

Reforming China's State Socialist Workfare System: A Cautionary and Incremental Approach

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This paper explains the cautionary and incremental approach that China has adopted toward the reform of its state socialist workfare system, an approach in great contrast to the use of shock therapy by some East European countries. This paper adopts a structural-institutional perspective that contextualizes the socialist workfare system into the wider framework of China's restructuring of its command economy. The paper relates workfare to China's dual welfare system and highlights the privileged position that urban state-owned enterprise (SOE) workers enjoy under the socialist workfare system. Workfare has been under harsh criticism, however, as it becomes increasingly incompatible with the emerging so-called socialist market economy. Despite cost reduction as the overall objective in the restructuring of the workfare system, in reality, however, the reforms are more about turning workfare into social welfare and overhauling SOEs to become more economically competitive. Furthermore, this paper explains why the establishment of a three-tier social protection system is related to the reform of workfare. In conclusion, this paper argues that China's reformers are not free in their choice of strategies to adopt in the reform of the workfare and welfare systems. Moreover, how far this cautionary and incremental approach is effective in tackling economic and

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Acknowledgments: An earlier draft of this paper was written during a stay at the East Asian Institute of the National University of Singapore in April and May 1999. I am indebted to Professors Wang Gungwu and John Wong, as well as two anonymous reviewers for their invaluable comments.

welfare reforms is also discussed.

KEYWORDS: Chinese welfare; workfare; social welfare; welfare reform; economic reform

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There has been a recent upsurge of interest in China concerning problems and issues related to the reform of the social security system. The fact that Deng Xiaoping, the late patriarch, launched the economic reforms in 1978 suggests that welfare reforms are, in general, a laggard phenomenon in reform China. However, the Chinese government has now placed a greater role on welfare reform. According to a research group at the Chinese Academy of Social Sciences (CASC), the transition to the socialist market economy has reached its most difficult stage, and the reform of China's social security system is one of the critical hurdles.¹ Despite the importance of social security reform, the Chinese government's approach has been cautious and incremental, being characterized as a "long march" rather than a "great leap."² This paper elaborates the "long march" approach by focusing on one key area—the reform of *workfare* of state-owned enterprises (SOEs)—and relates it to the wider scope of the reform of China's welfare system.

The cause of the reform of the state socialist *workfare* system is primarily structural in the sense that the changes aim to reduce the financial burden of the unprofitable SOEs. Underneath this structural factor is the retreat of the command economy as the driving force for social and economic development in China. The command economy has several important features that are pertinent to the Chinese socialist *workfare* system. First, full employment is guaranteed for the urban workforce. Second, wages are kept at low levels and the gap between the top and the bottom in

¹CASC Project Group on Social Development in China, "The Institutional Reforms and Challenges at the Middle Stage of China's Reform," *Social Sciences in China* 19 (1998): 83-93.

²Athar Hussain, "Social Security in Present-Day China and Its Reform," *American Economic Review* 84, no. 2 (1994): 276-80.

the wage echelon is narrow. Third, those who have employment with a work unit (*danwei*, i.e., economic enterprise, professional institute, or government bureau) are provided with comprehensive in-kind benefits to compensate low in-cash wage in employment. Fourth, secondary redistribution by taxation is not necessary in the low-wage regime because the command economy has already ensured a somewhat egalitarian outcome among the employed population.

In other words, reforming China's state socialist *workfare* system needs to overcome the institutional constraints that have been installed by the command economy. Only a structural-institutional perspective offers a comprehensive understanding of why the Chinese government has adopted a cautionary and incremental approach in reforming its state socialist *workfare* system. There is, however, an alternative strategy, one that was experimented by some former Soviet bloc's countries such as Poland and Russia: shock therapy.³

There are two major reasons why the Chinese government has not taken that alternative path. First, given that most urban employment has been with SOEs (to be discussed later), popular support for a radical reform approach would have been weak. Second, with the absence of a Western-styled political democracy, Chinese reformers have been even more cautious in their strategies toward reform—especially in the aftermath of the Tiananmen Incident. Thus, the approach adopted by Chinese leaders is somewhat defined by the structural and institutional contexts of the country—the political economy of state socialism in general and the command economy in particular. Understandably, the command economy has become structurally and institutionally incompatible with the overall goals of economic reform—opening up China to the outside world and incorporating market operations and principles into the domestic economy. Apparently, Chinese decisionmakers are not free to choose the strategy they, normatively or functionally, likely prefer.

³Josef C. Brada, "The Transformation from Communism to Capitalism: How Far? How Fast?" *Post-Soviet Affairs* 9, no. 2 (1992): 87-110; Peter Murrell, "Evolutionary and Radical Approaches to Economic Reform," *International Studies in Economics and Econometrics* 29 (1993): 215-31.

With the above in mind, this paper first locates the state socialist *welfare* in a wider context of a dual welfare system. Second, it looks into why China needs to reform its welfare system in general and *welfare* system in particular. Third, the inherent problems of *welfare* reform are disentangled to reveal the wider institutional constraints inherited from the command economy. Fourth, the emergence outside the *welfare* arena of an institutionalized social protection system is outlined as an important step forward in the reform of China's state socialist *welfare* system. Finally, a few issues are discussed in the conclusion to assess how far problems and issues facing economic and welfare reforms are effectively being tackled.

A Dual Welfare System: Socialist *Welfare* vs. Residual Social Welfare

Unlike Western welfare systems, the government in China does not require a major role in social spending in social welfare. For instance, the average OECD (Organization for Economic Cooperation and Development) countries spent about 14 percent of gross domestic product (GDP) on social security, which was only one item of social spending in the late 1980s. In China, however, this part of the expenditure is clearly underreported, for the spending on pension and social security indeed counts as benefits for veterans and relief for the poor. This type of spending was only 0.19 percent of China's GDP in 1997, a ratio that is definitely much lower than that in 1978—0.52 percent (see table 1). Thus, we have to include China's labor insurance and welfare fund as government welfare spending. In this regard, a higher figure can be identified. China spent 4.07 percent of its GDP for labor insurance and a welfare fund in 1997—a ratio that is an increase of 1.91 percentage points from the figure of 2.16 percent in 1978 (see table 1). In other words, government spending on benefits for veterans and relief for the poor has not caught up with the phenomenal growth of the economy (i.e., an increase of 20.64 times in national wealth over the same period, see table 1). If this comparison reflects the relative importance of "labor welfare" over "social welfare," we then need to examine China's dual welfare system for some explanation.

Table 1
Welfare Spending as Percentage of GDP in China (Selected Years)

Year	GDP [#]	As Percentage of GDP				Total Welfare Spending as % of GDP
		Spending on culture, education, & health care	Spending on pension & social welfare*	Price subsidies	Labor insurance & welfare fund	
1978	3,624.1	3.11	0.52	0.25	2.16	6.04
1980	4,517.8	3.46	0.45	2.61	3.02	9.54
1985	8,989.1	3.52	0.35	2.91	3.69	10.47
1987	11,954.5	3.37	0.31	2.46	4.26	10.40
1990	18,598.4	3.32	0.30	2.05	5.04	10.71
1993	34,560.5	2.77	0.22	0.87	4.83	8.69
1996	67,559.7	2.52	0.19	0.67	4.03	7.41
1997	74,772.4	2.55	0.19	0.49	4.07	7.30

[#]GDP in 100 million yuan.

*Refers to social relief and personal social services for veterans and their relatives; orphans; elderly; and people with disabilities.

Sources: *Zhongguo tongji nianjian* (China statistical yearbook) (1997), 42, 242, 746; *ibid.* (1998), 55, 276, 795.

In China, even under Deng's economic reforms, the means of production are largely owned by state organizations at different government levels. This remains the case despite the recent official sanction of private ownership. The government relies on its work units, which include SOEs and government bureaus, to do the job of providing sufficient social welfare and social protection for most of its urban population. In this case, to hold this welfare system intact, the government has to maintain a high level of employment.

In this urban welfare system, an individual's status in a work unit has become a lifelong voucher giving access to different welfare packages. Some large state organizations even run their own medical clinics and schools.⁴ Three major items of social services are common: health care

⁴For instance, a mega-corporation in the steelmaking industry with 7,200 employers runs 7 clinic/hospital establishments and 30 schools of all sorts, in addition to numerous canteens, staff quarters, and guesthouses. See *Zhongguo gaige bao* (China Reform Daily), April 1, 1999.

subsidies, pension benefits, and housing subsidies—all of which are usually provided free. In a few cases, however, beneficiaries are charged with an extremely low fee. For instance, the rent paid by urban residents was between 0.5 and 1.5 percent of their wages in the period of 1980-95.⁵ The welfare system of these work units is described as "small-and-comprehensive" or "work-unit-managing-society," indicating the comprehensiveness of the benefits. This is somewhat akin to the almost mythical "cradle-to-grave" benefits of the idealized welfare states of the West, despite the fact that China is a developing country with low level of social spending to GDP. Apparently, this is a welfare phenomenon that conflicts with T. H. Marshall's conception about the development of social citizenship.⁶

The above-mentioned points are the state socialist features of the welfare system; they denote the provision of welfare by the state via its lower-level organizational units, in particular the SOEs. "State" in this sense means the ownership of the means of production. Furthermore, "socialist" implies the underpinning of this strand of welfare system by the principle of "each according to his work/contribution."⁷ Apparently, this is manifested by the employment status, which indicates the contribution of one's labor in exchange for the "iron rice bowl" and "comprehensive welfare" from the state.

Workfare is an appropriate shorthand description for this form of work unit-derived institutionalized welfare, since there is an element of compulsion involved in the employment. We forgo the use of the description of "work unit socialism"⁸ in order to contrast China's experience with the Western conception of *workfare*. *Workfare*, as mostly used in the United States, means the demonstration of intention or effort to work in exchange for welfare benefits from the state.⁹ Therefore, it is generally pu-

⁵Chack-kie Wong, "How Many Poor People in Shanghai Today? The Question of Poverty and Poverty Measure," *Issues & Studies* 33, no. 12 (December 1997): 47.

⁶Mark Selden and Laiyin You, "The Reform of Social Welfare in China," *World Development* 25, no. 10 (1997): 1665.

⁷John Dixon, *The Chinese Welfare System, 1949-79* (New York: Praeger, 1981); Ramesh Mishra, *Society and Social Policy* (London: Macmillan, 1981).

⁸Brantly Womack, "Transfigured Community: Neo-Traditionalism and Work Unit Socialism in China," *The China Quarterly*, no. 126 (1991): 313-32.

⁹Chris Grover and John Stewart, "Market Workfare: Social Security, Social Regulation, and

nitive in practice and negative in moral connotation. This is why recently *workfare* is part of the discussion about underclass, a concept loaded with moralistic explanations about the poor and the socially excluded in society. More importantly, the Western conception of *workfare* is incomplete because of a lack of an institutional dimension. Welfare benefits are generally absent once the recipients have employment. In other words, the conception of *workfare* in the Western sense indicates a process state of welfare, rather than an end state where welfare recipients are institutionally provided with actual benefits for livelihood. When *workfare* took shape primarily in urban employment in China, it was supported by a strong sense of Maoist self-reliance work ethic in the pre-reform era.¹⁰ Apparently, this work ethic has withered away because, once institutionalized, employees have started to regard *workfare* as an unconditional entitlement derived from their employment status. In other words, the underlying ethic has changed to one of institutionally constructed welfare dependency; or, in some observers' words, a state of organized dependency.¹¹

Apparently, China has a dual welfare system in two senses.¹² First, those urban residents who do not have employment status are excluded from *workfare* and are residualized. In addition to the inability to work, those who do not have family relations and no means to make a living are commonly known as the "three no's"—a terminology which usually refers to the official recipient groups of the social assistance program.¹³ Second,

Competitiveness in the 1990s," *Journal of Social Policy* 28, no. 1 (1999): 73-96; Desmond King, "From Clinton to Blair: The Democratic (Party) Origins of Welfare to Work," *The Political Quarterly* 70, no. 1 (1999): 62-71; Phil Mizen, "Work, Welfare, and the Regulation of the Poor: The Pessimism of Post-Structuralism," *Capital and Class*, no. 65 (1998): 35-53.

¹⁰Dixon, *The Chinese Welfare System*, 16.

¹¹Ching-kwan Lee, "From Organized Dependence to Disorganized Despotism: Changing Labour Regimes in Chinese Factories," *The China Quarterly*, no. 157 (1999): 44-71; Andrew G. Walder, *Communist Neo-Traditionalism* (Berkeley: University of California Press, 1986), 29-84.

¹²Hussain, "Social Security in Present-Day China," 278; Selden and You, "The Reform of Social Welfare in China," 1657-58.

¹³They are the official recipients of the state's long-term poverty relief benefits in the urban areas in China. Most are mental patients, lepers, older people without families, and orphans. Often, low-income households are not called the "three no's," but "households in

rural peasants are also excluded from *workfare* because they do not have a work unit to take care of their welfare. For those who cannot be self-reliant and are without family support in the rural areas, are covered by the "five guarantees" scheme. This scheme, equivalent to the "three no's" of the urban areas, has been in place in the rural areas since 1957. The "five guarantees" include the provision of clothes, food, housing, medicine, and burial services. In 1997, the urban and rural poverty relief schemes benefited about 2.7 million people each. These figures are far below the total number of those who require help from the state,¹⁴ despite the fact that the right to basic social protection is enshrined in the PRC Constitution.¹⁵ The problem is that lower-level governments have to take up the major share in the financing of social protection. When local budgets are depleted, the newcomers poor do not receive relief. Thus, social protection is not yet an institutionalized system in rural China.

The dual welfare system in place is clearly in the favor of urban residents who have employment in the SOEs. Also worthy to note is that in China's welfare system, the state does not play a direct role, especially in the realms of financing and welfare provision, because the state primarily relies on its regulating role (i.e., enforcement). In principle, productive enterprises in a command economy do not have to worry about competition and profit-making. Welfare expenses for their employees are their social obligation as they themselves are state apparatuses. In this light, the state's job is to oversee whether productive enterprises follow its regulations in regard to *workfare*. Nevertheless, the state has also directly provided social services such as secondary schools and universities that serve a target

hardship" (*kunnan hu*). They are provided with short-term relief in the forms of oil and rice coupons.

¹⁴It was estimated that in the 1950s, about 3-5 percent of the rural population needed relief from the state; one estimate suggests that only 1.5 percent received it. See Dixon, *The Chinese Welfare System*, 189.

¹⁵The right to basic social protection is enshrined in Art. 45 of the PRC's 1982 Constitution which states: "Citizens of the PRC have the right to material assistance from the state and society when they are old, ill, and disabled. The state develops social insurance, social relief, and medical and health services that are required to enable citizens to enjoy this right. . . . The state and society help make arrangements for work, livelihood, and education of the blind, deaf-mute, and other handicapped persons."

population wider than the employees and their family members of an individual work unit. In the same light, hospitals are established as public services because they require capital investment and maintenance for their operations usually beyond an individual work unit's capacity. However, government spending on education and health (including culture) only amounted to 2.55 percent of China's GDP in 1997—a share much less than the spending on labor insurance and the welfare fund in the same year (see table 1). This comparison reflects the relative weight given to *workfare* in China's dual welfare system.

In sum, China has a dual welfare system that is in favor of those who have SOE employment. In general, those who are in the rural areas and those who do not have employment are residualized. More importantly, a relatively larger share of China's national wealth has been allocated to its spending on *workfare*. This reflects the relative weight, if not rigidity, of *workfare* as compared with social welfare in China.

Welfare Reform Driven by Economic Reform

The state socialist *workfare* system has come under harsh criticism with the introduction of market-oriented reforms since 1978. The major target for criticism is the job security system that results from the full-employment policy. This system is regarded as an impediment to the market competitiveness of SOEs. The SOEs have been regarded as having low economic productivity, and their employees as having low work incentives. A recent source suggests that more than 40 percent of the SOEs are unprofitable, while one-third to one-half of their employees are redundant.¹⁶ Needless to say, *workfare* is seen as an impediment to economic productivity of the SOEs as *workfare* is a mounting burden on production costs.

¹⁶Zhang Yuming, "Rational Analysis of the 'Retreat' Question of State-Owned Enterprises," *Fudan xuebao* (Fudan University Journal, Social Science Edition), 1998, no. 2:37-41. This sweeping argument about the loss-making of SOEs is too general, however. In fact, according to a 1993 survey, large and medium-sized SOEs consisted only 1.09 percent and 2.55 percent of all SOEs, respectively. Therefore, the 40 percent of unprofitable SOEs were mostly from small-sized ones.

Table 2**Employment of State-Owned Enterprises (SOEs) as Percentage of Total Urban Employment in China (Selected Years)**

Year	Total Urban Employment (1,000)	Urban Employment of SOEs (1,000)	Employment of SOEs as % of Total Urban Employment
1952	24,860	15,800	63.6
1957	32,050	24,510	76.5
1962	45,370	33,090	72.9
1965	51,360	37,380	72.8
1978	95,140	74,510	78.3
1980	105,250	80,190	76.2
1985	128,080	89,900	70.2
1990	147,300	103,460	70.2
1993	175,890	109,200	62.1
1994	184,130	112,140	60.9
1995	190,930	112,610	59.0
1996	198,150	112,440	56.7
1997	202,070	110,440	54.7
1998	206,780	90,580	43.8

Sources: *Zhongguo tongji nianjian* (1994), 84; *ibid.* (1998), 127; *Zhongguo tongji zhaiyao* (China statistical summary), 1999, 33.

The "iron rice bowl," moreover, discourages labor mobility.

In addressing these problems related to *workfare*, the "iron rice bowl" of job security began to be dismantled in 1986 by a series of measures, including the introduction of the contract worker system, bankruptcy law, open recruitment of labor, and the allowance of employee dismissal. Thereafter, SOEs have been able to lay off their redundant and inefficient workers, and the enterprises themselves are liable to bankruptcy in cases of lossmaking. Nevertheless, SOEs still employ the largest share of urban workers. In 1985, for instance, SOEs employed 70.2 percent of total urban workers; this share remained the same in 1990. The remarkable fact is that SOE employment, in absolute terms, grew from 89.9 million in 1985 to 103.46 million in 1990. This figure remained stable at around 110 million in 1993-97, and dropped to 90.58 million in 1998, a 43.8 percent share of total urban employment (see table 2). Despite this recent drop, the SOEs still play the important social function of providing employment through-

Table 3

A Balance Sheet of the Financial Contributions of SOEs to Government Total Revenue in China (1992-96)

Year	Government Total Revenue (billion <i>yuan</i>)	Revenue from SOEs (billion <i>yuan</i>)	Government Subsidies to Unprofitable Enterprises (billion <i>yuan</i>)	SOE Contribution as Share of Total Government Revenue
1992	348.34	248.30	44.50	71.3%
1993	439.00	311.57	44.13	71.6%
1994	521.81	372.74	36.62	71.4%
1995	624.22	444.10	32.78	71.5%
1996	740.80	—	33.74	—

Source: *Zhongguo tongji nianjian* (1997), 233.

out the 1990s. The recent drastic drop is seemingly a result of the policy change to allow the privatization of the SOEs (i.e., their sale and corporatization) after the Chinese Communist Party's (CCP's) Fifteenth Congress in 1997.¹⁷ Apparently, welfare reforms have contributed to this restructuring process of the SOEs in China today. This role will be discussed later.

The SOEs carry out another important function: they are the major source of government revenues. Table 3 illustrates that the SOEs consistently contributed up to 71 percent of the government's total revenue between the years 1992 and 1995. In terms of current monetary values, in 1995 the SOEs paid a total of 444.1 billion *yuan* to the government. In contrast, government subsidies to the unprofitable SOEs only amounted to 32.78 billion *yuan*. The SOEs are thus a major revenue-raiser that the Chinese government does not wish to part with easily.

¹⁷The Fourth Plenary Session of the CCP's Fifteenth Central Committee held in September 1999 decided that SOEs will retain their predominant role in certain strategic and important industries in an economy with multiple types of ownership. At the same time, the meeting also reiterated that privatization should not be the strategy for future restructuring of SOEs. See *Ming Pao* (Hong Kong), September 23, 1999, available at *Ming Pao Electronic News* <<http://www.mingpao.com/newspaper/archives/990923/cab1hl.htm>>. These new ideas suggest that further decreases in the category of SOEs are inevitable, yet SOEs will reappear under new titles such as corporations by "limited liabilities"—a new type of ownership which appears in the 1999 edition of *Zhongguo tongji nianjian* (China statistical yearbook).

It seems that the SOEs have not been dismantled; in fact, it is the growth of the non-SOE sector that has contributed to the drop in the share of SOE urban employment.¹⁸ Two important implications can be generalized from the figures in table 2 on the development of China's welfare system. First, SOEs will remain the predominant ownership type of enterprises in China in the foreseeable future; thus, imperative is to restructure the *workfare* system and "iron rice bowl" in line with market principles and mechanisms. Second, the growing of non-SOE employment means that China must develop a new welfare system with the capacity to include urban employment. These two factors are interrelated. For instance, if newly emerging privately-owned or foreign-invested enterprises are not included in a welfare system that requires equal treatment for all, the SOEs would be placed in a structurally disadvantaged position in terms of production costs. Considered in this light, the reform of China's welfare system is structural, and thus quite pertinent to economic reforms.

The whole objective of reforming China's welfare system centers around the restructuring of the SOEs into more market-competitive enterprises. Nevertheless, this is a matter related to the restructuring of *workfare* and the reform of the larger welfare system. However, Chinese reformers must be very careful about the restructuring of the SOEs because these enterprises have still been the major employment and government revenue providers. Henceforth, the reform of *workfare* is not meant to be load-shedding, but to incorporate *workfare* into the larger welfare system.

The Main Features of Welfare Reform

The reform of China's *workfare* system has two component ideas: first, to transform *workfare* into *social* welfare, outside the domain of work units; second, to transfer the larger welfare system into one that incor-

¹⁸In general, the newly emerging company types such as "shareholding companies," "companies by limited liabilities," and "units with collaborated shares" are in fact former SOEs. Although they are not categorized as SOEs, these new types of enterprises still have similar welfare responsibilities for their employees.

porates *workfare*. With this understanding, we can now illustrate the main features of China's welfare reform.

First, the reform endeavor can be characterized as the socialization of the welfare system: moving from *workfare* to social insurance. The *workfare* system is, in fact, not a "social" system;¹⁹ therefore, the primary reform initiative is to transfer the lifelong security and welfare provided to workers by individual work units to a social system managed by quasi-statutory bodies. In this regard, a third party, which is a newly established bureau, collects contributions for health care, retirement benefits, unemployment benefits, fertility, and housing benefits from enterprises—including non-SOEs—in order to spread risk. In this regard, individual workers are no longer tied to their work units simply because they would not fear the loss of their welfare entitlements in case of job change. Other things being equal, labor mobility is apparently enhanced in a social insurance system.

In general, this process is predominantly an administrative reform rather than a load-shedding exercise to relieve enterprises of their welfare responsibility.²⁰ In this light, despite the reform initiatives, the contributions of enterprises to social insurance schemes as a share of the gross wage expenses remain enormous. It is quite common for enterprises to contribute around 25 percent of their gross wage expenses to their workers' retirement fund, 8 to 10 percent to health care, about 6 percent to housing, and another 1 percent and 0.5 percent to unemployment and fertility insurance schemes, respectively. Added together, a minimum of 40 percent of the gross wages earmarked for insurance contributions is often the case among enterprises.

The second characteristic is the institutionalization of individual responsibility in China's welfare system. Despite its comprehensiveness, employees generally do not have to pay for their benefits. Even if they do, their contribution is minimal. For instance, it was only until 1991 when employees were required to contribute up to 3 percent of their total wages

¹⁹Huang Xiaojing and Yang Xiao, "From Iron Rice Bowls to Labor Markets: Reforming the Social Security System," in *Reform in China*, ed. Bruce Reynolds (New York: M.E. Sharpe, 1987), 148.

²⁰This is always misunderstood with regard to reform of China's social security system. See Hussain, "Social Security in Present-Day China," 277.

for their retirement benefits. As there is an obligation "deficit" in the *work-fare* system, unscrupulous overuse is inevitable, especially in health care. For instance, a phenomenon called "*xiao bing da yang*" (big rest for minor illness) is a case in point. Therefore, health care reform is about the institutionalization of the principle of individual responsibility in order to contain costs.

An example of health care reform is illustrative of how individual responsibility can be institutionalized. An experimental project in the name of the "Two Jiangs" model²¹ was first initiated in two medium-sized cities in late 1994 and was later extended to cover sixty more cities for further trial in 1996. Basically, the experiment sought to put a brake on the overloading of health care services due to unchecked use by beneficiaries. The major strategy was to incorporate incentive (and disincentive) mechanisms. The experiment divided the total contributions from both employers (up to 10 percent) and employees (1 percent, initially) into two accounts. The first account is for "personal savings" and is usually more than half of the total contributions, and the second is the "socially coordinated account." The main idea is that individuals must exhaust their personal accounts first before they are allowed, with some additional criteria,²² to use the "socially coordinated accounts." Those who do not use their own accounts may keep those savings. Planners have hoped that, in this manner, the problem of unscrupulous overuse in health care insurance can be minimized. Later in November 1998, the government launched a new proposal along the same line of the "Two Jiangs" model, but with the introduction of a withdrawal ceiling from the "socially coordinated account." Under this new proposal, the contribution rate from enterprises is reduced from 10 to

²¹In 1994, the State Council chose Zhenjiang of Jiangsu province and Jiujiang of Jiangxi province as the pilot scheme to experiment with the reform of China's medical insurance system. Ziao Qinzeng, "The Ministry of Health and Social Welfare," in *Zhongguo shehui fuli* (China's social welfare), ed. Wang Sibin et al. (Hong Kong: Zhonghua shuju, 1998), 94-118.

²²For instance, they have to pay in cash up to 5 percent of their annual income at first; afterwards, employees are allowed to draw money from the "socially coordinated accounts." However, they still have to share part of the medical costs, with the personal contribution percentage declining with the rise in total expenses. For example, personal contributions vary from 10-20 percent for the first 5,000 *yuan* and are gradually lowered to 2-5 percent in case the amount exceeds 10,000 *yuan*.

6 percent while the employee contribution is increased from 1 to 2 percent. The maximum amount beneficiaries can receive from the "socially coordinated accounts" is four times the average wage. Beneficiaries must exhaust their "personal savings accounts" first before they are entitled to access the social accounts.²³ In brief, we can discern a trend toward the increasing of the part paid by employees; this reflects a very cautious move by the reformers to implant the principle of shared responsibility into *workfare*. Similar mechanisms to institutionalize individual responsibility are also implemented in such social insurance schemes as retirement benefits.

The third characteristic is the privatization of the welfare system. This is most evident in the housing sector. Housing rents for workers have been fixed without regard for building and maintenance costs; therefore, it is difficult for work units to build new houses or to maintain the present stock on the basis of rental charges. Increasing rents is one possible strategy, but one that is less effective simply because the rental base is too low. Nevertheless, rental increases are also carried out in phases. Therefore, privatizing housing is regarded as a better option. Two methods are attempted; one is to sell the present stock of housing in order to cast off, once and for all, future maintenance and repair responsibilities. Apparently, this is less successful because the sitting tenants are also concerned with the maintenance costs and the resale value of the housing. Second, the newly built houses are also sold at heavily subsidized prices. The problems with this strategy are quite complicated.²⁴ Issues such as the resale market,

²³Zhao Man, "Reform and Innovation of the Medical Insurance System," *Zhongguo gaige* (China Reform), 1999, no. 2:53.

²⁴The need for housing reform was first raised by Deng Xiaoping in the early 1980s with the idea of the need to "recycle" the building, maintenance, and management of social housing provided by the state and work units. Then Premier Zhao Ziyang authorized trial implementation in a few medium-sized cities such as Bengbu of Anhui province and Yantai of Shandong province during 1985-88 with the central idea of increasing rents to make home purchase schemes attractive. It was suspended for a while after the Tiananmen Incident. The plan was restarted again in 1992 after Deng's visit to south China earlier that year. The emphasis is, however, placed on home purchases. See Peter N.S. Lee, "Housing Privatization with Chinese Characteristics," in *Social Change and Social Policy in Contemporary China*, ed. Linda Wong and Stewart MacPherson (Aldershot, U.K.: Avebury, 1995), 126; Kwokyu Lau, "Urban Housing Reform in China amidst Property Boom Year," in *China Review 1993*, ed. Joseph Y.S. Cheng and Maurice Brosseau (Hong Kong: Chinese University Press, 1993), 24.9-24.10. Apart from the above brief background, the more eye-catching

mortgage financing, private property rights, and wage structure all need additional attention.

In general, the primary reform endeavor is to transform the *workfare* system into one that is social and incorporated with individual interests. Apparently, these features of welfare reform reflect more than the intention to cut production costs. They are also intended to overhaul the *workfare* system in order to make it compatible with a market-driven economy. Apart from this, the other reform objective is to include the non-SOEs into the larger welfare system so that the SOEs would not be placed in a disadvantageous position in terms of welfare spending. In other words, the non-SOEs are included in the newly emerging social welfare system. Nevertheless, the responsibility of enterprises for the welfare of their employees remains the same. SOE workers remain protected (perhaps less generously) and in some aspects gain more leeway (i.e., job mobility without losing significant benefits). SOE workers now enjoy both personal incentive and responsibility (e.g., the establishment of personal savings accounts and home purchase schemes).

Problems of *Workfare* Reform and a Social Welfare Solution

In general, the reform effort seeks to restructure the *workfare* system as part of the social welfare system. The predominant problem is that *workfare* is based on a wage structure with low in-cash wages and nearly free and noncontributory comprehensive in-kind supplements. In other words, when this *workfare* is restructured to one that is social, the wage structure has not yet been reformed at a pace that allows the welfare benefits to reflect the current monetary value. Henceforth, social insurance for retirement carries a particular set of problems, indicating the paradox of under-benefits and overcontributions.²⁵ On the one hand, the labor and welfare

issues about housing reforms are corruption and drainage of state assets. These are often termed as "rent-seeking" phenomenon by Chinese authors.

²⁵ Chack-kie Wong, "Reforms in the Social Security System," in *China Review 1995*, ed. Lo Chi Kin, Suzanne Pepper, and Tsui Kai Yuen (Hong Kong: Chinese University Press, 1995), 13.6.

expenses of enterprises are the equivalent to about one-third of the total wages or 40-50 percent of the gross wages. On the other hand, retired workers normally enjoy a benefit level equivalent to about 30-40 percent of the average wage.²⁶

In this regard, the Chinese government likely needs to inject more resources into the system to tackle this paradox either by lowering contribution levels or by increasing benefit standards. When taking the decline of state financial capacity into consideration, however, it is no surprise that the government has not been able to do so. For instance, government expenditures amounted to 30.96 percent of GDP when China began reforms in 1978; however, the respective percentage was drastically reduced to 12.35 percent in 1997.²⁷

Inadequate state financial capacity for smoothing the restructuring of the *workfare* system can also be reflected in the undercoverage of the newly created social insurance schemes for retirement, unemployment, and health care. For instance, urban employment was estimated to be at around 190 million people in 1995; only 89 million (or 46.6 percent) of which joined the social insurance for retirement scheme, whereas 95 million (or 50 percent) participated in unemployment insurance program in the same year.²⁸ In the case of the so-called coordinated scheme for severe illness in health care, only 5 million workers (or 2.6 percent) of the total urban employed population joined at the end of 1994.²⁹

Because of the lack of additional resources, the reform endeavor is in fact a resource extraction project. This project seeks to coerce all

²⁶Ibid.

²⁷Calculated on the basis of total government expenditure and GDP figures in *Zhongguo tongji nianjian 1998* (China statistical yearbook 1998) (Beijing: Zhongguo tongji chubanshe, 1998).

²⁸Calculated on the basis of sources in Tang Jun, "The Review and Forecast of China's Social Security Reforms," in Wang, *Zhongguo shehui fuli*, 321-22; and table 1 on total urban employment in China.

²⁹The very small coverage of this particular medical insurance scheme serves only to highlight the issue of undercoverage. In fact, there were many other health care insurance schemes in China at the time. The recent attempt in the proposal for the "Reform of Workers' Medical Insurance," which was released in November 1998, sets the coverage target of all urban employees—300 million. See Zhao, "Reform and Innovation of the Medical Insurance System," 52.

kinds of enterprises to join the social insurance schemes managed by quasi-statutory bodies in order to maximize the redistributive effects between age groups (generations) as well as enterprises (both profitable and unprofitable). Unsurprisingly, those enterprises that have a younger workforce or which are more profitable are reluctant to join, unless made mandatory. Apart from this, those cities with a younger population are also reluctant to join a province-wide redistributive social insurance fund.³⁰ This explains why that in 1999, according to the information now available, only thirteen province-wide social insurance schemes have been established; the other schemes are all city-based. Probably because of this resistance from local-level governments and enterprises, a law on social security was promulgated that originally was to go in effect in 1995. Later, it was introduced in the form of a State Council document in 1997, requiring every enterprise to join the retirement insurance program in 1998.³¹ Even if the State Council directs those profitable enterprises to join the socially coordinated insurance schemes (such as the retirement plan), implementation will be problematic.³² This reminds us of the gap between policy initiative and policy implementation that is common in China today.

In general, the central government in Beijing is cautious and incremental in its approach toward the reform of the welfare system. Evidently, any new move is usually driven by the needs of economic restructuring, in particular the restructuring of the SOEs.³³ The problems encountered in the

³⁰Complicating the situation is that some cities (such as Guangzhou) with aging labor forces seem to benefit from joining the province-based social insurance fund. The concern seems interest-based, as these cities are not willing to hand over the control of their own "golden geese" to the provincial authorities.

³¹Chen Juegui, "The Reform of State-Owned Enterprises and the Establishment of the Social Insurance System," *Jiangxi caijing daxue xuebao* (Journal of Jiangxi University of Finance and Economics) (Nanchang), 1999, no. 1:8-12.

³²Before 1998, the State Council allowed enterprises under the administration of eleven ministries to set up their own insurance schemes. According to a report in 1999, this exemption from joining the city/provincial-level social insurance schemes was terminated in 1998. See Yuan Yonghai, "Reflection on the Establishment of a Multi-Level Social Security System," *Daziran tansuo* (Exploration of Great Nature) (Chengtu), 1999, no. 5:10-13.

³³For instance, in 1994, China proclaimed an "Eight-Seven Plan" to relieve 80 million rural people from poverty within a time span of seven years. However, little has yet to be heard since regarding the progress despite the approaching deadline. Evidently, this is an issue unrelated to the restructuring of SOEs.

reform of the *workfare* system itself are clear and no short-cut can be seen. However, China still sees the restructuring of the SOEs as pertinent to the success of the overall economic reforms.³⁴ The paramount problem is to deal with the unprofitable SOEs, most of which are small in size. The most effective way is to allow the unprofitable SOEs to declare bankruptcy or to equip them with the power to lay off their redundant workers. Chinese policymakers thus have to confront the sizeable problem of social protection in view of the unanticipated massive layoffs resulting from the restructuring of the unprofitable SOEs.

Clearly, social protection stands in the way to any effective restructuring of the SOEs. Social protection refers to the provision by the state or society of a minimum living standard to those who cannot fend for themselves. Unemployment, poverty, and population aging are on the rise,³⁵ all of which are related to the restructuring of the SOEs, as these enterprises are now allowed to lay off redundant workers or to go bankrupt. In this regard, a safety net of last resort has to be established to meet the basic needs of those being laid off or without a work unit to rely on (their work units might be bankrupt as well).

Recently, a three-tier social protection system has been installed in most cities in China. At the first level, a minimum wage is established with a benefit for the workers to maintain a basic living standard healthy enough to work. The second is the minimum unemployment benefits which are set below minimum wage. This living standard results in some hardship in order to discourage dependency. The third and lowest level is the newly devised "minimum living protection line" (MLPL), initiated first by the Shanghai municipal government in 1993. Nowadays, nearly all cities in China have such a poverty relief system in place.³⁶ The last social protection standard is usually set at a level equivalent to 30-40 percent of the average wage of each city. Apparently, this only allows a subsistence

³⁴"The Institutional Reforms and Challenges at the Middle Stage of China's Reform," 90-91.

³⁵Ruby C.M. Chau and Sam W.K. Yu, "Social Welfare and Economic Development in China and Hong Kong," *Critical Social Policy* 19, no. 1 (1999): 87-107.

³⁶Information gleaned from the Ministry of Civil Affairs. The problem confronting the Chinese authorities nowadays is the inadequacy of benefits, especially in the cities that are less well-off.

standard of living fair enough to fend off absolute destitution. However, judging from China's status as a developing economy, a poverty relief standard that allows the purchase of basic necessities plus some sundry items should be cautiously accepted as appropriate.³⁷

The establishment of this social protection of last resort—in fact, a poverty line—needs further elaboration in terms of its significance in the relations between economic restructuring and the reform of the *workfare* system. Economic restructuring of the SOEs needs to lay off redundant workers and to let unprofitable enterprises go bankrupt. This requires the establishment of unemployment social insurance schemes in order to help the unemployed to cope with an interruption in earning power. However, there are still loopholes to be tackled in order for no one to be left unattended in case of insufficient income. For instance, not all enterprises have joined the social insurance scheme. In addition, there is a time limit on the entitlement to unemployment benefits so as to encourage reemployment, apart from the financial consideration. Henceforth, an institutionalized and open-ended poverty relief system has to be installed to replace the "three no's" system. In this new system, any household whose income falls below the MLPL is eligible for government assistance.³⁸ Note that this, unlike the two upper-tier ones, is a household-based benefit. The objective is clear: individuals must resort to family resources before they turn to state welfare.

Needless to say, this institutionalization of social protection by establishing the MLPL is in response to the threat of massive layoffs and bankruptcy of unprofitable enterprises, the SOEs in particular. Apparently, this vividly illustrates that economic restructuring primarily drives the re-

³⁷The calculation of benefits in Shanghai allows adjustments for price changes. Usually, this is less than an adjustment based on wage changes in the case of a fast-growing economy.

³⁸This is an open-ended form of entitlement as contrasted with the traditional "three no's." Shanghai, the first city government to implement the MLPL, was quite worried about the financial implications when it started the scheme in 1993. Later, officials discovered that the low level of provided benefits resulted in few people coming forth to make claims. Indeed, on top of this MLPL, city governments like Shanghai also provide different sorts of tangible relief (such as oil and rice coupons) for those who are identified as *kunnan hu*. Those households whose income falls between the MLPL and the low-income households (the lowest 10 percent of households in terms of income) are eligible for this sort of in-kind relief.

form of the welfare system. More importantly, a modern social assistance system offering a safety net of last resort has been finally established, albeit in rudimentary shape, in urban China. In sum, a social welfare solution is devised to cope with the inherent problems that arise from the structural-institutional constraints laid down by the larger framework of a command economy.

Conclusion and Discussion: Chinese Social Welfare into the New Millennium

To conclude, the Chinese government has been cautious and incremental in its reform of the urban welfare system that is primarily predominated by state socialist *workfare*. China's welfare system is best described as a dual system that provides comprehensive welfare for urban SOE employees while the welfare of rural peasants is primarily residualized. The reform of *workfare* is driven by the need to restructure SOEs with the objective to make them more economically competitive. However, this load-shedding function has apparently not been successful at all; the responsibility of enterprises for the welfare of their employees remains the same. Despite various reform endeavors, the SOEs have remained the major providers of urban employment and government revenue. Clearly, the Chinese government has strong grounds to undertake a cautionary approach.

Moreover, reforms of the *workfare* system are constrained by the structural-institutional features inherited from a command economy, such as a "low wage, full employment" regime and inadequate tax revenues for redistribution. Given that economic restructuring and tax reforms are long-term objectives of economic reform, the Chinese government recently started to reform its welfare system in relation to *workfare*. Three main features of the reform strategies have been identified in this paper: socialization, institutionalization of individual responsibility, and privatization. These are attempts to "socialize" *workfare* into the larger welfare system and to reform the larger welfare system to allow SOEs equal treatment, in terms of welfare costs, as the other non-SOEs. In the meantime, a three-

tier social protection system has been recently established to serve as a safety net of last resort. In this connection, a social welfare solution is set up to cope with the newly emerging poverty resulting from the restructuring of the unprofitable SOEs. All in all, these illustrate that *workfare* and welfare reforms in China are initiated from needs and forces outside the welfare domain, and that they are indeed part of the larger institutional transformation of Chinese society to the so-called socialist market economy.

In sum, the reform of China's state socialist welfare has to be understood from an institutional-structural perspective. China's welfare system is not divorced from its overall economic and social systems. A cautious and incremental approach, insofar as adopted, has been defined primarily by factors beyond the control of reformers in China. However, such a cautionary and incremental approach does not mean issues and problems facing welfare reforms in particular and economic reform at large are effectively being tackled. Given the above, three related issues are briefly discussed below in order to explore the future development of related issues in China in the new millennium.

First, some argue that welfare reforms are driven by the need for economic reform. Thus, important is to assess whether welfare reform helps to mitigate the obstacles it was designed to overcome. The main features of welfare reform outlined above—socialization, institutionalization of individual responsibility, and privatization—are apparently helpful in creating an institutional arrangement of welfare that is compatible with the incorporation of market operations and principles. Judging from the limited coverage of social insurance schemes so far, resistance to reform should not be underestimated. However, the welfare reform endeavors, especially the establishment of a three-tier social protection system, with three social security lines, are useful for the prevention of any resident of registered status—retired or laid-off worker—from being deprived of a basic living. Perhaps, there are reports concerning retired or laid-off workers protesting against inadequate benefits; however, there has not been serious social unrest amidst increases in unemployment and layoffs in recent years. This circumstantial evidence suggests that the Chinese government's cautionary and incremental approach is effective in minimizing the social costs

inflicted upon the most deprived groups in the course of economic restructuring.

The three-tier social protection system, which now seems to have been adopted by most cities, paves the ground for the restructuring of the SOEs. This is reflected by the decline of urban employment in both absolute numbers and the share of total urban employment by the SOEs from 1996 onwards (see table 2). This three-tier social protection system is not only used by the Chinese government for restructuring the SOEs, but is also regarded as an instrument to increase household consumption for the sake of sustaining economic growth.³⁹

On the basis of this circumstantial evidence, welfare reforms seem instrumental to social stability and economic reform. These reforms are even taken as economic measures, as evidenced by the Chinese government's latest move to use them to boost household consumption.

Second is the issue of adequate financing of social insurance: Will the insurance funds, now saved, be available when they are most needed? Perhaps the paradox of high contribution rates yet low benefit levels is one reason underlying this worry. The other legitimate worry is the misuse or even corruption of insurance funds by the management authorities.⁴⁰ At present, the issue of "emptied [personal savings] accounts" is a case in point. This suggests that the personal savings accounts are primarily transferred to the socially coordinated accounts, as the latter have been emptied in the first place. Given this sort of difficulty, there are many initiatives or suggestions to cope with the issue of inadequate financing of social insurance. The further extraction of funds by extending the coverage to all types of enterprises is the official policy. However, resistance to this initiative has been enormous. For example, it was mentioned earlier that the

³⁹In July 1999, the Chinese government increased the benefit level of all three social security benefits by 30 percent. This is cited by the Municipal Survey Team of Guangdong Province as one of the main reasons underlying the drastic increase in the consumption of durable goods in September 1999, as compared with that of September 1998. See *Hong Kong Financial Times*, October 16, 1999.

⁴⁰Definitely, this is an issue without any "quick fix" solution. The problem is related to national wealth (for sufficient state financial ability to redistribute), comparative high remuneration for civil servants (higher costs to corruption), and open and democratic government (accountability of governance).

State Council planned to start the provincial-level social coordination of retirement insurance in 1998. Little evidence suggests that this policy initiative has been followed suit. Alternative suggestions such as the sale of SOE assets to pay for the retirement benefits of employees from those bankrupted enterprises and the establishment of social security taxes are in the pipeline.⁴¹ All these examples reflect the complications of policy implementation in China. Evidently, there is an enormous gap between policy planning and policy implementation, not to mention policy outcome, even in a society with a very strong political state.

Third, one may ponder whether social measures such as welfare reforms can solve economic and even political problems. Neo-Marxist political economy analysis may be helpful in this regard. Marxism suggests that social welfare, in terms of social policy, both legitimizes and reduces capital accumulation.⁴² In general, the legitimization of capital is carried out by the extraction of resources through taxation so that the cost of production can be socialized. Nevertheless, there is always a contradiction between capital's need of accumulation and its need of legitimization. The current issue in the West is the recognition of the greater power that capital enjoys in a globalized economy. In this respect, national governments have adopted welfare reform initiatives such as privatization and retrenching in order to reduce public expenditures and incur less extraction from the production sphere for capital accumulation. In other words, welfare reforms are social, economic, and political in nature.

In the Chinese case, the government's initial drive to legitimize economic reforms is to turn socialist *workfare* into social welfare without additional financial commitment from the state. Now, it has to go back to the use of state finances (albeit on the part of local government) to move ahead in welfare reform, as evident from the use of an institutionalized poverty

⁴¹Chen, "The Reform of State-Owned Enterprises," 8-12; Yu Lanxiang and Lu Jiansuo, "The Support of the Primary Financial Structure of China's Social Security System: Exploring the Use of Social Security Tax," *Shanxi caijing daxue xuebao* (Journal of Shanxi University of Finance and Economics) (Taiyuan), 1999, no. 1:50-52.

⁴²Ian Gough, *The Political Economy of the Welfare State* (London: Macmillan, 1979); James S. O'Connor, *The Fiscal Crisis of the State* (New York: St. Martin's Press, 1973); Claus Offe, *The Contradictions of the Welfare State* (London: Hutchinson, 1984).

line (i.e., MLPL) over the past few years. Needless to say, this social welfare measure must be funded by public taxation. Thus, the Chinese government has to adopt Western welfare state practices in order to politically legitimize its reform endeavor. This recent development indicates the interdependence between social, economic, and political issues, as well as the convergence of the Chinese welfare system to the Western welfare model by adopting more institutional-redistributive welfare practices. If this is the trend, the "fiscal crisis" of the Western welfare states should be a warning to the Chinese government: welfare issues of this sort are better tackled in an era with higher growth rates in order to enjoy the benefits of the so-called growth dividend.⁴³ With the recent slowing down of China's growth rates, it seems that the Chinese government has to speed up its welfare reform initiatives.

In conclusion, the Chinese "long march" into welfare reforms is a good story to reveal the constraints imposed upon governments. The restructuring of *workfare* to social welfare is apparently dictated by factors beyond the control of Chinese reformers. Despite this, welfare reforms in China seem—based on circumstantial evidence—to serve the purposes of mitigating social costs and paving the way for further economic reforms. Nevertheless, quite a number of inherent problems related to the larger institutional changes have to be tackled.

Whether the Chinese government can turn its state socialist *workfare* into social welfare remains to be seen. Three things are quite certain, however, as China approaches the new millennium. First, what is occurring in China today is institutional transformation. This trend seems irreversible and will have an impact far beyond the economic domain, as evidenced in our case study of the reform of China's state socialist *workfare*. Second, in the welfare domain, state socialist *workfare* of the pre-reform era is clearly a thing of the past. This is another irreversible trend. Third and finally, more institutional-redistributive welfare practices seem inevitable because of the need to mitigate any social discontent arising from the widened so-

⁴³Rudolf Klein, "The Welfare State: A Self-inflicted Crisis?" *Political Quarterly* 51, no. 1 (1980): 24-34; Vic George and Stewart Miller, *Social Policy Towards 2000: Squaring the Welfare Circle* (London and New York: Routledge, 1994).

cial disparities of a market-oriented economy. For instance, low-cost social rental housing should be provided as part of the overall housing reform that is oriented toward home ownership. Likewise, any increase in university tuition fees has to incorporate fee subsidy scheme for students from poorer families. These welfare practices are redistributive, common among Western welfare systems, and they have to be in-built as part the reform initiative to enhance the state's legitimization. It seems that more commonality between China and the West is occurring as we enter the new millennium.