

**OLD BOTTLE, NEW WINE:  
THE *GUAOKAO* APPROACH AND THE DEVELOPMENT OF  
THE BEIJING TAXI INDUSTRY**

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## ABSTRACT

This paper studies a unique phenomenon in contemporary China – the *guakao* practice. *Guakao* literally means “attach” or “affiliate” in English. The *guakao* mechanism has been widely used by private entrepreneurs to handle issues such as legitimacy, market entry barriers, and other discrimination as well as political, legal, regulatory, and administrative uncertainties. Under the *guakao* mechanism, private investors “attach” or “affiliate” themselves or their subsidiaries either to collectively owned or state-owned units. Such an enterprise was sometimes said to be wearing a “red hat,” which enabled it to circumvent discriminations towards private enterprises and reduce the uncertainties of business environments.

Policy-makers were the first to understand the significance and influence of the *guakao* mechanism. Using case studies on the development of the Beijing taxi industry, this paper will explore the purposes and uses of the *guakao* mechanism. Most importantly, this paper will examine how the Beijing municipal government has used the *guakao* mechanism to circumvent the central regulations and policies and to diversify risks of various uncertainties regarding the private enterprises in the Beijing taxi industry. The *guakao* mechanism has functioned as an instrument to overcome market-entry barriers for private investors, and ultimately to virtually privatize the Beijing taxi industry beyond the reaches of the central government.

The *guakao* mechanism is a flux of China's old command systems and the market-oriented transitional institutions. The *guakao* phenomenon does not exist in isolation, but a resultant of forces by all participating parties. Since the central government recognized the side effects of the *guakao* practice and the private sector as a pillar of the national economy alongside the public sector, it has faced the difficult reform agenda of leveling the playing field between the public and private sectors. One of the high priorities of this agenda will be to shift from a discretionary, particularistic way of regulating the private sector towards a rules-based system. But the future growth of the private enterprises also depends on progress in more fundamental reforms, such as strengthening property rights, removing market entry restrictions and ensuring that the judicial system enforces them.

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