China: developmentalism and social security

Tang K-L, Ngan R. China: developmentalism and social security

China began its social security reform when the market-oriented economy was first promoted in the late 1970s. Initiatives have been taken to replace the employer-based labour insurance model with a largely social insurance model. However, it is a mistake to argue that China is pursuing a neo-liberal agenda in its social initiatives. Instead, the state has played a major role in the process. Based on a developmental analysis, it is argued that the direction of change is generally encouraging. The emerging social insurance programme has the following advantages: it widens coverage, facilitates economic development, seeks a minimum entitlement, fosters social integration, and enhances individual participation and responsibility. The creation of an economically and socially viable social insurance programme will support the economic development of the country in the twenty-first century.

The reform of the social security system in China has generated much interest among international organisations, academics from different disciplines and policy analysts. Dismantling a comprehensive, employer-based labour insurance programme and replacing it with a mixed social insurance and individual accounts programme, the change process was first initiated in the mid-1980s. It is an opportune time to assess the nature and initial impact of these changes. This paper will examine China’s social security reform from the developmental perspective. Although a number of studies have already discussed this issue (Hu, 1997; Selden & You, 1997; Song & Chu, 1997; World Bank, 1997a, 1997b; Hu, 1998; Leung, 1998), few have approached the topic from a developmental perspective or considered the way China’s reform has affected economic development. This paper seeks to address these issues.

Developmental approach to social welfare

In response to the neo-liberal critique of welfare state and what is seen as an over-reliance on state welfare, progressive policy analysts have been searching for an appropriate and effective approach to social provision (Gilbert & Gilbert, 1989). Some, such as Midgley (1995, 1996, 1997, 1999) have called for the adoption of a developmental approach that will promote social development and be consonant with the need for continued economic development. This perspective is rooted in the Third World experience and it has received strong backing from international organisations. In the last three decades, for instance, the United Nations has sought to promote the developmental perspective through the 1995 World Summit on Social Development. This and other initiatives have helped to popularise the need for a renewed commitment to social development (United Nations Development Programme, 1998).

The developmental approach to social welfare, or as developmentalism as it is also known, seeks to ensure people’s integration into society as productive citizens who contribute not only to their own well-being but to the development of the community as well (Midgley, 1997). This approach seeks to avoid the perpetuation of dependence of needy people on social-work services. Developmentalism offers a macro-perspective on social policy and links economic and social policies within the framework of a planned development process. It regards economic development as a desirable and essential element in social welfare, and proposes that social programmes support the developmental imperative. It sees an activist role for the state in promoting economic development and raising standards of living (Midgley, 2000).

According to Midgley (1999), developmentalism is based on three considerations. First, it proposes the creation of organisational arrangements at the national level that harmonise economic and social policies within a comprehensive commitment to sustainable development.
and people-centred development. Second, it urges the adoption of macro-economic policies that promote employment, raise incomes and attain other ‘people-centred’ economic development outcomes. Lastly, it recommends that social programmes should be investment-oriented, by promoting economic participation and generating positive rates of return to the economy.

The goals of social development are many: the harmonisation of social and economic development; the realisation of new social arrangements that accelerate the pace of development and assure the satisfaction of basic needs of people; and the transformation of societies toward more humanistic values based on social justice and the attainment of the fullest possible human development (Estes, 1998).

There are a number of ways in which social policies and programmes can contribute to economic development. First, they can assist in the mobilisation of human capital for development. Second, they can foster the creation of social capital, which contributes to economic development. Third, they can help low-income and special-needs clients engage in productive employment and self-employment. Above all, the participation of people in the determination of both the means and outcome of development is important (Midgley, 1996, 1997; Estes, 1998).

In sum, the developmental approach puts emphasis on the following goals and values: harmonisation of economic and social goals, investment-oriented social welfare, people’s participation, adequacy, equality and promotion of social cohesion. In this paper, these criteria will be used to analyse China’s social security programme.

**China: from enterprise welfare to social insurance**

Social security in China generally includes the formal programmes of the national, provincial and local governments, the formal programmes of enterprises and non-government institutions and the informal programmes of these institutions. Generally, these programmes cover labour protection, retirement and old-age pensions (Mackerras, 1998). Earlier than most developing countries, China introduced social security for its industrial workers soon after the Communist takeover. The social security programme in China can be traced back to 1951, when the first Labour Insurance Regulation was promulgated. This programme only applied to industrial workers in China’s state-owned and collective-owned enterprises, hence the number of its beneficiaries was relatively small. There were three main components of this programme, which was known as labour insurance: health insurance, injured-worker insurance and old-age insurance. The benefits were very generous, with some pensioners collecting 80% of their final salary as pension, along with subsidised housing, health care and transport. Essentially, all the costs of the labour insurance programme were borne by the state-owned enterprises (SOEs), which became the mainstay of the system. The system was funded on a pay-as-you-go basis. The pensions were paid from the output of current workers and the profits of their enterprises. There was no contribution from the employees, since the worker’s rights to labour insurance had been specifically written into the Constitution (Dixon, 1981). Whenever SOEs were financially incapable of paying for social spending, the government always assumed responsibility for supporting the system. In sum, the enterprise sector, along with the state, provided almost cradle-to-grave care for many of China’s urban workers.

Despite its strengths, the soundness of the labour insurance system was eventually questioned. Since 1978, the state has faced considerable pressures to change this model of welfare provision. First, for some time, there had been a concern among party and government officials about the soundness of the pension scheme. The two main criticisms against the labour insurance system were that it instituted the ‘iron rice bowl’ of lifetime employment (thus reducing labour mobility) and encouraged ‘eating from the same big pot’ (Forster, 1998). More importantly, many state enterprises were inefficient, and they suffered heavy economic losses. Ever since the 1980s, the enterprise system has faced a financial crisis. One-third of SOEs have been loss-making (Hu, 1998). Consequently, social spending gradually became a heavy burden on most of the enterprises. The problem of funding pensions for the employees of SOEs became a major challenge.

The central government poured more than 80% of the state bank’s financial assets into SOEs to encourage growth in the mid-1990s. The Communist Party tried to maintain the loyalty of urban workers and local managerial elites by channelling huge subsidies into loss-making SOEs, which continue to dominate the industrial sector. This is important since some 70% of urban households have workers in the state sector. Spending on labour insurance has been increasing (Hu, 1998). SOEs’ outlays accounted for 70% of China’s total spending on social security or 1.9% of the GDP in 1978. By 1993, SOEs’ spending on labour insurance and welfare had risen to 80% of total social security payments. By contrast, central government financing of social security benefits has been relatively insignificant: 0.4% of GDP was spent on social welfare from 1978 to 1993 (Hu, 1998).

The SOEs are clearly unable to cope with new changes and growing market competition. Under the socialist market economy, many private enterprises have been established. Since 1986, a new labour
system based on contract employment has been evolving while a variety of businesses have flourished: joint ventures, overseas ventures and urban collective enterprises. In this context, the SOEs are facing a very competitive environment. They have to assume social responsibilities for their workers and at the same time have to survive intense competition from a dynamic private sector.

There is also pressure from demographic growth. The Chinese economy has been strong since the reform era. Between 1978 and 1997, China enjoyed an annual average growth rate of 8.2% in terms of gross domestic product. But now, in the context of slowing economic growth, an ageing crisis looms. According to estimates (World Bank, 1997a), the number of China’s elderly will rise from about 76 million in 1995 to 300 million by 2050. At the same time, the ratio of workers to pensioners is projected to decline to about three to one in 2050 from ten to one in 1995. Ageing is not an immediately serious concern but, if these projections are reliable – and they have been too gloomy in the past (Ngan, 1999) – there could be an enormous problem in using the resources of those working to support a large retired population in the near future.

Socially, the existing social security programme has some undesirable consequences resulting from uneven economic development in China. While a comprehensive and generous social security system is available for industrial workers in the urban SOEs, there is no comparable system in the rural areas, which contain some 70% of the population. The implementation of the labour insurance social security system has effectively excluded China’s vast rural agricultural population. Subsidies to urban industry can also be seen as a massive transfer of resources from the countryside. This has resulted in unequal access to social programmes with an inevitable increase in inequality (Tang, 1999).

Inherently, the whole system of enterprises delivering welfare has been fragile and decentralised. The uneven sharing of financial responsibility for employees’ social security among enterprises is problematic. The financing and administration of the traditional labour insurance programmes was highly decentralised, with varying rates of pension payment. Older enterprises with more retired people to support are in a disadvantaged position when compared to younger enterprises.

The World Bank has painted a most dismal picture of maintaining the status quo:

There is no way the present pension system can support a fraction of the aged army. Not unless all market reforms are halted and the iron rice bowl recast, with state-owned enterprises once more becoming responsible for paying pensioners out of cash flow. The result is a deadly sclerosis . . . (South China Morning Post, 13 October 1998).

The reform of the labour insurance system

Today, the need to reform the social security system is undisputed. In fact, pressures for reform have been building for many years. They are related to the economic reform of the SOEs. For instance, Prime Minister Zhu Rongji reaffirmed in mid-1998 that the government would reform the state sector and urban-welfare system radically. The plan is to reduce loans to inefficient SOEs, modify the banking sector significantly, dismiss 30 million state employees over the next three years, raise funds by selling urban public housing and cut medical costs.

As far as social security is concerned, the overarching goal is to set up a basic pension, medical and unemployment insurance system to ensure social stability. Although the process of reform has been evolving since the mid-1980s, key elements are now in place. They include: unifying the pension system nationally; bringing together enterprises and workers currently covered under separate plans into a single system with common standards; introducing funded individual accounts to end the problems associated with the employment-funded system; a reallocation of responsibility for social security provisions, especially the reduction in the state’s financial responsibility on the one hand, and the emphasis on individual duty and family and community support on the other (Hu, 1997; Hu, 1998). The central government wants to promote a unified national system with unified contribution rates (Selden & You, 1997). Several levels of unification are envisaged by the government: (a) the unified pension system covering all workers, regardless of the ownership of their enterprises; (b) the standardised contribution rates and benefit rates; and (c) the integration of the pension monies into a single pooling fund (Hu, 1997). The government also realises the need for provincial-level resource management, which is important to achieve equity and promote enterprise efficiency. The new system will be administered by the provinces, and although each is permitted a degree of autonomy in policy-making and administration, the system has uniform features.

Although the process of reform began in the mid-1980s, the framework of the new system had gradually emerged by the early 1990s. China would develop a multiple-tiered pension system, sharing the costs among the state, employers and employees. At the first level, it set up a basic pension. The basic pension will meet the basic subsistence needs of workers. It comprises two parts: a social pension component with a scale of flat rates and an income-related pension
component. Additionally, there will be a top-up supplementary component stemming from a complementary employer-funded pension scheme and/or additional personal savings (Hu, 1998). Guangdong Province has followed closely this three-tiered model by creating basic and supplementary pensions. However, the central government wants to make the new pension programme financially viable by encouraging greater workers’ savings and contributions. An ideal model whereby contributions from the workers will assume a larger role was devised in 1998. In this latest conception, savings in the individual accounts will make up the major portion of the benefit rate, which will be lowered to 58% of wage replacement.

As the new system has evolved, several common features can be noted. First, support from the state is guaranteed. The state does not abrogate its role. The basic pension is instituted to provide a universal social provision for the retired workers. Second, the idea of contribution has spread to other contingencies. For instance, the workers are asked to contribute to an unemployment benefit programme which would cover them in times of unemployment, which becomes a social issue since many inefficient enterprises were forced to close down after the market reform. Also, to combat escalating health-care costs, trials to test health insurance and the injured worker programme have been going on since 1987. In late 1998, some 38 municipalities had health insurance programme trials in progress (China News Analysis, 15 November 1998).

Finally, the new system contains both insurance-funded and mandatory-funded individual retirement accounts. As was noted earlier, the change to this multi-tiered pattern is intended to reduce the financial burden on the state and the SOEs. The new system is mandatory and requires the introduction of pensions to all urban enterprises, even privately-owned ones (Mackerras, 1998). To this end, China has accumulated more than 60 billion yuan ($7.5 billion) in pension funds for urban state-owned businesses’ employees. However, the system is highly decentralised and therefore practices vary. In some case, businesses are required to set up a personal account for each of the individual employees that equals up to 11% of their salaries. Employees pay 4% of their personal account and the rest is covered by their employers.

There is some information about the status of individual accounts. In Liaoning Province, for instance, workers have belonged to an old-age social insurance programme since 1985, and individual retirement accounts have been set up for about 84% of the eligible 3.6 million workers. A slightly higher number, 88.3% of the eligible workers, are enrolled in the basic old-age insurance programme, and all 14 of the province’s prefectural-level municipalities have been making pension payments, servicing 290,000 retired workers (China News Analysis, 1998).

The example of Guangdong Province, one of the most prosperous provinces on the southern coast of China close to Hong Kong, well illustrates the operations of the new pension programme. The new insurance programme in Guangdong was introduced in 1993 and is administered by the Bureau of Social Insurance. The wage replacement rate was set high at 72%. According to World Bank (1997b), the ratio of pensioner to contributors was 23% in 1994, which allowed the province to build up a surplus for reserves and future investments. This programme is contributory in nature. In 1994, the contribution rate was 19% (2% from workers, 17% from enterprises). The workers’ contribution rate was increased to 4% in 1998. As noted earlier, the insurance programme has three main components: the basic pension, the supplementary pension and the individual account. The basic pension is paid at 30% of the average provincial wage. In 1996, the average wage was 600 yuan, and hence the basic pension was 180 yuan. The top-up supplementary pension is funded by the enterprises and it is contingent on workers’ contribution records. Finally, the contributions of workers to their individual accounts will be paid out as a lump sum upon retirement. In line with a directive from the central government, the wage replacement rate will be reduced and the individual accounts will become more important in the future.

An assessment of China’s new social security system

Some analysts (Song & Chu, 1997) have suggested that China must develop market-based systems based on individual accounts and private investments to provide adequate old age and health protection. They claim that such a private system will increase economic growth and assist economic restructuring. However, the model that has emerged is not a market-

Table 1. Social security programme in Guangdong Province, China.

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<tr>
<th>Level</th>
<th>Structure</th>
<th>Payer</th>
<th>Functions</th>
</tr>
</thead>
<tbody>
<tr>
<td>One</td>
<td>Basic pension</td>
<td>Enterprise</td>
<td>To guarantee basic living minimum and promote social equality</td>
</tr>
<tr>
<td>Two</td>
<td>Supplementary pension</td>
<td>Enterprise</td>
<td>To provide further financial support</td>
</tr>
<tr>
<td>Three</td>
<td>Individual account</td>
<td>Worker</td>
<td>To emphasise individual responsibility and encourage saving for one’s future</td>
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Sources: Ngan & Li (1998); Guangdong Social Insurance Bureau (1998).
based retirement system. It is not an endorsement for the privatisation of social security. Rather, the continued involvement of government in the system represents a pragmatic approach to deal with the social security issue.

Given its short history, it is not surprising to find that the new system has a number of limitations. For instance, the present pension system leaves room for improvement in terms of legislation, coverage, fund pooling, management and risk resistance. The low collection rate of contribution poses difficulties in supporting the system. Lastly, half of the employees in private, collective and foreign-funded enterprises are not covered by the system. However, the change toward an old-age social insurance system with individual retirement accounts is a step in the right direction. Another positive feature of the new system is its potential to contribute to economic development. Using the criteria from the developmental approach, the evolving programme can be evaluated in the following terms.

Increasing coverage and adequacy

Through this evolving programme, China is able to extend its old-age insurance coverage to a wider section of the population. More urban workers are being covered. The immediate goal is to have every urban worker receive some social security. A more distant goal is to extend the system to the rural areas. This is most important since the peasants in the rural areas have been deprived of a state-sponsored programme. Furthermore, the provision of a basic pension has obvious appeal. It demonstrates the state’s commitment to maintain a basic level of living after retirement. Such contribution from the state is geared toward the goal of adequacy for the retirees.

The new pension system promises a higher amount of pension than the old pension. The new pension, comprising the basic pension and supplementary pension together with the worker’s account, is multi-tiered in its source of financing. In one study, informants in an old state-owned shipyard factory in Guangzhou indicated that the new pension in 1995 was 22% to 25% higher than the old pension, and it was able to catch up with the increase in average wages of their working colleagues. It was thus able to improve their livelihood after retirement. More and more workers have realised the benefit of a top-up supplementary employer-funded pension scheme with an additional worker-contributed personal savings account (Ngan & Li, 1998). Although workers need to contribute to their pension funds, the contribution rate in 1995 was a nominal one, at only 2% of their monthly salary. In 1998, it was still low, at 4%.

Pension pooling and risk sharing

Various efforts are made to unify the system and to strive for equity, which is a correct thing to do. The government is now giving priority to speeding up legislative work. It is set to promulgate a Regulation on Fee Collection for the Social Security Fund and a Regulation on Basic Pensions to provide a legislative guarantee of pensioners’ legal rights. These efforts are expected to achieve provincial-level pooling of funds, unify the contribution rate as a proportion of payrolls and implement full payment of benefits and collection of contributions. The primary rationale for this policy is to have social security expenses shared equitably among enterprises. It is estimated that by the end of 1999 all urban employees will be covered by the social insurance system.

The new insurance system is able to solve the bankruptcy problems of the old labour insurance funds owned by old collective enterprises. The new system has the merit of unifying all pension schemes run by different collective enterprises. By pooling all individual workers and enterprises’ pension contribution together, the contributions collected from younger workers are used to finance the claims of retired and retiring workers, whether or not they are coming from the financially challenged SOEs. Hence their burden on pension payment is eased to allow more funds to be invested to finance the enterprises’ economic and industrial development efforts.

Maintaining a minimum floor of protection

In the context of pension reform, the most affected group, the retired, seldom has a say. Studies have found that the Chinese elderly are predominantly illiterate and residing in rural areas (Li, 1998). They become socially marginalised in the process of rapid social change. Politically, they are not powerful and their interests in the social welfare system are not protected. The majority of them still rely on traditional family support despite the socialist ideals of collective welfare. Many young people disregard their responsibilities for the old. An adequate social security system is most essential to old people.

Under the new social insurance system, the basic pension is set at a level of 30% flat rate of the average annual wages of workers in a city or country for every retired worker. This rate is the same and universal for every retiring worker. The basic pension is to meet the basic subsistence needs of retirees. Thus a basic floor of social protection is promised throughout China, though mostly in cities. One should not forget that besides the basic pension, there is also the top-up amount from a complementary employer-funded pension scheme and additional personal savings from
the worker’s individual pension account. In theory, the new system should promise a higher amount of pension than the old one.

Promoting individual responsibility

The old employer-based labour insurance system gave very generous social entitlements to urban workers. As argued above, this was not economically viable or socially desirable. The emerging programme aims to promote individual responsibility. In other words, through their own savings and contributions, workers are taking care of their future. When the new system of individual pension contribution was first set up, workers were hesitant to join, fearing that the accrued money in their pension account would be expropriated by the government. However, after seeing the promise of higher pension from retiring colleagues, and with a computerised individual pension account records, they are now more motivated to contribute. Some redundant workers from bankrupted enterprises have even requested the government to allow them to contribute to their individual pension accounts during the period of their redundancy.

A developmental approach?

China is moving from an employer-based labour insurance model introduced in 1951 to a social insurance model. This has led to the creation of a multi-tiered system of social provision supplemented with individual contributions. The evolving programme has become more financially viable. Using the criteria of the harmonisation of economic and social policies, adequacy, equity and participation, and individual responsibility, the new programme is a significant improvement on the old one.

However, the system is state-managed and there have been persistent calls for privatisation from some policy analysts and economists. For instance, Feldstein (1998), taking a neo-liberal approach, has called for greater emphasis on funded benefits and a shift to a conditional defined (state) benefit guarantee. Rising unemployment and expensive health-care costs have fuelled the call for a privatised system. The supposed success of the Chilean model is often cited in support of their claims.

However, there is no indication that the central government will abandon its present efforts to build a pragmatic model which aims to incorporate the strengths of the social insurance system supplemented by individual retirement accounts. It is likely that, through a series of pilot projects in the country, the government will attempt to refine this evolving model. It appears that the basic pension will be maintained intact and changes are more likely to be made to the individual accounts. One question is whether the workers are confident enough and willing to contribute more to their individual accounts, since their savings can only be withdrawn in the long term. Another question is whether the market is sufficiently developed to provide security for these accounts. There is another thorny problem. In the context of rising social inequalities in both cities and rural areas, any efforts at exacerbating existing inequalities will be avoided by the government. The government probably realises that increasing workers’ contribution rates to their individual accounts is not a simple matter. In particular, workers in the declining SOEs are not able to do much with their individual accounts.

On the other hand, international organisations such as World Bank (1997a, 1997b) have advised China to adopt other measures to lessen the state’s responsibility and to control the ageing problem. This involves reducing the pension burden by gradually increasing the retirement age, lowering the wage replacement rate and indexing pensions to prices rather than wages. In particular, the government has been advised to achieve an adequate real rate of return on pension-fund investments. Certainly, these financial concerns need to be addressed by the government. Yet the government is cautious, not losing sight of the social goals and benefits of the present system. The fear of social instability has provided a strong and consistent incentive for the government not to forfeit its responsibility to urban workers. In terms of social development, the Chinese government is moving cautiously, while maintaining a balance between social protection and economic development.

Fostering productivistic welfare

As noted earlier, the reform of social security is intended to support the general economic reform and facilitate SOE reform. One of the key goals in the restructuring of the SOEs is to lower the costs of operations so that they become more competitive and are not overburdened by social spending. This has obvious implications for the economic future of the enterprises. It is also hoped that as the contributions from enterprises and workers accumulate, there will be sizeable funds for the local governments and social security authorities to invest in local infra-structural and economic projects, thus harmonising the twin goals of social and economic developments. Academics have described such efforts as ‘developmental statist’ (White, 1998), a term borrowed from the study of East Asian welfare states. It is also compatible with the notion of developmental welfare as defined by Midgley (1995, 1996, 1997, 1999). This orientation puts emphasis on rapid economic growth along with a pragmatic redesign of the pension
programme. Accumulation of funding from the pension programme is encouraged, and these resources will be channelled into the economic sphere to help stimulate the local economy. The official guidelines for this plan specify that 80% of the accumulated funds are to be invested in government bonds and 20% in bank deposits. Feldstein (1998) notes that in practice some funds are diverted into investments in local projects in pursuit of higher yields, but he notes that the additional savings that are accumulated in these defined contribution accounts will increase China's capital stock.

Taking account of the individual worker's contribution, government plans to reduce the contribution by collective enterprises and employers from 25% of workers' total monthly payroll to 10%, to enable enterprises to accumulate social security funds. It is planned that the worker's contribution rate will be increased at a slow pace, 1% for every two years, leading to an eventually equal rate of contribution by both workers and enterprises of about 10% (Lung, 1997). Accumulated social security funds from these contributions could be invested into the national economy to facilitate development. In this respect, the building of an economically and socially viable social insurance programme for retirement would provide a solid foundation for the economic development of the country in the twenty-first century.

References