Breaking through the dilemma of enterprise soft budget constraints: an analysis based on the linkage effect of countercyclical regulation and institutional reform

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Abstract. This paper focuses on the dilemma of enterprise soft budget constraints, deeply analyzes the current situation and harm of soft budget constraints in Chinese enterprises, and systematically elaborates on the impact mechanism and linkage effect of countercyclical adjustment and institutional reform on enterprise soft budget constraints. By combining theoretical analysis with practical exploration, strategies such as optimizing the countercyclical regulation policy system, deepening institutional reform, and strengthening the coordination between the two are proposed, aiming to provide theoretical basis and practical guidance for the government to formulate policies and enterprises to overcome difficulties, help enhance the market competitiveness of enterprises, and promote high-quality economic development.

Keywords: Enterprise soft budget constraints; Countercyclical regulation; structural reform; Linkage effect; Breakthrough of Difficulties.

1. Introduction

1.1 Research Background

In the process of economic development in our country, the phenomenon of soft budget constraints in enterprises has long existed and its impact is far-reaching. As an important pillar of the national economy, some state-owned enterprises face serious soft budget constraints. For example, some state-owned enterprises that are operating at a loss continue to rely on government subsidies to maintain their operations. According to statistics, in some traditional industries, some loss making state-owned enterprises receive financial subsidies that account for as much as [X]% of their annual losses. In the field of credit, banks often give special preferential treatment to loans to state-owned enterprises in anticipation of implicit government guarantees, lowering loan thresholds and extending repayment periods, resulting in low acquisition costs and poor utilization efficiency of funds for state-owned enterprises. At the same time, China's macroeconomic environment is complex and ever-changing, with frequent use of countercyclical adjustment policies to smooth out economic fluctuations. Fiscal policy stimulates the economy through large-scale tax cuts, fee reductions, and increased government investment, while monetary policy regulates market liquidity through adjusting interest rates, credit scale, and other means. Institutional reform is also constantly advancing, covering multiple key areas such as property rights system, financial system, and transformation of government functions. However, the phenomenon of soft budget constraints in enterprises goes against the current goal of pursuing high-quality economic development. It weakens the fairness of market competition, reduces resource allocation efficiency, and becomes an important factor hindering economic transformation and upgrading. [1]

1.2 Research significance

From a theoretical perspective, this study contributes to enriching the theory of budget constraints in enterprises. Deeply explore the impact mechanism of the linkage between countercyclical regulation and institutional reform on enterprise budget constraints, provide new perspectives and ideas for theoretical research in this field, and further improve the theoretical system of enterprise budget constraints. In practice, this study can provide important references for the government to formulate more scientific and effective countercyclical adjustment policies and deepen institutional reforms. By proposing targeted strategies to help enterprises break through the dilemma of soft budget constraints, strengthen cost control, improve operational efficiency, enhance market competitiveness, and thus promote high-quality and sustainable development of China's economy.

2. Theoretical basis and current situation analysis of enterprise soft budget constraints

2.1 Theoretical Connotation of Enterprise Soft Budget Constraints

2.1.1 Concept Definition

Enterprise soft budget constraint refers to the situation where an enterprise's budget constraint boundary is not rigid in economic activities, and when facing financial difficulties or business failures, it can expect to receive external assistance, thereby weakening its own budget constraint. Unlike hard budget constraints, under hard budget constraints, enterprises conduct business activities within the limits of their own resources, and once their assets are insufficient to cover their debts, they face bankruptcy liquidation; However, due to the expectation of external support, enterprises with soft budget constraints lack the necessary caution in investment decisions, cost control, and other aspects. Its root causes mainly include government intervention, where the government provides unreasonable support to enterprises for multiple goals such as employment and industrial policies; The ambiguity of property rights leads to unclear responsibilities and rights of enterprises, making it difficult to form effective self-restraint mechanisms. [1]

2.1.2 Theoretical Development

The theory of soft budget constraints for enterprises originated in the 1970s, when Hungarian economist Korne first proposed this concept to explain the operational behavior of state-owned enterprises under a planned economy system. With the development of economic theory, scholars at home and abroad continue to expand this theory. Foreign scholars analyze the reasons and impacts of soft budget constraints from the perspectives of agency theory and political economy; Domestic scholars have studied the relationship between state-owned enterprise reform, financial system reform, and soft budget constraints based on China's national conditions, and proposed a series of theoretical viewpoints and solutions with Chinese characteristics. [2]

2.2 The current situation and performance of soft budget constraints in Chinese enterprises

2.2.1 Soft budget constraints of state-owned enterprises

In terms of financial subsidies, state-owned enterprises have long relied on government subsidies to maintain their survival and development. State owned enterprises with excess production capacity can still receive subsidies issued by the government in the name of industrial support and technological transformation, even if market demand is insufficient and products are unsold. In the field of bank credit, state-owned enterprises are more likely to obtain bank loans due to their special status. Banks often overlook the actual debt paying ability of state-owned enterprises during loan approval, giving them lower loan interest rates and larger loan amounts. In terms of debt financing, after state-owned enterprises default on their debts, the government usually intervenes to coordinate and help them overcome difficulties through debt restructuring, injecting high-quality assets, and other means, further strengthening the expectation of soft budget constraints for state-owned enterprises. [3]

2.2.2 Soft budget constraints of private enterprises

Although private enterprises face relatively stricter budget constraints in market competition, there are also instances of soft budget constraints. Some local governments provide certain policy support to private enterprises in order to promote local economic development and attract investment, such as tax incentives, land transfer fee reductions, etc. In terms of financing, some private enterprises establish cooperative relationships with state-owned enterprises and obtain bank loans with the credit guarantee of state-owned enterprises, forming soft budget constraints under implicit guarantees. However, compared to state-owned enterprises, private enterprises have relatively smaller scope and degree of soft budget constraints, and rely more on specific policy environments and market relationships.

2.3 Hazards of Enterprise Soft Budget Constraints

2.3.1 Inefficient resource allocation

Soft budget constraints lead to a lack of cost control and risk awareness in enterprises, resulting in blind overinvestment and redundant construction. In order to obtain more resources, enterprises expand their production scale without considering costs, resulting in overcapacity and inefficient or even ineffective allocation of a large amount of resources. Taking the steel industry as an example, some steel companies with soft budget constraints continue to expand production capacity even when market demand is saturated, resulting in resource waste and hindering the development of other efficient enterprises in the industry. [4]

2.3.2 Impaired fairness in market competition

Soft budget constraints enable enterprises to gain competitive advantages through non market factors such as government subsidies and credit preferences, which undermines the fair competition environment in the market. These enterprises can sell products at prices lower than market costs, squeezing the survival space of other enterprises and suppressing their innovation drive and development enthusiasm. Over time, the mechanism of survival of the fittest in the market becomes ineffective, which is not conducive to cultivating market entities with core competitiveness.

2.3.3 Threats to macroeconomic stability

Soft budget constraints in enterprises can easily trigger debt risks, and the existence of a large number of inefficient enterprises leads to an increase in non-performing loans in banks, posing a threat to financial stability. At the same time, the problem of overcapacity has intensified, putting macroeconomic pressure on deflation and affecting the sustainability of economic growth. In addition, the dependence of enterprises on government assistance has also increased the financial burden on the government, further increasing the risks of macroeconomic operation. [5]

3. Analysis of the Impact of Counter cyclical Adjustment and Institutional Reform on Soft Budget Constraints in Enterprises

3.1 Impact of countercyclical adjustment on soft budget constraints of enterprises

3.1.1 The role of monetary policy

Under loose monetary policy, interest rates have decreased, credit scale has expanded, financing costs for enterprises have decreased, and funding availability has increased. For enterprises with soft budget constraints, it is easier to obtain funds, which may further exacerbate their overinvestment behavior and strengthen soft budget constraints. For example, in a low interest rate environment, some state-owned enterprises will increase their investment in inefficient projects. Under the tight monetary policy, rising interest rates, tightened credit, increased difficulty in corporate financing, and rising capital costs have forced companies to make more cautious investment decisions, which to some extent has hardened their budget constraints.

3.1.2 The role of fiscal policy

If fiscal subsidies lack effective supervision and precise guidance, they may exacerbate the soft budget constraints of enterprises. In order to obtain subsidies, companies may allocate resources towards seeking subsidies rather than improving operational efficiency. However, precise tax regulation policies, such as increasing taxes on high energy consuming and high polluting enterprises and providing tax incentives to innovative enterprises, can guide enterprises to adjust their business strategies and strengthen budget constraints. Government investment can also affect the investment decisions and budget constraints of enterprises by optimizing investment direction and structure. [6]

3.2 Impact of System Reform on Soft Budget Constraints of Enterprises

3.2.1 Property Rights System Reform

The reform of clear and diversified property rights can clarify the responsibilities and rights of enterprises, and reduce improper government intervention in enterprises. By introducing multiple investment entities and establishing a modern corporate system, enterprises can become market entities that operate independently and are responsible for their own profits and losses, fundamentally improving the situation of soft budget constraints. For example, after the mixed ownership reform of state-owned enterprises, the corporate governance structure has become more perfect, the attention to their own operating conditions has increased, and budget constraints have been hardened.

3.2.2 Financial System Reform

The market-oriented reform of interest rates has made the financing costs of enterprises more accurately reflect the market supply and demand relationship and the level of enterprise risk. Banks will pay more attention to the actual repayment ability of enterprises when lending, regulate credit behavior, reduce unreasonable credit support for enterprises, and thus harden the financing constraints of enterprises. Strengthening financial regulation can prevent financial institutions from operating in violation of regulations, improve the transparency and stability of the financial market, encourage enterprises to conduct financing activities in a more standardized manner, and enhance their awareness of budget constraints.

3.2.3 Transformation of Government Functions

The government is shifting from a "omnipotent" to a "service-oriented" approach, reducing direct intervention in enterprises and improving market mechanisms. The government creates a fair competitive market environment by establishing fair market rules, strengthening market supervision, and providing public services. In such an environment, enterprises can only rely on their own capabilities to cope with market challenges, thereby strengthening budget constraints.

3.3 The linkage effect between countercyclical regulation and institutional reform

3.3.1 Policy synergy mechanism

The countercyclical adjustment policy and institutional reform measures have consistency in their goals, both aimed at promoting stable economic growth and improving resource allocation efficiency. In terms of means, the two cooperate with each other. For example, when supporting the reform of state-owned enterprises, fiscal policy can be promoted in conjunction with the reform of the property rights system, guiding social capital to participate in the mixed ownership reform of state-owned enterprises through fiscal funds and promoting the hardening of budget constraints for state-owned enterprises.

3.3.2 Mutual Promotion

The countercyclical adjustment policy creates a stable macroeconomic environment for institutional reform, reduces the risk of economic fluctuations during the reform process, and enables the smooth progress of institutional reform. Institutional reform has enhanced the sensitivity and responsiveness of enterprises to countercyclical adjustment policies, improving the effectiveness of policy implementation. For example, after the reform of the financial system, corporate financing has become more market-oriented, and the transmission mechanism of monetary policy has become smoother, which can better play a role in regulating the economy. The two promote each other and work together to improve the soft budget constraints of enterprises.

4. Breakthrough strategy for enterprise soft budget constraint dilemma based on linkage effect

4.1 Optimizing the countercyclical adjustment policy system

4.1.1 Enhance policy precision

The government should formulate differentiated countercyclical adjustment policies based on the characteristics of different industries and types of enterprises. For enterprises in industries with overcapacity, when implementing fiscal and monetary policies, their access to funds should be restricted to guide them towards industrial upgrading; For innovative small and medium-sized enterprises, increase policy support, reduce financing costs, and encourage their innovative development. By implementing precise policies, the regulatory effect of policies on corporate budget constraints can be improved.

4.1.2 Strengthen policy transparency and expectation management

Strengthen the disclosure of policy information, timely convey policy objectives, tools, and implementation paths to enterprises and markets, and stabilize enterprise expectations. Reduce the dependence of enterprises on soft budget constraints caused by policy uncertainty, encourage enterprises to arrange production and operation activities reasonably according to policy guidance, and improve their market adaptability and self-restraint ability.

4.2 Deepening institutional reform

4.2.1 Promote the reform of state-owned enterprises

Further deepen the reform of the property rights system of state-owned enterprises and improve the corporate governance structure. Clarify the functional positioning of state-owned enterprises, gradually eliminate implicit government guarantees for state-owned enterprises in competitive fields, and promote their full operation in accordance with market-oriented principles. Establish a sound market-oriented operation mechanism, improve the performance evaluation system, link the operational efficiency of enterprises with the interests of management and employees, and strengthen the budget constraints of state-owned enterprises.

4.2.2 Improve the financial market system

Accelerate the pace of interest rate marketization reform, so that interest rates can fully reflect the supply and demand relationship and risk level of funds. Strengthen financial supervision, regulate the behavior of financial institutions, break down ownership discrimination in the allocation of financial resources, and ensure that all types of enterprises can obtain financing in a fair environment. Develop multi-level capital markets, broaden financing channels for enterprises, and improve the marketization level of financing constraints for enterprises.

4.2.3 Accelerate the transformation of government functions

Clarify the boundary between government and market, reduce administrative intervention, shift the focus of work to strengthening market supervision, providing public services, and maintaining market order. Improve market access and exit mechanisms, and create a fair competitive market environment. Through the transformation of government functions, enterprises are encouraged to rely on their own capabilities to cope with market challenges, enhance their market competitiveness and budget constraint awareness.

4.3 Strengthen the coordination between countercyclical regulation and institutional reform

4.3.1 Establish a policy coordination mechanism

Establish a cross departmental policy coordination mechanism to coordinate the formulation and implementation of countercyclical adjustment policies and institutional reform measures. A joint working group consisting of multiple departments such as finance, currency, and development and reform, regularly communicates and coordinates to ensure consistent policy objectives and complementary means. When formulating policies, fully consider the impact of countercyclical adjustment policies on institutional reform, as well as the promoting effect of institutional reform on the effectiveness of countercyclical adjustment policies, in order to achieve policy synergy.

4.3.2 Strengthen dynamic monitoring and evaluation

Establish a dynamic monitoring and evaluation system for enterprise budget constraints, countercyclical adjustment policy effects, and institutional reform progress. By utilizing technologies such as big data and information technology, real-time tracking of enterprise operations, policy implementation effectiveness, and reform progress can be achieved. Regularly evaluate policies and reform measures, adjust policy direction and reform efforts in a timely manner based on the evaluation results, enhance the linkage effect between countercyclical regulation and institutional reform, and ensure effective improvement of enterprise soft budget constraints.

5. Conclusion and Prospect

5.1 Research Conclusion

This study conducted an in-depth analysis of the current situation and harm of soft budget constraints in enterprises, and found that state-owned and private enterprises have varying degrees of soft budget constraints, which have serious negative impacts on resource allocation efficiency, market competition fairness, and macroeconomic stability. The system elaborates on the impact mechanism and linkage effect of countercyclical regulation and institutional reform on enterprise soft budget constraints. Monetary policy and fiscal policy have different effects on enterprise budget constraints by regulating financing costs and fund acquisition; The institutional reform starts from the aspects of property rights system, financial system, and government functions, fundamentally improving the soft budget constraints of enterprises, and coordinating and promoting countercyclical adjustment and institutional reform. Based on this, a series of strategies have been proposed to break through the dilemma of enterprise soft budget constraints, such as optimizing the countercyclical adjustment policy system, deepening institutional reform, and strengthening the coordination between the two, providing comprehensive theoretical and practical guidance for solving the problem of enterprise soft budget constraints.

5.2 Research Prospects

In terms of data selection, this study is limited by the non disclosure of financial data from some enterprises and differences in statistical standards, which limits the quantitative analysis of the degree of soft budget constraints on enterprises. In terms of model construction, the characterization of the linkage effect between countercyclical regulation and institutional reform is not precise enough. Future research can further expand data sources and adopt more scientific methods to accurately measure enterprise soft budget constraints. Conduct in-depth research on the optimization path of the linkage between countercyclical regulation and institutional reform under different economic cycles, and explore how to dynamically adjust policy combinations and reform efforts according to changes in the economic situation. In addition, with the continuous development of new technologies, the impact of the application of new technologies such as artificial intelligence and blockchain on enterprise budget constraints can be studied, providing new perspectives and methods for the research of soft budget constraints in enterprises.

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