ADOPTING LEVERAGED BUYOUT (LBO) MECHANISM FOR IMPROVING THE COMPETITIVENESS OF THE STATE-OWNED CONSTRUCTION ENTERPRISES

Dang XIANG \(^1\) and H LI\(^2\)

\(^1\) China Cinda Asset Management Corporation (Chongqing), China, xiangdang@cindamc.com.cn
\(^2\) Department of Building & Real Estate, The Hong Kong Polytechnic University, Hong Kong, bshengli@polyu.edu.hk

Abstract
China’s accession to the World Trade Organization (WTO) has marked the beginning of a new era of China’s opening-up to the world. This development will lead to the full opening up of the Chinese construction market to overseas construction companies. This has brought significant challenge to the domestic construction firms, in particular, these state-owned construction enterprises (SOCE). Efforts have been made by the Chinese government for improving the competitiveness of SOCEs in order to compete with overseas firms. Various reforming mechanisms have been introduced such as merger and leveraged buyout (LBO). Using an example, the research reveals the applicability of LBO principles in improving the competitiveness of the SOCEs in China. The example suggests that the LBO mechanism has good future in application to enhance the competitiveness of the SOCEs by altering the corporate governance and capital structure although the difficulties exist in promoting the mechanism under the current Chinese financing mechanism.

Key Words
Competitiveness, construction, state-owned construction enterprise, leveraged buyout, China

INTRODUCTION
Improving the competitiveness of the state-owned construction enterprises (SOCE) has been among the major strategies for the Chinese government to reform its construction industry. This has become a pressing strategy after China’s entry to the WTO. Previous studies suggest that the SOCEs in China are less competitive than private businesses because of their inefficient management system developed over previous decades (Shen and Song, 1998). Since the introduction of economic reform programme in the early 1980s, the Chinese government has transferred its purely planned economy system into a market-oriented economy system. This transformation has led to the increasing promotion of competition among economic sectors. In line with this development, competitive tendering method has been adopted in the Chinese construction industry. Nevertheless, the development of competitive procurement has brought challenges to the operation of SOCEs as they are less competitive than the private construction sectors or other types businesses such as joint ventures and overseas firms (Zang, 2002). There is a large number of small- and medium-sized construction firms formed from rural areas in the Chinese construction market. As a result, the market share of the SOCEs has been decreasing, which has caused bankruptcies to many SOCEs in recent years, resulting in the serious problem of unemployed in these organisations. According to a study by Yang and Ge (2003), the number of unemployed in China was about 22 million in 2001, giving an 11% unemployment rate. In fact, unemployment due to the bankruptcy of state-owned enterprises has become a major social problem in China. Both the government and the enterprises have