continue China's transition to the next phase of economic growth, the building of a consumption-based economy. So, what really went on here? From our analysis, there are three possibilities (and all of these can be true at the same time):

- Jack Ma is being punished for speaking out too dismissively against the banking sector, and the government is reminding him that they are in a partnership together and the adversarial rhetoric needs to be dialed back. In his speech, Ma criticized several Chinese regulatory agencies, including the China Securities Regulatory Commission, the China Banking and Insurance Regulatory Commission, the State Administration of Foreign Exchange, and the People's Bank of China. It may simply be that government officials believed Ma went too far – in his public speech – and therefore needed to be an example.
- There is also a feeling that Alibaba and Jack Ma are becoming too big, and this delay in the ANT IPO was a reminder that the Chinese Government is still in control. In 2014, the Alibaba IPO was the largest in history to date. Six years later, Jack Ma was set to oversee another record-setting IPO. It may be the case that the Chinese Government felt a need to remind Mr. Ma (and his peers) that the Chinese Government is still in control of the powerful global corporations that are emerging in China.
- There may also be basic regulatory issues in play here. Technology companies have the advantages of less regulation (and as one consequence, higher trading multiples), and, while the ANT Group has been arguing that they are a technology company and therefore should not be subject to the same regulations of the commercial banking industry (e.g., capital reserve requirements and the like), it may just be that the government is not buying it. It is clear that ANT is a FinTech company and perhaps it should be subject to the same type of regulatory oversight that the commercial banking industry is subject to.

All three of these dynamics are likely in play, and the Chinese Government decided to slow things down and invite Mr. Ma and his team in for tea and a chat. Mr. Ma would subsequently drop out of sight for more than a year, and Alibaba would release what is surely the most comprehensive corporate compliance report in the company's twenty-five-year history.

The Most Expensive Speech in the History of the World
ANT is the most important arm of the Alibaba Empire. This Fintech behemoth is controlled by Jack Ma, founder of China's e-commerce platform Alibaba. On November 5, ANT was ready to break the world record for the largest IPO in history with a $37 billion offering and an estimated valuation close to $300 billion, a valuation nearly equal to the market value of Bank of America and Goldman Sachs combined.

From ANT's 2019 revenue, we can see CreditTech which provides credit and loans to consumers and SMBs (small and micro businesses) has surpassed Digital payment and merchant service as ANT's biggest revenue generator. Two major products of CreditTech are Huabei and Jiebei. Huabei serves as a virtual credit card to Alipay users, allowing 40 40-day interest-free periods for a consumption quota ranging from 500 to 50,000 yuan. Jiebei provides loans typically ranging from 1,000 to 300,000 yuan for Alipay users, the amount is affected by the credit scores calculated by ANT. Approximately 98% of the consumer and SMB credit balances enabled through CreditTech as of June 30, 2020, were underwritten by ANT's partner financial institutions or securitized through ABS. ANT receives technology service fees as a percentage of the interest income.

From the constant of the company's name change to its prospectus, it was clear that ANT sought to hide its financial identity and be treated as a technology company, in order to avoid the strict regulation of financial companies. Article 2 of the new regulation stipulates that online micro-landings as the businesses that are "using big data, cloud computing, mobile network, and other technical means as tools, analyzing and evaluating credit risks of borrowers and determining loan methods and amount through internet platforms' data of client management, online consumptions, online transactions, as well as through other legally acquired data information, completing loan applications, risk reviews, loan approvals, loan issuance, and loan recovery processes online." The definition hits the point, the underlying logic of ANT's CreditTech business is micro-loan, ANT jointly lends with other banks.

If the Consultation Paper is to be strictly implemented, the impact on ANT's CreditTech business will be enormous. Among the new regulatory requirements, loan leverage ratio and lender's contribution to a joint loan are the biggest challenges for ANT. Article 12 stipulates that funds received through borrowing or ABS shall not exceed 5 times the lender's net assets. In a single joint loan, the proportion of fund contribution of an Internet company shall not be less than 30%. Based on the new requirement, ANT's 2.15 trillion-yuan CreditTech loan balance as of the end of June 2020 requires a minimum registered capital of 107.5 billion yuan, while the total net assets of the two small loan companies of ANT only reach 35.8 billion yuan.

Did the Chinese Government wrong ANT? No matter how ANT is packaged, the core of its business is finance. From our perspective, the IPO of ANT has greatly speeded up the regulation

process on Fintech companies and Jack Ma's speech made the regulators more determined, rather than saying the new regulation is mainly targeting at ANT. One lesson of the 2008 global financial crisis is that the losses caused by "innovative" financial products are not borne by a few people who enjoy the benefits but by the whole society, the taxpayers. In recent years, the internet finance chaos represented by P2P has interfered with the Chinese economy. The government, regulatory agencies, financial consumers, and even ordinary people have all paid a price.

The big trend of China's financial regulation is to penetrate the external technical form and determine the essence of various "new businesses" and "new products." To create a fair competition environment, it is critical to bring all financial activities into same supervision with the same regulatory rules. Compared to financial industry which has received strict regulation and supervision, the rise of ANT and other Fintech companies have benefited from regulatory arbitrage and relatively loose regulatory standards. The future of ANT is to some extent in the hands of regulators. Jack Ma's speech at the Bund Summit seems to give people the impression that he was publicly lobbying for Fintech companies like ANT. It now appears that his speech was counterproductive.

Jack Ma's so-called big data social credit system is built on data from user scenario provided by the Alibaba eco-system. However, their credit evaluation algorithm is a black box. Its validity and reliability have not been tested through complete economic cycle, especially in the pressure of an economic downturn. Most of ANT's 500 million consumer credit users are long-tail customers, most of them fail to get a credit card and most don't know the difference between interest and a service fee. If risk in this population occurs, it will have greater adverse social consequences than will be weathered by wealthier consumer banks. In addition, the collection and use of big data is also subject to compliance issues such as customer privacy protection. Are these reasons why Jack Ma did not mention a word on data risk in his controversial speech?

From a public perspective, despite mixed comments on the government's sudden suspension of ANT's IPO, Internet giants represented by Alibaba and Tencent are facing greater pressure and harsher scrutiny as well. In this winner-take-all business climate, these Internet companies have reached a de facto monopoly in their fields, and their users are facing increasing arrogance and deteriorating user experience. Although ANT has enabled many people who don't meet bank loan requirements to find the money they need, the borrowers will pay a total of about 15% interest and service fees compared to about 6% of normal bank loan interest. In Huabei's latest advertisement, the 37-year-old construction team leader has a tight family budget and needs to "calculate carefully" on spending, but he still borrows money through Huabei to give his daughter a decent birthday celebration. The advertisement suggests that without this, he would not be a good father. What Huabei has not told this family, or many other families is that the money used for the birthday needs to be repaid at 15% interest – starting to sound like the rates of credit card companies in the United States.

The stock market's valuation of technology companies and financial companies differs greatly. Here we pick China Merchants Bank (CBM) and Lufax Holding Ltd. (Lufax) as benchmarks to understand the valuation of ANT. CBM is the best-performing retail bank and the 6th largest bank in China, currently listed in SSE (600036), total market value of China Merchants Bank is

1.12 trillion yuan or USD 169.7 billion. CBM overlaps with ANT's Jiebei and SMB credit business. Lufax (LU) is a rival Fintech platform backed by Ping An Insurance Group, debuted on the New York Stock Exchange on 31 October,2020, current market value of Lufax is around USD 36 billion. The business of Lufax has transitioned from peer-to-peer (P2P) to retail borrowing and wealth management, targeting personal lending among small business owners as well as salaried employees in China.

Considering new regulatory measures and the valuation of financial companies, it is generally estimated that ANT's valuation will be reduced by at least 30%. As for the timing of an IPO restart, if more regulatory measures related to ANT's other businesses are introduced, it will further affect ANT's valuation and further delay IPO time. In the future, we expect that the suspension of ANT's IPO will not only impact ANT itself but also other companies in Alibaba's ecology as well. ANT is a powerful FinTech company, a symbol of the digital economy in China, and a source of pride there. However, good luck may not always be with ANT. To most people in China, ANT was brought to heal in the autumn of 2020, and a dispute over corporate governance was at the center of this process. It may be the case that all of this was a little more intentional. Perhaps we have all been cheated by Jack Ma because his speech could be a sacrifice fly. If the listing price and expectations for ANT were too high because of the new regulations that were coming, ANT's IPO suspension has allowed ANT and CSRC to pull themselves back into the regulatory world that is emerging in China surrounding banking and FinTech.

A provocative speech may have provided all parties a decent way out: regulatory authorities can naturally introduce new regulatory measures; ANT can avoid a series of risks like lawsuits brought by the new regulations; and Jack Ma keeps his chivalrous halo for courageously criticizing the banking industry, which is mostly state-owned and has allowed Ma to speak for the interests of shareholders and his friends, regardless of his personal gains and losses. Even without an IPO, ANT's competitiveness is still much stronger than most traditional financial companies, not to mention foreign-invested financial institutions known in China as pandas. And the IPO will eventually come. As long as Ma and ANT know where the boundary is and as long as they realize they are in partnership with the Chinese Government, they will be fine.

For other countries around the world, the ANT incident provides a vivid case of regulating technology giants. While one part of this narrative looks like the Chinese Government disciplining and reigning in a tech tycoon, there is also a serious regulatory story. This is also about the Chinese Government applying the same regulatory standards to the fast-evolving fintech sector as it does to commercial banking in order, perhaps, to avoid another crisis like we experienced in 2008. Then Jack Ma went silent; he disappeared for over a year.

For China, the last week of the first quarter of 2023 was, to put it mildly, an active week. In Beijing, Tim Cook (CEO of Apple), Jay Y. Lee (executive chairman of Samsung Electronics), Amin Nasser (CEO of Aramco), Ola Källenius (CEO of Mercedes-Benz), and some 60+ global business leaders discussed the economic recovery in the 2023 Annual Meeting of the China Development Forum. In Hainan, 2,000 delegates including Singaporean Prime Minister Lee Hsien Loong, Malaysian Prime Minister Anwar Ibrahim, Spanish Prime Minister Pedro Sanchez, Cote d'Ivoire Prime Minister Patrick Achi, and Chinese Premier Li Qiang attended the Boao Forum for the Asia Annual Conference 2023, and its theme was an "Uncertain World: Unity and

Cooperation." Maye Musk, the mother of Tesla's founder Elon Musk, toured different cities across China and promoted her new book, *A Woman Makes a Plan.* Meanwhile, Ma Ying-jeou, former president of the Republic of China, began a 12-day ancestral worship tour to China on March 27, his first trip to the mainland.

Yet none of these events could match the return of Jack Ma, one of the most prominent Chinese entrepreneurs, the founder of multinational technology giant Alibaba, and the exiled bad boy of China's business community. At 1:00 p.m. on March 27, 2023, five hours after Bloomberg released a tweet noting, "Beijing wants to show it's backing private businesses, but Ma's decision to stay overseas suggests otherwise," China's STAR Market app announced that inside a tunnel in Hangzhou, a witness took video of Jack Ma sitting in a van. At 2:00 p.m., Yungu Education's WeChat public account released an article on Jack Ma's visit to Hangzhou Yungu School (a private school invested in by Alibaba Partners). In this moment, Ma was confirmed as returning to China. *Jack Ma is back.*

Here again, setting the political drama aside, this is a corporate governance story, a story of the careful dance between the Chinese government and the economic entities under its jurisdiction. As an individual, Jack Ma lost billions of dollars as a result of delivering a speech that was critical of the Chinese government and, in particular, the People's Bank of China. But this was not just a rebuke of Jack Ma. The rebuke did emerge in response to Jack Ma's speech, but the underlying debate was fundamentally about corporate governance. It was about the question of how ANT was categorized as an organization. The key question was whether ANT could retain its categorization as an Internet e-commerce giant or whether it would be categorized as a FinTech organization and thereby be subject to regulatory scrutiny of the China Securities Regulatory Commission, the China Banking and Insurance Regulatory Commission, the State Administration of Foreign Exchange, and the People's Bank of China – all the organizations called out in Ma's speech.

It is interesting to note that Alibaba's 2022 corporate report (Alibaba 2023) was very careful to document all of the ways the company is working to be an upstanding citizen in the Environment, Social and Governance (ESG) space, particularly concerning carbon neutrality. It is also important to note that, just one day after the news of Ma's return, Alibaba Group announced a "1+6+N" reorganization plan. The most significant reorganization in the Chinese e-commerce giant's history will see Alibaba become a holding group and split its core businesses into six different business groups, each led by a separate CEO and board that are empowered to bring in outside capital or list publicly, and other smaller business units. The six groups are:

1. Cloud Intelligence Group, including cloud, AI, DingTalk, and other businesses, with Daniel Zhang serving as CEO.
2. Taobao Tmall Business Group, including Taobao, Tmall, Taobao Deals, Taocaica\i, 1688.com, and other businesses, with Trudy Dai serving as CEO.
3. Local Services Group, including Amap, Ele.me, and other businesses, with Yongfu Yu serving as CEO.
4. Global Digital Business Group including Lazada, AliExpress, Trendyol, Daraz, Alibaba.com, and other businesses, with Fan Jiang serving as CEO.
5. Cainiao Smart Logistics with Lin Wan serving as CEO.

6. Digital Media and Entertainment Group including Youku, Alibaba Pictures, and other businesses, with Luyuan Fan serving as CEO.

A mammoth enterprise with annual revenue of $134.6 billion and 230,000 employees, Alibaba's reorganization would simplify its hierarchy and shorten the decision chain, improve efficiency, and speed up response to market needs. It is hoped that the independent operation of these business groups will improve efficiency and performance and revive the long-depressed stock price. Another apparent benefit of the plan is to remove a long-time regulatory overhang. Beijing's obvious anti-monopoly concern is that Alibaba has become too large and too influential. The headwinds facing Alibaba are a combination of slowing growth of China's economy, anti-monopoly regulations that have helped Alibaba's competitors, as well as geopolitical risks stemming from intensifying tensions between China and the United States.

From an industry perspective, with its saturation of China's mobile internet market and the expansion of its organizational scale, Alibaba has become a "traditional company". Alibaba's major businesses are facing fierce competition. According to the latest earnings data, only two out of Alibaba's six business groups are profitable, so there could be some consequences to dismembering the company. Taobao Tmall Business Group (e-commerce) is the cornerstone of the Alibaba empire, its cash cow, and its major source of profit. From Pinduoduo to Douyin, younger competitors continue to encroach the Taobao Tmall market with newer business models, better customer experience, and faster responses, Alibaba's domestic e-commerce market share has dropped from 70% in 2018 to less than 50% in 2022. The Chinese government's anti-monopoly measures have had a considerable impact during the process. The Cloud Intelligence Group, which will be headed by Daniel Zhang, Chairman and CEO of Alibaba Group, is the second most profitable business group. In 2022, Alibaba Cloud ranked first with a market share of 36% in China. Although its revenue increased by 7.6% year-on-year to 75.3 billion yuan ($10.9 billion), its market share decreased by 2.7%. Alibaba's other four major business units are currently losing money or playing catch-up in their respective industry segments.

Conclusions

In this chapter, we have attempted to lay out the complex issues surrounding corporate governance in China on a few levels. First, we have framed the evolution of China's corporate governance regime in the context of the general process of institutional reform in China. China's transition to a market economy has been a gradual and stepwise process, where new institutions are built iteratively, with the government introducing the new institutions as the market and economic development complexities demand new regulations. This contrasts with the "shock therapy" or "big bang" approaches to reform advocated by the likes of Jeffrey Sachs and Janos Kornai, where rapid liberalization and privatization were the cornerstone of market reforms. Corporate governance in China has followed China's gradualist model of reform, as the institutions of corporate governance have been introduced into the economy step-by-step from the late 1980s through the present day, beginning with the Enterprise Law, the State-Owned Asset Management Bureau (1988), the Company Law (1994), and continuing on through the present day more recent institutions such as the Labor Dispatch Regulations (2014), the Cybersecurity Law (2015), and others.

Second, we have emphasized the importance of local governments as the overseers of corporate behavior. Local governments, which are focused primarily on local economic development, become the de facto overseers of the implementation of these regulations. In the post-WTO accession period (post-2001), the Chinese government can no longer demand a quid pro quo for market access. But they can make the lives and operations of corporate actors easy or difficult, depending on how they assess the partnership and local contribution. Through this process, local governments as the corporate overseers are often flexible in how aggressively they mete out compliance to these institutions of corporate governance. China today still exists in the context of a Rule *by* Law system in which the government can use formal institutions – and how aggressively they are implemented as institutions of oversight – to force corporations to contribute to their localities. This is, in effect, an end run around the rules of the WTO accession, where it became against WTO rules to demand of corporations a quid pro quo for market access.

Third, we have employed a few key case studies to illuminate the dynamics described above. We have used the case of Foxconn to illuminate the ways in which a close affiliation with local governments, in this case, Zhengzhou Municipality and Henan Province, brought significant economic development resources to the localities and created a great deal of corporate access for the corporate partner. We have used the case of Apple to illuminate how the Chinese government has the tools to facilitate or make difficult the relationships between foreign corporations and their Chinese suppliers. In this case, it is very clear that the Chinese government had become dissatisfied with how Apple was operating and benefitting from those operations in China. With the tools of new corporate governance institutions – such as the Dispatch Labor Regulations (2014) and the Cybersecurity Law (2015) – the Chinese government could make operations much more difficult for Apple. And, of course, if the tech giant delivered resources and support that various local governments craved, the monitoring of adherence to these institutions could ease. Finally, we have used to case of Alibaba/ANT to illuminate the role of corporate governance as it has been recently applied to the rapidly evolving FinTech sector. Here again, the institutions of corporate governance and the bodies that oversee the corporations that are subject to these institutions have a strong hand in controlling how corporations in China operate.

Corporate governance in today's China represents a complex and fascinating process of institutional development and corporate control by state agents. We have the Central Government in Beijing, the architect of China's gradual transition from plan to market. Then we have local governments – as Andrew Walder (1995) presciently described it, "local governments as industrial firms" – which are focused on meeting projections on issues ranging from local economic development to poverty reduction to environmental safety. Corporations are key partners in many of these endeavors, though their incentives are more narrowly organized around revenues and profits. In the post-WTO accession era (post-2001), China is no longer allowed to require quid pro quos for market access – and practice that was very common in pre-WTO accession China – so they need to find other means to induce the kind of partnership they desire. The institutions of corporate governance become one of the key tools to help push corporations to engage in China's local economic development process.

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