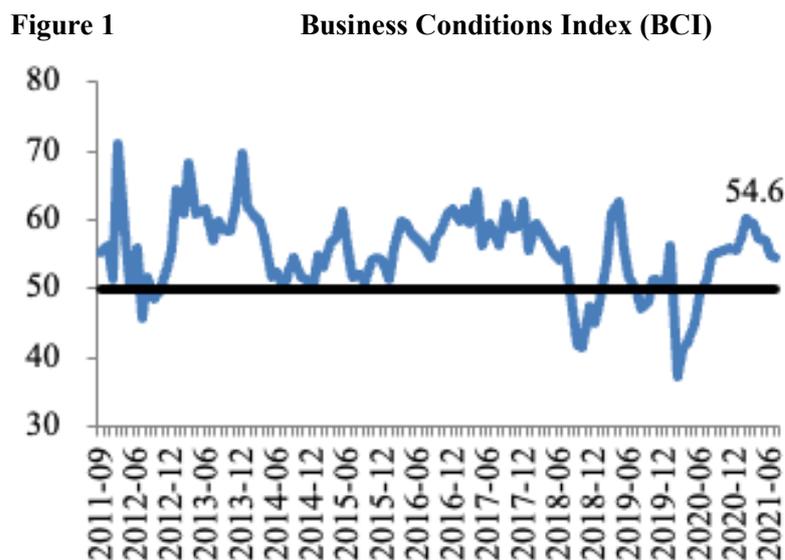


## Commentary on the July 2021 CKGSB Business Conditions Index

*Professor Li Wei*

In July, the CKGSB Business Conditions Index (BCI) fell slightly, from 54.9 to 54.6, remaining above the confidence threshold (Figure 1).



Source: CKGSB Case Center and Center for Economic Research

Very soon after Didi Chuxing went public in the U.S., it fell under regulatory scrutiny that scuppered its forecasted success. Its apps were removed from Chinese app stores, and multiple departments came together to carry out a rectification of the ride-hailing company. The impact on the U.S. stock market quickly spread to other Chinese concept stocks. Shortly after this episode, China's education and tutoring market is now also undergoing a storm of rectification of unprecedented intensity. These two markets are precisely those that are dominated by private enterprises, so people are naturally asking what will come under regulatory scrutiny next? Under such circumstances, entrepreneurs may well reconsider their investment plans, and think carefully before engaging in expansion plans. Rectification has increased company uncertainty, and has the potential to undermine future economic confidence.

The author has nothing against rectification per se. On the contrary, many such measures are highly welcomed. China's private businesses are extremely efficient and flexible, attributes that make them also good at skirting regulations in a way that may ultimately harm others and themselves. Better supervision and a certain degree of rectification are necessary. Didi Chuxing has a huge amount of customer data from the millions of rides people take daily in China, and the company's use of all this touches on consumer privacy. If this use is not well

supervised, Didi may indeed use the data in violation of regulations, infringing on privacy. As for education and tutoring, the market has expanded rapidly in recent years, leaving chaos in its wake, and regular educational institutions has felt the impact. In this respect, rectification is necessary and even beneficial to the development of the industry.

Although the government's business rectification is necessary, its implementation has had its rough edges. Were the rules clear to begin with? Are companies being rectified in accordance with the law, and are there channels for companies to complain? It does appear that there are many areas for improvement here. After all, when an industry or a company is supervised, the point is not to eliminate it, but to regulate and provide guidance. There are two main reasons why China has witnessed tremendous economic progress in the past 20 years. One is the dividends brought about by the admission to the WTO, and the other is the post-factor supervision model the government has applied to companies such as Alibaba. Taking a look at the second point, after the establishment of Alibaba and its cohort of tech firms, the government did not immediately issue restrictive regulations, but instead adopted an attitude of examining their developments and seeing where they would go. This gave such companies room for expansion, which inadvertently, led to them becoming giant companies. If the government had adopted strict control of companies such as Alibaba, it is inconceivable that they would be as strong as they are now. From this point of view, regulation and guidance of such startups has to be combined with a tolerant attitude as they grow.

Moreover, the current round of policy may be addressing the symptoms but not the root cause. Taking the rectification of the education and tutoring market as an example, policy makers have a clear goal: reducing the burden on primary and secondary school students, and in turn, reducing the burden on families, thereby encouraging families to thrive and consider having a second or third child. However, the current rectification has focused its fire on training institutions, without touching our education system as a whole. The mainstream system is a pyramid structure, in which the college entrance exam (gaokao) determines which universities take in which students. As a selective examination, the gaokao directs schools and examinations at every level below it. So, if the examination system stays the same, demand for extracurricular exam prep remains. Supervisory bodies wishing to reduce the burden on students will have to keep up the fight against supply and demand "arbitrage" for a long time.

Although it's been 43 years since China entered its reform and opening up period, and the country has experienced tremendous changes, we are still lagging behind in some aspects. For example, in the legal system, we still see campaign-style law enforcement. In fact, although local governments often give enterprises preferential conditions such as low-priced land when attracting investment, this is not what enterprises need most. They are begging for a predictable and stable operating environment. Only such an environment will help companies invest, recruit, and expand production. In order to achieve such an environment, the government must rely on the rule of law, because only with the rule of law can the behavior of all participants be predictable. It is hoped that the rectification of Didi Chuxing and the

education and tutoring market will not only guide related companies on the right track, but also bring other industries into the fold. If this goal can be achieved, GDP, taxation and employment in related industries will bolster the development of China's economy. From a wider perspective, this would be great for the country and the people.

This is a commentary on the CKGSB BCI report for July 2021 to which you are welcome to refer for detailed statistics. Do not hesitate to contact the BCI team by email for the accompanying BCI data report.

CKGSB Professor Li Wei

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