

## The Great Transformation: The Double Movement in China

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Both the title and the subtitle of this essay are adopted from Karl Polanyi, who published his famous book *The Great Transformation: The Political and Economic Origins of Our Time*<sup>1</sup> in 1944. More than six decades have passed since its publication, but, as Joseph E. Stiglitz states in the preface of the recent new reprint, “the issues and perspectives Polanyi raises have not lost their salience . . . it often seems as if Polanyi is speaking directly to present-day issues.”<sup>2</sup>

Although Polanyi’s analysis is elaborate and abstruse, his point of view is concise and straightforward. In short, he argues that “the idea of a self-regulating market implied a stark utopianism. Such an institution could not exist for any length of time without annihilating the human and natural substance of society; it would physically destroy man and transform his sur-

Unless otherwise indicated, all data presented in this essay come from the author’s research.

1. See Karl Polanyi, *The Great Transformation: The Political and Economic Origins of Our Time* (Boston: Beacon Press, 2001).

2. Polanyi, *The Great Transformation*, vii.

roundings into a wilderness.”<sup>3</sup> According to Polanyi, the market has always existed throughout the history of mankind, but it is rare to see a market economy. If a market economy has existed, it has not been a fully functioning one. Until the nineteenth century, the economy had always been embedded in society. We should call such an economy a “moral economy,” because the economic activities were subordinated to political, religious, and social relations. However, the classical economists of the nineteenth century attempted to create a disembedded and fully self-regulating market economy that subordinated society to the market. This disembedded market economy led to the destruction of society. Therefore, human society since the nineteenth century has witnessed a double movement—the expansion of the market triggered the protective countermovement to protect human beings, nature and productive organizations; the protective legislation and other interventions are the characteristics of this countermovement.<sup>4</sup>

### From a Moral Economy to a Market Society

Polanyi’s analytical framework is helpful in understanding the great transformation China has experienced in the past decades. The Chinese economy in traditional society was a moral economy. As Liang Shuming, a philosopher and reformer of the 1930s, observed,

In a moral society, the property of husband and wife, father and son was indivisible. If parents were still alive, the property of sons was indivisible. If grandparents were still alive, then the property of three generations was indivisible. Since property was supposed to be shared, the division of property was regarded as unreasonable (in ancient times the division of property was sometimes even forbidden). However, the relations among family members were not all the same, with some being closer than others, and separate living indeed made life easier. Therefore, property could not always be shared. Then the new moral value of property division appeared among brothers and close relatives. Property was first divided among them when they chose to live separately. Then there might be further redistribution from rich relatives to poor ones. Among relatives, friends, and neighbors, property could be redistributed. Those who benefited from redistribution were supposed to repay, but it all depended on circumstances. It was ~~was~~ common to give property

3. Polanyi, *The Great Transformation*, 3.

4. Polanyi, *The Great Transformation*, 136.



away to those who were in great need. Under certain situations, giving property as charity was actually an obligation, and it was one of the most general moral values. In short, people were expected to care for one another economically. Failure to meet this obligation was viewed as immoral. Additionally, ritual land, charity houses, and charity schools were all properties shared by the clans. The community grain storehouse, charity grain storehouse, and school land were all prosperities shared by the same village community. All these prosperities were used for helping the poor and subsidizing education. This institutional arrangement originated from the moral value of obligation and was very similar to collective living.<sup>5</sup>

In short, economic relations were subject to kinship relations and ethical norms. The old saying “giving property away to others is more important than keeping it to yourself” refers to this kind of ethical relation.

After the establishment of the People’s Republic of China in 1949, social values radically changed. Collective and national interests replaced familial relations as the most important of social values. Nevertheless, although the connotation of ethics changed, the subordination of economic relations to social ethics remained the same. While the new regime did pursue economic development, efficiency and economic growth were taken only as secondary concerns, and the market did not play a great role in the overall arrangement of the economic system. Under the planned (moral) economy, two mechanisms—“soft budget constraint” and “iron bowl” (*tie fanwan*)—helped embed economic relations into social and political relations. “Soft budget constraint” means that the activities of an economic organization (either a corporation or a low-level government) are not constrained by its own resources. When revenue does not meet expenses, and a deficit ensues, the corporation or low-level government can expect help from an outside organization (for example, an upper-level government). The principle of “survival of the fittest” does not apply to this system. “Iron bowl” means lifelong guaranteed employment, no matter how one performs on the job. “Soft budget constraint” and “iron bowl” obviously are not conducive to competition and maximum efficiency, but they became the two pillars of the planned economic system because it gave priority to human subsistence and equality at the expense of efficiency.

Under the planned (moral) economy, communes (*she*) and brigades (*dui*) in rural areas and units (*danwei*) in cities were not only economic

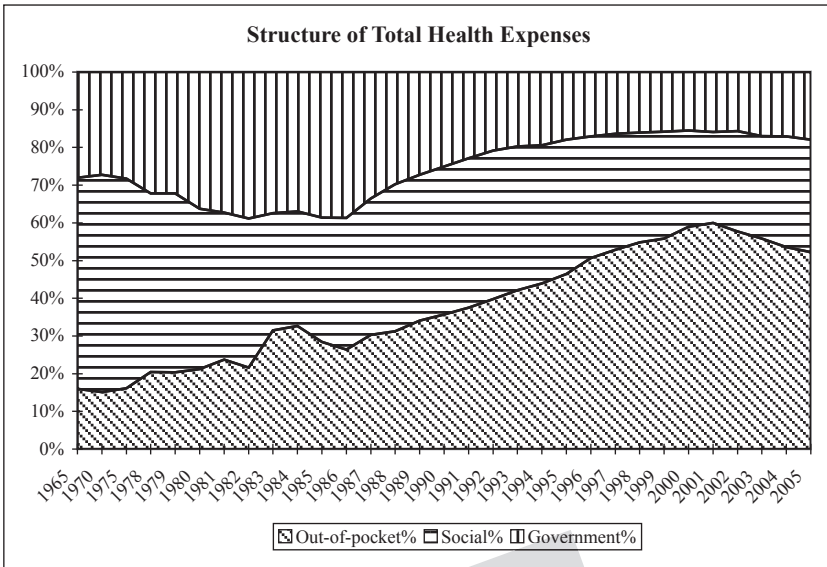
5. Liang Shuming, *Zhongguo wenhua yao yi* [The key principles of Chinese culture] (Shanghai: Shanghai People’s Press, 2005), chap. 5.

institutions but were also social and political institutions. They provided not only job opportunities and salaries (or work points) to their members but also social welfare services (daycare, kindergarten, school, medical care, assistance, old-aged insurance, burial and funeral services) to them and their family members. In other words, the communes and brigades in rural areas and units in cities, rather than the government, provided welfare for individuals. There was no need for the state to provide for these social policies directly. This situation continued until the early phase of economic reform in the 1980s.

After the Chinese government launched its economic reform, their guiding ideology changed. Policy makers abandoned the search for basic welfare and equality, and focused on “development as priority” (*fazhan shi ying daoli*), exclusively pursuing economic growth. Although policy makers insisted that “efficiency was first but fairness needs to be considered” (*xiaolu youxian, jiangou gongping*), they actually deemed fairness less important. In order to achieve maximum efficiency and rapid overall economic development, they deferred all other concerns, such as equality, employment, employees’ rights and interests, health care, the environment, and national defense. At that time, the leaders at all levels accepted the theory of the “trickle-down effect” advocated by neoliberal economists, who suggested that if the “pie” continued to grow, all other problems would eventually be solved.

Along with the changing ideology, the Chinese moral economy was transformed into a market society in three stages. In the first stage (1979–1984), the sporadic market of consumer goods emerged, which played a very limited role in the whole economy. Interference from the government was still strong, and the nonmarket system and relationship still took precedence. In the second stage (1985–1992), a set of interconnected market systems, such as the commodity market, labor market, capital market, foreign currency market, and land market, emerged. In this stage, market principles, such as equivalent exchange, the law of supply and demand, and competition, started to play a role in the economy, but those principles did not yet influence noneconomic fields. In the third stage (1993–1999), the market society emerged as the dominating factor. Market principles also influenced noneconomic arenas and threatened to become the dominant mechanism integrating all of society (and even political life).

This three-stage transformation ruined the foundation of the moral economy. The financial relationship between the governments at different levels changed from “everyone eating from the same big pot” (*chi da*



**Figure 1.** State Retreat from Healthcare

*guofan*) to “everyone eating in separate kitchens” (*fen-zhao chifan*). The relationship between governmental finance and state-owned enterprises changed from “soft budget constraint” to “hard budget constraint.” In rural areas, peasants were granted the freedom of production. With the disintegration of the commune system and the introduction of the “all-around responsibility system” (*da baogan*), villages no longer took responsibility for individuals. In cities, the reform of the employment system smashed the “iron bowl” of urban workers. Because rural communities and urban units were deprived of social functions and turned into purely economic institutions, farmers and workers were forced to get by with reduced entitlement to assistance and security. Consequently, the welfare of individuals came to depend almost entirely on the cash nexus.

The magnitude of the market’s reach can be measured by the extent of commodification, or by the range of goods subject to commercial traffic. Figure 1 shows how the health care field was commercialized step by step. Before economic reform, individual payments accounted for less than 20 percent of total health expenses, while the government’s fiscal allocation and social insurance accounted for more than 80 percent. Therefore, at that time, although people had difficulty finding a good doctor, they did not have any problem in paying for their medical bills.



In the early phase of economic reform, social expenses (the portion of health expenses covered by social insurance) dropped slowly. However, the government's allocation was still increasing and reached nearly 40 percent. The turning point was in the mid-1980s, when both the government's allocation and social expenses dropped dramatically and almost reached the nadir at the beginning of the new century. By 2001, the government's allocation toward total health expenses had decreased to 15.9 percent; the portion of social insurance had decreased to 24.1 percent. Their combined share was barely 40 percent. As a result, people had to pay more of their own health care expenses. In 1980, Chinese people paid for 21 percent of their health expenses, but from 2000 to 2002, they were responsible for paying nearly 60 percent. By that time, China's health care system had become a system funded mainly by private sources, while the public sources filled in the blanks only here and there. This transformation fundamentally shifted the responsibility for health care from the government/society to the individual. At the turn of the century, generally speaking, in developed countries, out-of-pocket expenses account for 27 percent of total health care expenses; in transitional countries (*zhuanxing guojia*), 30 percent; in least developed countries, 40.7 percent, and in other developing countries, 42.8 percent. Thus, compared to other countries, China's health care system has become probably one of the most commercialized in the world.<sup>6</sup> The problem is that the market serves only the consumers who can pay the bill. This is why many rural and urban residents complain that it is too expensive to see a doctor (*kanbinggui*).

Health care is not the only noneconomic field which has been invaded by market forces. Other noneconomic fields, such as education, were also influenced by market forces. Following Polanyi, as the economy has been disembedded from society and become a controlling force, China has been effectively transformed into a market society. From a historical perspective, China has experienced an unprecedented transformation from a moral economy to a market society.

### **The Emergence of the Protective Countermovement**

Polanyi argues that a disembedding and self-adjusting market is destructive. When the market attempts to turn human beings and the natural environment into pure commodities, it will inevitably destroy society and

6. Wang Shaoguang, "China's Health System: From Crisis to Opportunity," *Yale-China Health Journal* 3 (Autumn 2004): 5–49.

the natural environment. Although the Chinese economy experienced a high rate of growth in the past quarter century, the pursuit of a high GDP growth rate brought with it many serious problems. These problems were not obvious in the early years of reform, but they became more noticeable as time went on. By the end of the 1990s, some of these problems had become very obvious, including the deteriorating environment and the increasing social polarization between rich and poor (e.g., regional disparities, urban/rural divide, inequality within urban China, and inequality within the countryside). People started to realize that economic growth did not necessarily mean social progress. More importantly, within a market society, the quality of people's lives depended almost entirely on the market, which served only those who were able to pay. Therefore, social protections and relief ordinary people like peasants and workers could take advantage of declined. Layoffs on a large scale, difficulties in getting into school or seeing a doctor, and numerous serious workplace accidents threatened the economic and social security of millions of people. From their perspective, the market society was making unbearable demands on ordinary people.

In this situation, the golden tablet (*jinzi zhaopan*) of market reform toppled, shattering the seeming consensus on the efficacy of market forces. Those who got hurt in the early stages of economic reform, or who barely benefited from it, stopped showing unconditional support for market-oriented reform and began to question any reform with the label "market" attached to it. They were hostile to corrupt officials, who abused their power and embezzled government funds; they were hostile to the nouveau riche, who made their fortune overnight; they disdained the arrogant scholars whose success came about as a result of reform. They felt that Chinese economic reform had gone astray, and they longed for harmony between the economy and society. This initiated the protective countermovement to re-embed the economy into the society.

As more things went wrong, policy makers started to seriously consider Deng Xiaoping's warning, "If there is polarization (between rich and poor) . . . then disparity between nationalities, regions, classes, and central and local government will grow, then things will go wrong."<sup>7</sup> "The purpose of socialism is to make all people rich instead of [creating] polarization. If our policy leads to polarization, we will fail."<sup>8</sup> In order to reduce social disparity,

7. Zhonggong zhongyang wenxian yanjiushi [Party Literature Research Center of the CPC Central Committee], ed., *Deng Xiaoping sixiang nianpu* [The chronicle of Deng Xiaoping's thoughts] (Beijing: Central Document Press, 1998), 453.

8. *Deng Xiaoping sixiang nianpu*, 311.

the Chinese government began to focus on security and equality. If, in the past, they paid only lip service to “fairness” (*jiangu*), they were now making a concerted effort to re-embed the economy within social relations through deccommercialization. Deccommercialization means treating the human subsistence-related services (such as health care, education, retirement, etc.) as basic human rights rather than as commercial commodities. The purpose of deccommercialization is to allow people to maintain “a livelihood without reliance on the market.”<sup>9</sup> When a planned economy and collective system disintegrates, a redistribution system must be established to achieve deccommercialization. On the one hand, people have to pay taxes according to their income levels; on the other hand, people receive benefits from the state redistribution (social assistance, social insurance, and public service) according to their needs. There is no relation between the taxes an individual pays and the benefit he or she receives. By using state power, the redistribution breaks the market chain and reconnects everyone. These are the changes China has been experiencing recently.

From 1978 to the mid-1990s, then, China had only economic policies and no social policies. Starting from around the turn of the century, social policies began to emerge in the country. Table 1 shows various social policies introduced in recent years. Before the new century, only the Go West policy (*xibu dakafa*) in 1999 could be considered a social policy. Most social policies were introduced after Hu Jintao and Wen Jiabao took office in 2002. In the next two sections, I will explain how these policies were carried out and how they brought dramatic changes to China. To simplify my analysis, I will divide these social policies into two large categories: those that aim to reduce inequality; and those that provide social security.

### Reducing Inequality

There are different kinds of income disparities: intra-urban/intra-rural disparity, urban/rural disparity, and regional disparity. Research shows that most serious income disparities in China are regional and urban/rural.<sup>10</sup>

9. Gøsta Esping-Andersen, *The Three Worlds of Welfare Capitalism* (Princeton, N.J.: Princeton University Press, 1990), 21–22.

10. Li Shi and Zhao Renwei, “Zhongguo jumin shouru fenpei zai yanjiu” [The reexamination of income distribution of Chinese residents], available at [http://www.usc.cuhk.edu.hk/wk\\_wzdetails.asp?id=597](http://www.usc.cuhk.edu.hk/wk_wzdetails.asp?id=597); Development Bureau of the UN, *Zhongguo renlei fazhan baogao 2005: zhuiqiu gongping de renlei fazhan* [The human development report of 2005: Pursuing the equal development of the human being], available at [http://ch.undp.org.cn/downloads/nhdr2005/c\\_NHDR2005\\_complete.pdf](http://ch.undp.org.cn/downloads/nhdr2005/c_NHDR2005_complete.pdf).



**Table 1.** New Social Policies, 1999–2007

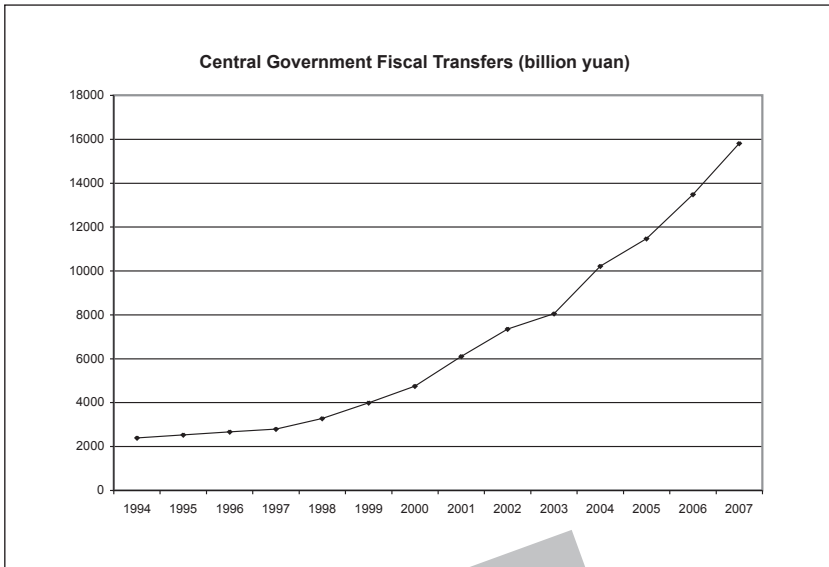
YEAR	NEW SOCIAL POLICIES
1999	Go-West policy
2002	Urban minimum income guarantee program
2003	Rural fee–tax reform; reestablishment of rural Cooperative Medical Systems (CMS)
2004	Reduction in agricultural taxes; introduction of 3 types of rural subsidies
2005	Partial abolishment of agricultural taxes
2006	Abolishment of all agricultural taxes; introduction of comprehensive rural subsidies, free compulsory education in western and central rural areas, public housing for urban poor
2007	Free compulsory education in all rural areas; basic health insurance for all urban residents; CMS for over 80 percent of rural population; promotion of rural minimum income guarantee program, pensions for migrant workers, public housing for urban poor

To reduce overall income disparity, China must first deal with regional and urban/rural disparity.

#### *Reducing Regional Disparity*

The most important measure taken to reduce regional income disparity was to increase the central government's "fiscal transfer" (*caizheng zhuanyi zhifu*) to the provinces, especially to the least economically developed provinces in central and western China. Before 1993, China's fiscal system was one of "eating in separate kitchens." This system was beneficial to the developed coastal provinces because they had more fiscal resources and did not have to share tax revenue with other provinces. The provinces in central and western China whose fiscal resources were limited could not, without the outside fiscal transfer, provide similar public services to their people, not to mention invest in new infrastructure or new industries. After the mid-1980s, regional disparity continued to expand; one of the main reasons was excessive fiscal decentralization.<sup>11</sup>

11. Wang Shaoguang and Hu Angang, *Zhongguo: bupingheng fazhan de zhengzhi jingjixue* [China: The political economy of unequal development] (Beijing: China Plan Press, 1999).



**Figure 2.** Fiscal Transfers from the National to Local Governments

In 1994, the Chinese government overhauled its fiscal system. This major reform eventually stopped “two ratios” from further decreasing after fifteen years of continuous decline.<sup>12</sup> More importantly, the reform enhanced the central government’s ability to extract fiscal resources and thus established a foundation for increasing fiscal transfers.

Figure 2 clearly shows that since 1994, the total amount of the central government’s fiscal transfer has increased steadily. Especially after 1999, the amount increased every year, and reached 1600 billion yuan in 2007, which was eight times the amount transferred in 1994. The turning point appeared in 1999, when the Chinese central government introduced its Go West policy.

According to statistics provided by the Ministry of Finance, during the period of 1994–2005, 10 percent of the central government’s fiscal transfers went to eastern provinces, 44 percent went to central provinces, and 46 percent went to western provinces.<sup>13</sup> Central government fiscal transfers have

12. “Two ratios” means the ratio of government revenue to the GDP, and the ratio of central government revenue to total government revenue.

13. Jin Renqing, “Wanshan cujin jiben gonggong fuwu jundenghua de gonggong caizheng zhidu” [Enhance and improve the public finance system in equalizing the basic public service], available at <http://www.zgdjyj.com/Default.aspx?tabid=99&ArticleId=721>.

helped reduce both vertical and horizontal fiscal imbalance and thereby regional inequalities. Before the 1994 fiscal reform, the GDP growth rates in the eastern, central, western, and northeastern areas were very different, ranging from 12 percent to 19.5 percent. After 1994, growth rates began to converge. In 2005, growth rates in the eastern, central, western, and northeastern areas were 13.13 percent, 12.54 percent, 12.81 percent and 12.01 percent, respectively. The differences in growth rate became quite small.<sup>14</sup>

The convergence of economic growth rates in different regions has been helpful in preventing regional disparity from growing, and may even reduce it. For some time after 1983, the Gini coefficient of provincial per capita GDP continued to increase. In the 1990s, the regional difference quickly expanded, but it leveled off after 2000. In 2004, the expansion tendency was reversed for the first time since 1990. By 2005, regional disparity was further reduced. The Fiscal Transfer System was seen as a miracle, one that brought about effective changes within a short period of time.<sup>15</sup>

#### *Reducing Urban/Rural Disparity*

In comparison with other developing countries, China's national income disparity is not the highest in the world. It is lower than that of some countries in Latin America and Africa in terms of the overall Gini coefficient. Still, the urban/rural divide in China is among the greatest in the world and is a telling characteristic of China's income distribution.<sup>16</sup>

In order to reduce urban/rural income disparity, the Chinese government in recent years has adopted a two-prong strategy: "taking less" from rural areas (*shaoku*), on the one hand, and "giving more" to rural areas (*duoyu*) on the other. One way of taking less was to abolish agricultural taxes. The agricultural tax was one of the oldest taxes in China, going back thousands of years. After economic reform, the share of agriculture in the national economy decreased consistently, from 31 percent in 1979 to 12.6 percent in 2005. However, from 1986 to 1996, various agricultural taxes (including the agricultural tax, the tax on special farm produce, the

14. Feng Jie and Xuan Xiaowei, "Woguo quyue zengzhang geju he diqu chaju de bianhua yu yuanyin fenxi" [An analysis on the current situation and causes of unbalanced regional development in China], Working Paper No. 138 (2006), Development Research Center of the State Council, PRC.

15. Feng Jie and Xuan Xiaowei, "Woguo quyue zengzhang geju he diqu chaju de bianhua yu yuanyin fenxi."

16. Development Bureau of the UN, *Zhongguo renlei fazhan baogao 2005: zhuiqiu gongping de renlei fazhan*.

husbandry tax, the land occupancy tax, and the deed tax) increased proportionally the overall fiscal revenue, from 2.1 percent to 5.2 percent. After 1996, agricultural taxes were comprising less of the national fiscal revenue. But in 2005, these taxes still amounted to 93.64 billion yuan and were still proportionally higher than the level in 1985.

In the Second Session of the 10th National People's Congress in 2004, Premier Wen Jiabao announced that the government would "eliminate the tax on special agricultural produce, except tobacco crops, and eliminate the agricultural tax entirely within five years." That year, eight provinces were exempted altogether from the agricultural taxes; twelve provinces had their agricultural taxes reduced by 3 percent, and eleven provinces had theirs reduced by 1 percent. By 2005, most provinces had their agricultural taxes cut or eliminated. By 2006, the agricultural taxes were eliminated entirely, a goal that the central government did not actually expect to meet until 2008. Approximately 900 million peasants in China were exempted from around 100 billion yuan in agricultural taxes, or about 100 yuan per person.<sup>17</sup>

In the mid-1980s, peasants in rural areas were also subject to arbitrary quotas, surcharges, and fines, in addition to the formal agricultural taxes. Since the early 1990s, the central government issued several documents requiring such illegal levies on peasants to be limited to less than 5 percent of their total income, but this provision did not do much to relieve the peasants' burden. In many places, especially in the rural areas in central China, the situation went from bad to worse. The central government had to bear the blame, because when it assigned new responsibilities to local governments (e.g., the Nine-Year Compulsory Education), the latter had to pay the bill, a classic "unfunded mandate." Local governments often found they had no choice but to impose new surcharges. In 2000, Anhui Province began to experiment with the Fee-to-Tax Reform (*feigaishui*), which eliminated illegal levies and converted all legal surcharges into formal agricultural taxes. At the beginning of the experiment, the central government showed no intention of using fiscal transfers to support the experimental province; rather, it hoped that the local government could resolve its revenue shortage problem on its own. However, the ensuing fiscal shortage in the experimental province soon disrupted the normal operation of rural organizations and of rural compulsory education. The central government

17. Su Ming, "Jinnan zhongyang canzheng zhinong xinzhengce" [This year's new central finance policies of supporting peasants], available at <http://www.cribs.org.cn>, March 31, 2006.

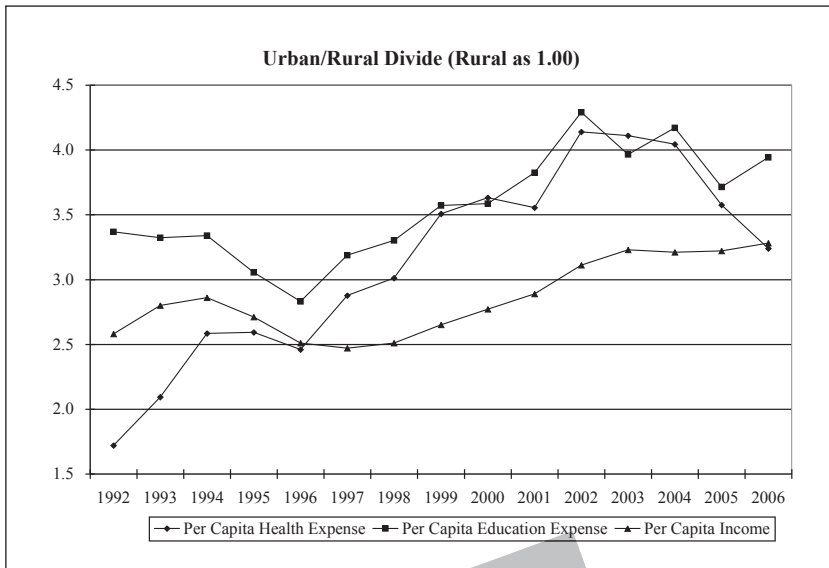
finally acknowledged the problem, and, in 2002, the State Council extended the rural tax reform to sixteen provinces. As a supplementary measure, the Ministry of Finance introduced the Central Fiscal Transfer Payment for Supporting Rural Tax Reform and transferred 24.5 billion yuan to the experimental provinces. In 2003, when rural tax reform was fully launched all over the country, the central government further increased the amount of fiscal transfer to support rural tax reform. This move greatly relieved the peasants' burden. In 2006, the special transfer amounted to 80 billion yuan, about 100 yuan per rural resident.

The central government's strategy of "giving more" has been even more pronounced. In 1997, it invested merely 70 billion yuan in the Three Rural Issues (*sannong*) fund, which included an agricultural subsidiary, an expenditure for elementary and secondary schools in rural areas, and an expenditure for rural health care, and twelve other main categories. In 2001, the Three Rural Issues fund surged to 190 billion yuan. Over the next two years, the amount did not increase, but in 2004, the central government invested 262.6 billion yuan in the fund, which was 70 billion more than what it had invested in 2003. After that, the annual increase was around 50 billion yuan. In 2007, the Ministry of Finance's budget for the Three Rural Issues fund was 391.7 billion yuan, which was more than five times the amount invested in 1997.

As Figure 3 shows, the per capita urban/rural income disparity has somewhat stabilized after a sharp increase in the mid-1990s as a result of the take less/give more strategy. The disparity in the per capita expense in health care and education has begun to drop. When, as the central government pledges, public revenue takes over the responsibility for education and basic health care in the coming years, it expects the urban and rural disparity to be further controlled and even reduced.

### **Increasing Social Security**

In modern society, people support themselves with their income. However, some people cannot work due to advanced age or illness or physical disability. Some people have jobs but do not earn enough to support themselves and their families (because they have too many children or have lost a spouse). Some people get injured on the job and lose their ability to work. Some people want to work but cannot find a job. Some families have limited living space, which hinders normal family life. Modern



**Figure 3.** Urban/Rural Divide Ratio

society is full of risks, and everyone is vulnerable to misfortune. Although family and nonprofit organizations can help to offset hardships, they cannot completely protect people from all risks.<sup>18</sup>

Before economic reform, rural communes and urban units provided help to people. After the collapse of communes and units, the society was supposed to take responsibility and provide basic economic protection for people. However, in the 1980s and 1990s, the Chinese government ignored its responsibility.<sup>19</sup> This situation has been reversed in recent years. The charts in the following subsections show new developments in the minimum income security system, and in health care, old-aged, work-related injury, and unemployment insurance.

18. Wang Shaoguang, "Xindan guojia zhidu zhong de zaifenpei jizhi" [The redistribution mechanism in the modern state system], in *Dierci zhuanxin: guojia zhidu jianshe* [The second transformation: The construction of the state system], ed. Hu Angang, Wang Shaoguang, and Zhou Jianming (Beijing: Tsinghua University Press, 2003), 275–311.

19. According to an evaluation of economic security conducted by the International Labor Organization in 2004, China was among the lowest of four levels. See International Labor Organization, *Economic Security for a Better World* (Geneva: International Labor Office, 2004).

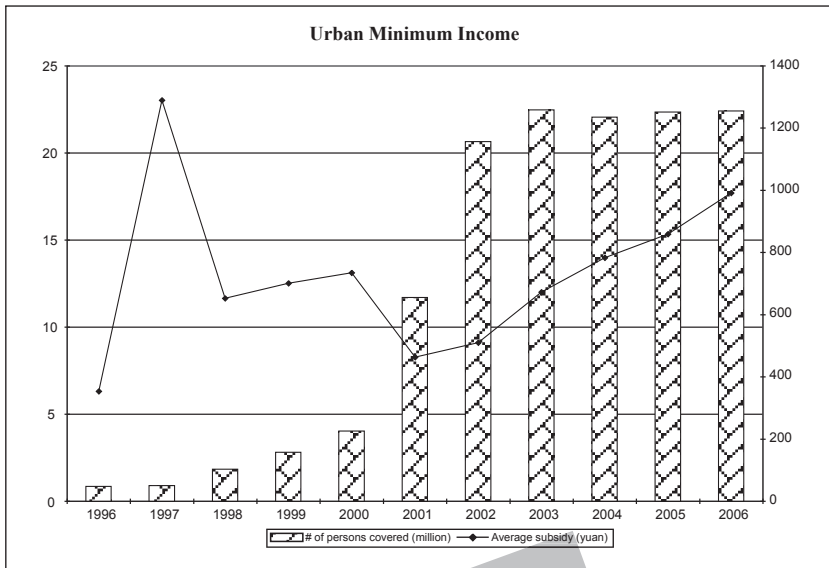
### *Minimum Income Security*

The Chinese government has recently been paying more attention to economic security, which can be seen from its policy on minimum income security. The problem of urban poverty did not draw much attention until the late 1990s, before which most people thought poverty a rural phenomenon. However, as unemployment became rampant in the mid-1990s, people realized that urban areas could suffer from serious poverty as well.

In 1993, the city of Shanghai established the first urban minimum income security system. In 1997, at the same time that the central government introduced the policy of Downsizing Staff and Improving Efficiency, Laying-off Workers, and Repositioning Personnel (*jianyuan zengxiao, xiagang fenliu*), the State Council published the Notice of Launching the Program of Minimum Income Security for the Urban Population (*guanyu zai quanguo jianli chengshi jumin zuidi shenghuo baozhang zhidu de tongzhi*) and began to practice the minimum income security system in urban China. However, the program was not carried out effectively until the second half of 2001, when the central government required this program to cover more poor workers in mid- and large-sized state-owned enterprises. As a result, the number of people covered doubled within six months, reaching 11.7 million at the end of 2001. In the next year, the central government mobilized thousands of people who were working in the national civil affairs system to search for urban poor people and tried its best to “cover everyone who needed to be covered” (*yingbao jinbao*). All local governments acted quickly, and the number of people covered steadily increased every month. At the end of 2002, the total number of people covered increased to 20.54 million. In the following years, coverage fluctuated to around 22 million people (Figure 4). Today, almost all eligible urban poor people are covered by the minimum income security system.

In the first several years, coverage expansion happened much faster than fiscal allocation. For several years, as the number of people covered grew, the average subsidy actually declined. After Hu Jintao and Wen Jiabao took their positions, the government, at all levels, increased its fiscal support for the minimum income security system. After 2001, the average minimum income subsidiary increased every year and reached 1000 yuan in 2006, which was more than double the 2001 level (Figure 4).

Although urban poverty is a big problem, rural poverty is even more acute. By the end of 2006, the rural population living in extreme poverty (annual income under 683 yuan) numbered 21.48 million, and the population living in poverty (annual income under 882 yuan) was 85.17 mil-



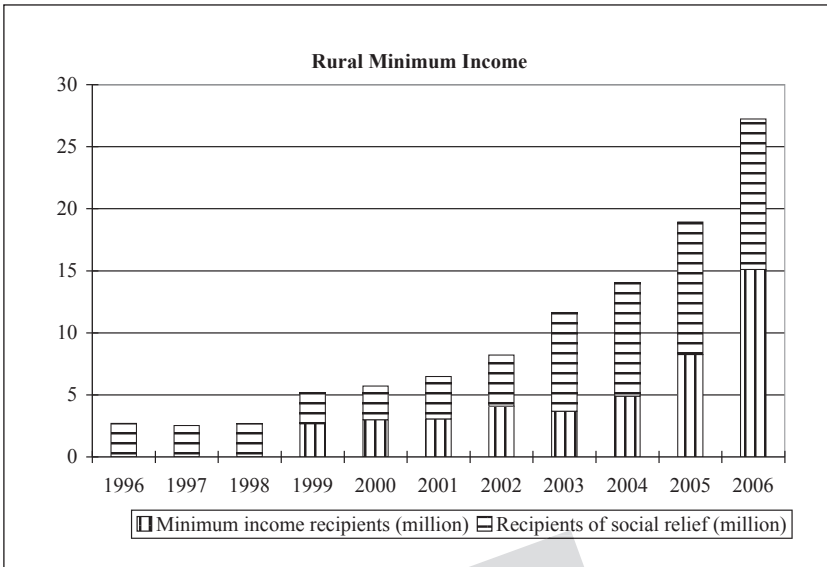
**Figure 4.** Urban Minimum Income Program

lion. If the UN standard (US\$1 per day) were to be adopted, there would be perhaps more than 100 million people in Chinese rural areas living in poverty.<sup>20</sup>

Since 1997, some fiscally sound provinces have established the rural minimum income security system. Some economically developed provinces, such as Guangdong and Zhejiang, issued the Measures on Rural Minimum Income Security (*nongcun zuidi shenghuo baozhang banfa*), which provided peasants with social security by law. Before the Fee-to-Tax Reform, in most rural areas, the relief funds came from “the village’s collective undertakings and the township’s public undertakings” (*cun tiliu he xiang tongchou*). Therefore, at that time, it was impossible to establish a normative minimum income security system in rural areas. Only after rural tax reform made certain progress could the minimum income security system be supported with local public money. The success of rural tax reform led to the central government issuing the No. 1 Central Document (*zhongyang yihao wenjian*) in 2004, which required local governments with

20. Wang Lifang, “Woguo gaige kaifang yilai nongcun pingkun renkou shuliang jianshao 2.28 yi” [The number of rural residents living in poverty is reduced to 228 million since 1978], *Xinhua News Net*, May 26, 2007, available at [http://news3.xinhuanet.com/fortune/2007-05/26/content\\_6156519.htm](http://news3.xinhuanet.com/fortune/2007-05/26/content_6156519.htm).





**Figure 5.** Rural Minimum Income Program (Per Million Persons)

the financial capacity to experiment with the rural minimum income security system. Consequently, at the end of 2005, fourteen provinces established the rural minimum income security system. At the end of 2006, the number of experimental provinces increased to twenty-two. Overall, 15 million peasants in China were covered by this system. Additionally, more than 12 million peasants were eligible for social relief in China and received a regular allowance. The total number of these two groups was 27.23 million, which was slightly higher than the population who lived under the subsistence level, but did not include all low-income people (Figure 5).

In 2007, the Central Party Committee and the State Council issued the Views on Promoting the Construction of a New Socialist Countryside (*guanyu jiji fazhan xiandai nongye zhashi tuijin shehuizhuyi xinnongcun jianshe de ruogan yijian*), which encouraged the establishment of the rural minimum income security system throughout the country. Poor peasants who are eligible for this system, especially the elderly, the disabled, and those who cannot work, are all covered and will receive the minimum living allowance by the end of the year.<sup>21</sup> With this initiative, the poorest

21. The local government will be mainly responsible for establishing the rural minimum life security system. The management of this system is locally based. The central government will subsidize any local government that has financial difficulties.

rural people, for the first time, are included in the social security system supported with public money. This is a historic change for rural China.<sup>22</sup> Although the amount of minimum-living allowance is still small, as the state invests more into this system, the rural minimum income security system will gradually improve.

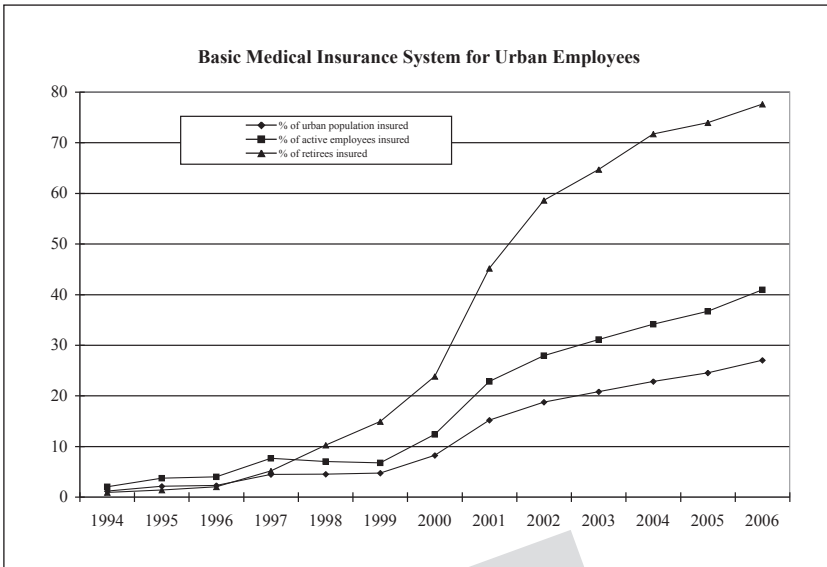
#### *Medical Insurance*

In Mao's period, China placed great emphasis on egalitarian principles. From 1950 through 1979, the government went to great lengths to establish a health care system that could provide all citizens with access to basic health care services at an affordable price. In urban areas, the health care finance system consisted of two schemes: (1) the Government Insurance Scheme (GIS), for all governmental employees (including retirees), disabled veterans, college teachers and students, and employees in non-profit organizations; and (2) the Labor Insurance Scheme (LIS), for employees (including retirees) of all state-owned enterprises (SOE) and some collective enterprises. In rural areas, there was a cooperative medical system serving rural residents. Thus, on the eve of economic reform, even though the quality of medical services was not very high at the time, this health care system provided inexpensive and equally accessible medical care for virtually all urban residents and for 90 percent of rural residents.<sup>23</sup> After economic reform, policy makers turned their attention to health care reform. Consequently, both the GIS and the LIS began to decline in the 1990s. In 1999, the two systems were replaced by the basic medical insurance system for urban employees.<sup>24</sup> The new system developed quickly. Within seven years, the number of employees who joined the system increased several times, from 18 million in 1999 to 157 million in 2006. It is noteworthy that the basic medical insurance system also covered retirees, so those people who tended to have a fragile constitution could also receive benefits from this system. By the end of 2006, more than three-quarters of retirees

22. In November 2006, the average monthly subsidy of the minimum income security was 79.5 yuan in cities and 22.3 yuan in the countryside.

23. World Bank, *Financing Health Care: Issues and Options for China* (Washington, D.C.: The World Bank, 1997).

24. It is important to point out that the transition to the new system is not yet complete. Therefore, the free medical care system and labor protection medical care system are still effective in some places and at some state-run enterprises. In addition, the government also provides medical care to special groups, including disabled veterans and the urban poor population, who meet the criteria for needing social assistance.



**Figure 6.** The Basic Medical Insurance System for Urban Employees

were covered under the basic medical insurance system. The proportion of those covered was much higher among retirees than among younger, active employees (Figure 6).

The new system was different from the free GIS and LIS in that it did not cover family members of employees. It also did not cover the self-employed, employees in the informal sectors (that is, economic activities that are neither taxed nor monitored by the government, as opposed to the formal sector), or migrant workers. The new system developed very fast, but it covered only one-fourth of urban employees by 2006 (Figure 6). This rate of coverage would be even smaller if migrant workers were included in these statistics.

In recent years, some cities have experimented with providing medical care to urban nonemployees. As a result, an additional 10 million people in one hundred cities in China joined the medical care insurance system. In order to cover as many urban residents as possible, in April 2006 the State Council decided to choose one or two cities in provinces that had the financial capacity to introduce an urban medical care program for protecting against catastrophic illness. This system covered those people who were not eligible for the basic medical insurance system for urban employees, such as children and nonemployees. The State Council will expand this

experiment to more cities in 2008 and reach 80 percent of cities in China by 2009. By 2010, this medical insurance system will be established in all cities in China.<sup>25</sup>

Medical insurance for migrant workers is more complicated, because migrant workers are young, mobile, and unwilling to pay for insurance. Moreover, their employers are not willing to pay for medical insurance for them. Early in September 2002, the city of Shanghai issued the Temporary Methods of Comprehensive Insurance for Migrant Labors in Shanghai (*Shanghaishi wailai congye renyuan zonghe shehui baoxian zhanying banfa*) to establish the comprehensive social insurance system exclusively for migrant workers. In March 2003, the city of Chengdu issued the Temporary Methods of Comprehensive Insurance for Nonurban Resident Workers in Chengdu (*Chengdushi feichengzhen huji congye renyuan zonghe shehui baoxian zhanxing banfa*), a system designed to provide comprehensive social insurance to nonurban resident workers (migrant workers from rural areas). The Ministry of Labor and Social Security in 2003 and 2004 issued the Guiding Opinions on Participation in Basic Medical Insurance by Nonpermanent Employees in Cities and Towns (*guanyu chengzhen linhuo jiuye renyuan canjia jiben yiliao baoxian de zhidao yijian*) and the Opinion on Employees of Organizations of Mixed Ownership and Non-state-owned Enterprises to Participate in Medical Insurance (*guanyu duijin hunhe suoyouzhi qiye he feigongyouzhi jingji zuzhi congye renyuan canjia yiliao baoxian de yijian*), respectively, which required local offices of labor and security to cover all migrant workers from rural areas who have already formed stable working relationships with employers in cities and towns. For those migrant workers who are self-employed in urban areas, the opinion required them to join the insurance system as nonpermanent employees. In 2004, Beijing and some cities in Shandong Province began to offer different kinds of medical insurance for migrant workers, but progress in the nation as a whole was rather slow. According to statistics from the Ministry of Labor and Social Security, of the 120 million migrant workers in China, only about 12 million, or 10 percent of migrant workers, participated in the medical insurance system.

In March 2006, the State Council issued the Views on Resolving

25. Meng Xiang, "Disanzhangwang: quanguo chengzhen jumin yibao shidian jijiang qitong" [The third net: The experiment on the nationwide medical insurance of urban residents will be launched], *Ershiyi shiji jingji baodao* [The economic report of the twenty-first century], July 1, 2007, available at <http://finance.sina.com.cn/g/20070701/04443742157.shtml>.

Rural Worker Problems (*guanyu jiejie nongmingong wenti de ruogan yijian*), which emphasized “the importance of resolving the problem of high medical expenses for migrant workers.” After that, the Ministry of Labor and Social Security issued the Opinions of the Implementation (*shishi yijian*). In May, the ministry issued the Notice on Special Expansion of Medical Insurance for Migrant Workers (*guanyu kanzhan nongmingong canjia yiliao baoxian zhuanxiang kuoda xingdong de tongzhi*), which aimed to cover more than 20 million migrant workers under the medical insurance system by the end of 2006, and to cover with basic medical insurance all migrant workers who have established long-term working relations with employers in cities and towns by the end of 2008. This indicated that medical insurance for migrant workers had been put on the agenda of the central government. Consequently, many local governments promptly issued opinions, methods, and measures in an effort to solve the medical insurance problem for migrant workers. By the end of 2006, 23.67 million migrant workers had participated in the medical insurance system, and this number increased to 24.1 million by March 2007.<sup>26</sup>

China was once known for its rural cooperative medical system. However, after the Chinese government launched the System of Contracted Responsibility Linking Remuneration to Output (*lianchan chengbao zeren zhi*) in the late 1970s and early 1980s, farm households replaced rural collectives as the basic productive units in rural areas. Meanwhile, the government took a laissez-faire attitude toward the cooperative medical system. Without support from the collective economy, which had been in a decline, the rural cooperative medical system quickly collapsed. According to research conducted in 1985, two years after the abolishment of the People’s Communes (*renmin gongshe*), the number of villages still practicing cooperative medicine decreased from 90 percent in 1979 to 5 percent then. In 1989, the number decreased further to 4.8 percent.<sup>27</sup> In the early 1990s, the Chinese government promised the World Health Organization that China would improve health care in rural areas,<sup>28</sup> and it called for

26. Bai Tianliang, “Chengzhen jumin yibao shidian jiang quanmian qitong, feicongye jumin ke canjia” [The experiment of urban resident medical insurance will be launched in full scale, non-employee resident will be covered], *Xinhua Net*, April 27, 2007, available at [http://news.xinhuanet.com/health/2007-04/27/content\\_6029436.htm](http://news.xinhuanet.com/health/2007-04/27/content_6029436.htm).

27. Cited from Wang Yanzhong, “Shilun guojia zai nongcun yiliao weisheng baozhang zhong de zuoyong” [My preliminary observations on the state role in rural medical insurance coverage], available at <http://www.cc.org.cn/wencui/020603200/0206032015.htm>.

28. Ministry of Health, “Guyu woguo nongcun shixian 2000 nian renren xiangyou wei-

“resuming and rebuilding” the rural cooperative medical system. The government, however, had no intention at that time of funding the rural medical system. Instead, it insisted that “the premiums [be] paid mainly by individuals themselves, supplemented by collectively pooled subsidies and supported by government policies,” which sounded practical but actually did not benefit the peasants. As a result, after ten years, the rural cooperative medical system still was not restored as expected. The number of people covered was always lower than 10 percent.<sup>29</sup>

In early 2003, the Chinese government changed its approach to the rural cooperative medical system. The State Council forwarded the Notice on Establishing a New Rural Cooperative Medical Service System (*guanyu jianli xinxing nongcun hezuo yiliao zhidu yijian de tongzhi*), issued by the Ministry of Health, the Ministry of Finance, and the Ministry of Agriculture. The notice required provinces, autonomous regions, and municipalities to select at least two or three counties to try this new system, and then to expand the system to cover more rural residents. The goal of the notice was to establish the new cooperative medical system across the country by 2010. The difference between the new system and the previous model lay in the support it received from public funds. Besides the contributions from the beneficiaries, the local governments subsidized those peasants who participated in the new system. The central government also subsidized the peasants in rural areas in central and western China with public funds.<sup>30</sup>

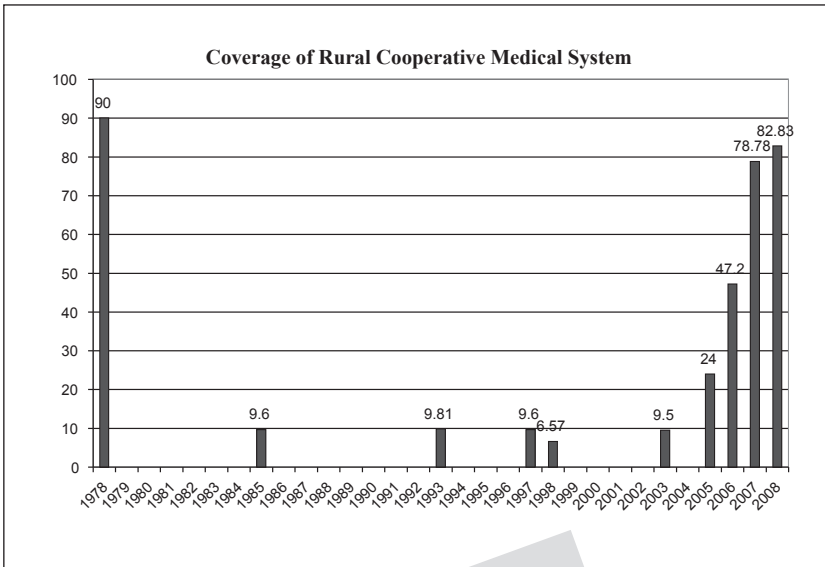
It is very clear from Figure 7 that the addition of public funds greatly helped to promote the development of the new system. In 2003, when the Ministry of Health conducted the Third National Survey on Health Service, the rural cooperative medical system covered only 9.5 percent of the rural population. Four years later, by June 30, 2007, the new system had been

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sheng baojian de guihua mubiao” [The planned goal of medical care coverage for everyone in the countryside in 2000], March 15, 1990, available at <http://www.chinaeh.com/zhengcefagui/yizheng/yizheng3.htm>.

29. Zhang Wenkang, lecture delivered at the Strategic Renovation Forum (*zhuangxin zhanliu luntan*), China Science Academy (*zhongguo kexueyuan*), January 31, 2002, <http://www.cas.ac.cn/html/Dir/2002/01/31/5616.htm>.

30. In 2003, the central government and local government each allocated 10 yuan per person to subsidize the peasants who participated in the new rural cooperative medical care program. Ban Jianfeng, “Woguo tuixing xinxing nongcun hezuo yiliao zhidu” [Our country is launching the new rural cooperative medical care system], *Renmin ribao* [People’s daily], column 11, January 24, 2003, available at <http://www.people.com.cn/GB/shizheng/3586/20030124/913612.html>.



**Figure 7.** Rural Cooperative Medical System Coverage

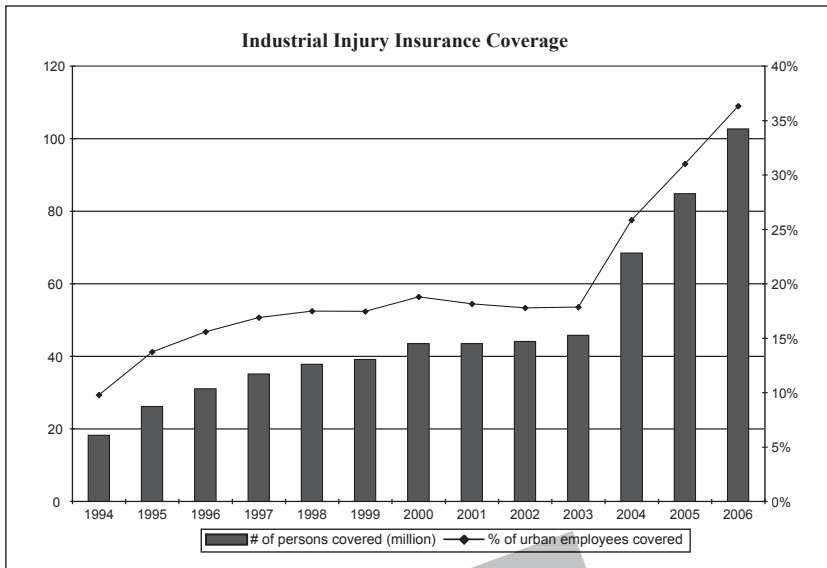
carried out in 2,429 counties, with 720 million participants, which accounts for 82.83 percent of the rural residents in China.<sup>31</sup>

On March 21, 2007, the Executive Meetings of the State Council discussed and passed the Outline of the 11th Five-Year (2006–2010) Plan for Health Development (*weisheng shiyi fazhan “shiyiwu” guihua gangyao*), which required an overhaul of China’s medical care system to provide basic health care to all urban and rural residents by 2006–2010. With an emphasis on building four medical care schemes (e.g., Basic Medical Insurance System for Urban Employees, Basic Medical Insurance System for Urban Residents, Basic Medical Insurance System for Migrant Workers, and New Rural Cooperative Medical System), China is now working toward its goal of providing public health and basic medical care for everyone.

#### *Insurance for Work-Related Injury*

An employee who suffers a work-related injury, illness, or disability, or death, is entitled to receive economic and material compensation. The

31. Chen Weisong, “Zhongguo 7.2 yi ren canjia hezuo yiliao” [Our country has 720 million peasants who have participated in the new rural cooperative medical insurance program], September 5, 2007, [http://www.china.com.cn/news/2007-09/05/content\\_8805092.htm](http://www.china.com.cn/news/2007-09/05/content_8805092.htm).



**Figure 8.** Industrial Injury Insurance Coverage

guiding principle of work-related injury insurance is one of “no-fault compensation” (*wugongchang bushi*). Article 73 of the Labor Law of the People’s Republic of China, revealed in 1995, states that “an employee who suffers injuries or occupational diseases on the job is eligible for the social insurance.” To implement the Labor Law, the Ministry of Labor and Social Security issued the Trial Procedures for Industrial Injury Insurance for Enterprise Employees (*qiye zhigong gongshang baoxian shixing banfa*) in 1996, which stated that the industrial injury insurance system applied equally to all employees in all industrial enterprises in China including private economic organizations. Over the next seven years, the industrial injury insurance system did not make much progress, but the situation changed in 2004, when the State Council announced the Regulations on Industrial Injury Insurance (*gongshang baoxian tiaoli*). Consequently, more than 15 million additional employees joined the insurance program each year over the next three years. The number more than doubled within three years, growing from 45.75 million in 2003 to 102.68 million in 2006 (Figure 8).

Figure 8 shows that, although the industrial injury insurance system developed quickly, only one-third of urban employees were covered by the program, mainly because it was difficult to include migrant workers in the system. By the end of 2005, only 12.52 million migrant workers participated



in the industrial injury insurance system.<sup>32</sup> In May 2006, the Ministry of Labor and Social Security issued the Three-Year Program on Encouraging Migrant Workers to Participate in the Industrial Injury Insurance System (*tuijin nongmingong canjia gongshang baoxian sannian xingtong jihua*), also known as the Wellness Program (*ping'an jihua*). The goal was to cover all migrants working in highly dangerous industries (e.g., the coal mining and the construction industries) over the next three years. By the end of 2006, all migrant workers in medium- and large-sized state-owned coal mines were expected to participate in the insurance program; by the end of 2007, more than half of the migrant workers working in small coal mines, noncoal mines, and the construction industry were expected to participate; and by the end of 2008, almost all migrant workers in legal coal mines and noncoal mines and most rural workers in the construction industry are expected to participate.

The Wellness Program effectively extended the industrial injury insurance system to migrant workers. By the end of 2006, almost all migrant workers at medium- and large-sized coal mines joined the program in some coal-producing provinces. The total number of covered migrant workers increased to 33 million by the end of August 2007, which almost tripled the number of workers covered in 2005.<sup>33</sup> The Ministry of Labor and Social Security will likely have no problem reaching its planned target for 2007, namely, covering 36 million migrant workers by the end of the year.<sup>34</sup>

#### *Old-Age Insurance*

Before economic reform, the Chinese government provided old-age insurance via work units to the employees of government agencies, public institutions, urban state-owned enterprises, and some collective enterprises. The disintegration of the unit system and the diversification of the

32. Liu Sheng, "Canjia yibao he gongshang baoxian de nongmingong renshu jun tupo qianwan" [The number of migrant workers who have participated in both medical insurance and work-related injury insurance is breaking 10 million], available at <http://nc.people.com.cn/GB/61154/4653823.html>.

33. Li Erqing, "Woguo nongmingong canjia gongshang baoxian renshu tupo 3300 wan" [The number of migrant workers covered by industrial injury insurance reached 33 million], CCTV, September 17, 2007, available at <http://news.cctv.com/society/20070917/104359.shtml>.

34. Feng Lei, "2007 nian canjia kongshang baoxian nongmingong renshu jiang da 3600 wan" [The work accident insurance will cover 36 million peasant workers in 2007], *Xinhua Net*, April 2, 2007, available at [http://news.xinhuanet.com/politics/2007-04/02/content\\_5921922.htm](http://news.xinhuanet.com/politics/2007-04/02/content_5921922.htm).

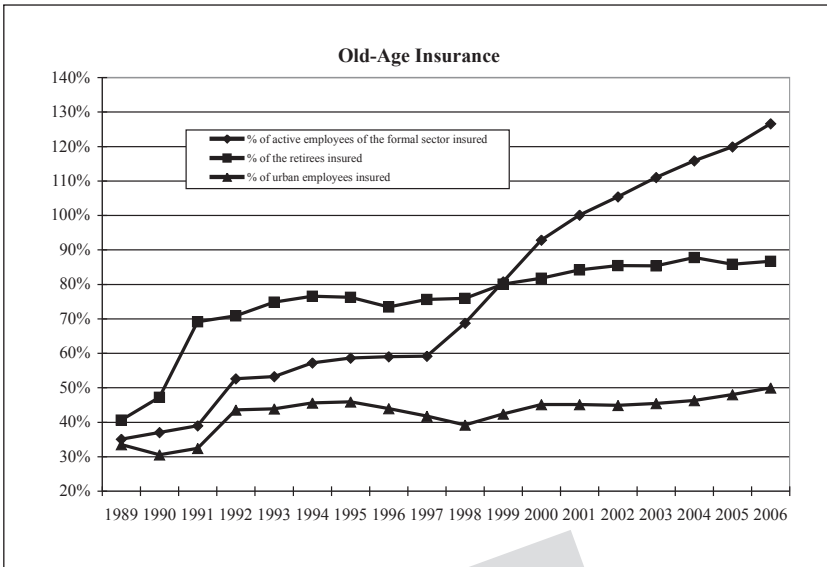
ownership structure pushed China to search for a new format of old-age insurance. In 1991, the State Council announced the Decisions on Reforming the Old-Age Insurance System for Enterprise Employees (*guanyu qiye zhigong yanglao baoxian zhidu gaige de jue ding*) and brought out a new framework for the old-age insurance system. In 1997, the State Council issued the Decisions on Establishing a Uniform Basic Old-Age Insurance System for Enterprise Employees (*guanyu jianli tongyi de qiye zhigong jiben yanglao baoxian zhidu de jue ding*) to establish an old-age insurance system in urban areas nationwide. This system extended the coverage to urban employees in non-state-owned enterprises and to those who were self-employed. Expanding the coverage was always the focus of old-age insurance reform. In the past decade, old-age insurance coverage for urban employees gradually expanded. From 1989 to 2006, the number of covered urban employees increased from 48.17 million to 141.31 million. The proportion of covered employees in the formal sector increased from 35 percent to 126.6 percent, which meant that many employees from the informal sector have also received coverage.<sup>35</sup> It is worth noting that during the same period (1989–2006), the number of covered urban retirees increased from 8.93 million to 46.35 million, accounting for 41 percent and 86.6 percent of the retirees, respectively (Figure 9), so most people who retired from the formal sector now have old-age insurance.

The goal of urban old-age insurance is to cover the entire urban working population (*jiuye ren yuan*).<sup>36</sup> From this perspective, the challenge of complete coverage is still formidable. By the end of 2006, 49.9 percent of the urban working population had old-age insurance (Figure 9), which meant that a large segment of the working population in the informal sectors, especially migrant workers, did not yet have old-age insurance. For instance, only 14.17 million migrant workers were covered by the end of 2006.

The biggest obstacle facing migrant workers is that their old-age insurance account could only be managed locally. If they move from one

35. In the Chinese statistic system, employees in the formal sector refer to those persons working in, and receiving payment from, units of state ownership, collective ownership, joint ownership, shareholding ownership, foreign ownership, and ownership by entrepreneurs from Hong Kong, Macao, and Taiwan, and other types of ownership and their affiliated units.

36. In the Chinese statistic system, the term *working population* (*jiuye ren yuan*) refers to people who are over sixteen years of age and earn their income from their labor or from managing their business.

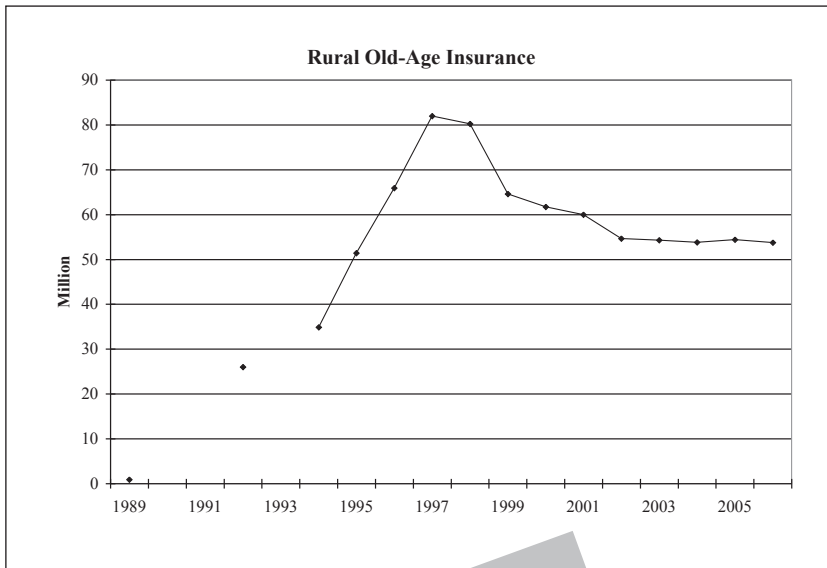


**Figure 9.** Urban Basic Old-Age Insurance Coverage

place to another, they may lose the money in their account. On June 29, 2007, the Standing Committee of the National People's Congress issued Labor Contract Law (*laodong hetong fa*), prescribed that "the government will take measures to gradually make the old-age insurance account portable throughout the whole country." This means that, in the future, when China enacts its Law of Social Insurance (*shehui baoxian fa*), old-age insurance will be managed nationally. Presently, the Ministry of Labor and Social Security is designing an insurance system for migrant workers that aims to resolve these problems and will include a cross-region subsequent transfer system.<sup>37</sup>

It is more challenging to expand the old-age insurance system in rural areas. In China today, 64 percent of the 140 million elderly people live in rural areas. As early as 1986, China was searching for a way to provide old-age insurance to those in rural areas. Based on experiments conducted in dozens of counties, on January 3, 1992, the Ministry of Civil Affairs issued the Basic Social Old-Age Insurance Plan for Villagers (*xianji nongcun she-*

37. Wang Wenlong and Xiao Ling, "Laodong he shehui baozhangbu niding nongmingong yanglao baoxian banfa" [The Ministry of Labor and Social Security has drafted a method for migrant workers to participate in old-age insurance], *Sina Net*, June 10, 2007, available at <http://news.sina.com.cn/c/2007-06-10/175013196219.shtml>



**Figure 10.** Rural Old-Age Insurance Coverage

*hui yanglao baoxian jiben fang'an*). The basic plan's premiums were paid for mainly by the beneficiaries themselves, supplemented by community-pooled funds and supported by government policies. After 1992, the old-age insurance program was carried out all over the country and the number of rural residents covered steadily increased. By the end of 1997, 82 million rural residents participated in the old-age insurance system.

After 1998, however, reforms to the rural old-age insurance system stalled, partly because the institutional reform of 1998 reassigned the managerial responsibility for the rural old-age insurance system from the Ministry of Civil Affairs to the Ministry of Labor and Social Security. But, more importantly, Chinese leaders started to question the feasibility of such an insurance system. In July 1999, the State Council pointed out that not all rural areas were ready just yet for old-age insurance. For this reason, it suggested that rural areas with the financial capacity to do so gradually switch to commercial insurance. The change of the policy prompted a sharp decline in coverage in the following five years (Figure 10).

The dramatic decline in rural old-age insurance coverage soon drew the attention of the National People's Congress and the People's Political Consultative Conference. Consequently, suggestions and proposals regarding the rural social insurance system proliferated, and debate about

the necessity and feasibility of the rural old-age insurance became more intense.<sup>38</sup> Rural old-age insurance coverage has stagnated for around 54 million people since 2002. The Report of the 16th Party Congress pointed out that “China should develop social insurance and social welfare in urban as well as rural areas. Places with the financial capacity should experiment with the systems of rural old-age insurance, medical care, and minimum income security.” The 3rd Plenary Session of the 16th Party Congress further stated that “the rural old-age insurance system is a system in which the premiums are to be paid mainly by households, supplemented by community-pooled funds and government subsidies.” In the No. 1 Central Document of 2007, the Suggestions on Accelerating the Development of Modern Agriculture and Solidly Advance the New Rural Construction of Socialism (*zhonggong zhongyang guwuyuan guanyu jiji fazhan xiandai nongye zhashi tuijin shehuizhuyi xinnongcun jianshe de ruogan yijian*), a new expression came to light: “search for various formats of rural old-age insurance.” Therefore, some local governments gradually resumed efforts to search for an appropriate social insurance for the rural population. In these new efforts, the most important change was that the insurance was funded by individuals, the collective, and the government, rather than “paid mainly by the beneficiaries themselves, supplemented community-pooled funds and supported by government policies.” The support from government fiscal subsidies had a significant effect on old-age insurance.<sup>39</sup> Currently, Shandong, Beijing, Jiangsu, Zhejiang, Anhui, Sichuan, and Xinjiang have already launched this new insurance system based on public subsidies. Among those provinces, Shandong has made the greatest progress. By July 2007, 10.67 million peasants in the province were participating in the rural old-age insurance system.<sup>40</sup>

38. Regarding the transformation of the rural old-age insurance policy, please see the article by Zhao Dianguo, Deputy-head of Rural Social Insurance Department of the Ministry of Labor and Social Security, “Nongcun yanglao baoxian gongzuo huigu yu tansuo” [Review of the rural old-age insurance], *Renkou yu jihua shengyu* [Population and one-child policy], No. 5 (2002), available at <http://www.fjlss.gov.cn/ShowInfo.asp?Infold=425>.

39. “Woguo jinnian wenbu tuijin xinxing nongcun shehui yanglao baoxian zhidu” [Our country is gradually improving the new rural social old-age insurance system], *CCTV Xinwen lianbo* [News], January 10, 2006, available at <http://cctv.sina.com.cn/news/2006-01-10/9058.html>.

40. Zhao Xiaojun and Zhao Yongde, “Wosheng nongcun yanglao baoxian canbao renshu quankuo jushou” [Our province has the highest coverage of rural old-age insurance in China], *Dazhong ribao* [Mass daily], July 5, 2007, available at [http://www.shandong.gov.cn/art/2007/07/05/art\\_5460\\_369745.html](http://www.shandong.gov.cn/art/2007/07/05/art_5460_369745.html).

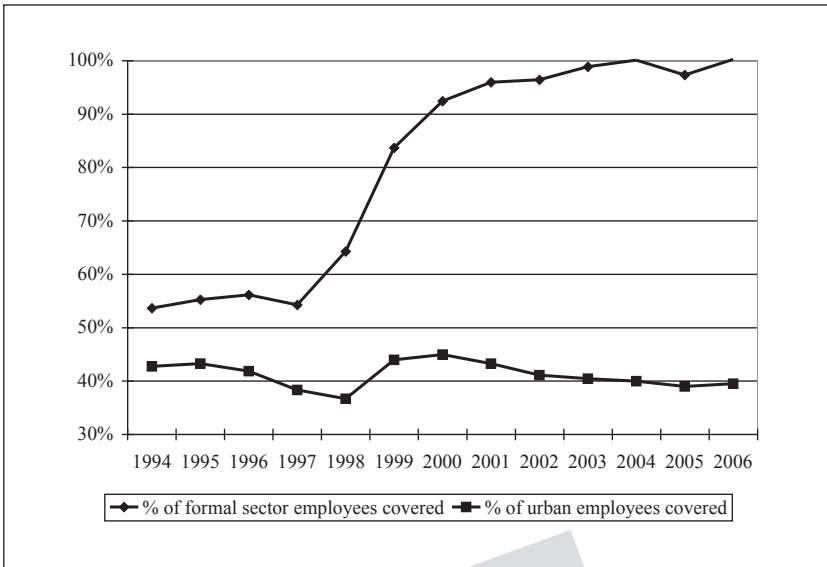
### *Unemployment Insurance*

In 1986, in order to implement the Labor Contract System and the Bankruptcy Law (*bochanfa*), the State Council issued the Provisional Regulations on Unemployment Insurance for Employees of State-Owned Enterprises (*guoying qiye zhigong daiye baoxian zhanxing guiding*), which established unemployment insurance in China. In 1993, in order to implement the Regulations on Transforming the Management of State-Owned Enterprises, the State Council issued the Regulations on Unemployment Insurance for Employees of State-Owned Enterprises (*guoying qiye zhigong daiye baoxian guiding*). However, both regulations applied only to state-owned enterprises. After the mid-1990s, as a number of state-owned and collective enterprises went bankrupt, or were reorganized, millions of “iron bowl” employees (those guaranteed lifelong employment) were laid off. Because the expanding non-state-owned enterprises did not provide “iron bowl” to begin with, the unemployment issue became more acute. In early 1999, the State Council issued the Regulations on Unemployment Insurance to extend the insurance from the state-owned enterprises to all sorts of enterprises, including collective, private, and foreign-invested enterprises.<sup>41</sup> These regulations helped increase the number of employees who participated in the insurance system from 79.28 million in 1998 to 104.08 million in 2000. The regulations had a strong impact in the formal sectors. In 1998, the coverage in formal sectors accounted for only 64.3 percent of the formal-sector employees, and the proportion increased to 92 percent by 2000 (Figure 11).

However, at the end of 2006, only 111.87 million individuals had unemployment insurance. In comparison to the year 2000, only 7.79 million were added to the insurance system over the course of those seven years. The coverage rate actually declined in recent years, falling from 45 percent in 2000 to 39.5 percent in 2006 (Figure 11).

The four different types of insurance—medical insurance, old-age insurance, and insurance for work-related injury—face similar difficulties in expanding into the informal sector. Why does unemployment insurance in the informal sector have much lower participation than the other kinds of insurance? There are two reasons. On the one hand, employees in the informal sector are not highly motivated, because, according to the Regulations on Unemployment Insurance, compensation from unemployment

41. It is up to provincial governments to decide whether social organizations and their staff, nonprofit service providers and their employees, private commercial and industrial corporations and their employees are required to participate in unemployment insurance.



**Figure 11.** Unemployment Insurance Coverage

insurance is merely about 20 to 30 percent of the local average salary, which is just slightly higher than the minimum income security system, but much lower than the minimum salary standard. Moreover, the compensation period is no more than twenty-four months. After the minimum income security system accomplished the goal of “covering whoever is eligible for the insurance” (*yingbao jinbao*) in 2002, unemployment insurance paled in its insignificance in terms of guaranteeing the minimum income. On the other hand, the government does not have a strong incentive to promote unemployment insurance. In recent years, unemployment insurance has been the subject of debate in China’s policy circle. Although expressed ideas vary, the consensus is to abandon the unemployment insurance system altogether, while strengthening the minimum income security system. This explains why the government has not done much in the area of unemployment insurance.

### Conclusion

China is experiencing “a transformation unprecedented in thousands of years” (*qiannian weiyou zhi da bianju*). More than one hundred years ago, the Qing official Li Hongzhang used these words to describe the

era he was living in. Two decades later, the May Fourth generation had a similar take on their time, too. However, in terms of the economic foundation and the speed, depth, and scope of the social structure's transformation, no other era can be compared to the last two decades or so. During the Self-Strengthening Movement (the Western influence spreading from the East" (*xixue dongjian*) started on the east coast; the countryside in the central and western regions was not touched. In the early twentieth century, the Western economy invaded China. It destroyed the craft industry along the coast area, but the traditional agricultural economy and the village structure—clans—were not greatly affected. After the establishment of the People's Republic, public ownership replaced private ownership, and the planned economy replaced the market. But almost all people in urban areas were attached to their work units for life, and the majority of peasants in rural areas depended on their collectives and families. There were limited rural markets, but they were just the necessary supplement to a largely self-sufficient economy. Such a lifestyle was not very different from the earlier one that had been based on close family and local ties.

In the early 1980s, China started its transformation toward a market economy. In the beginning, market forces had only marginal influence on the Chinese economy, but very soon they started to erode the planned and public economy. In the end, the market forces went beyond the economy and engulfed the whole society. Within two decades, market forces grew so powerful that they overwhelmed all areas, enterprise, families, and individuals. These changes were unprecedented and the most dramatic in Chinese history.

The market has magic powers. It turns stone into gold. In a market economy, great social wealth is created. Chinese people who had suffered from a shortage of material goods quickly experienced a period of surplus. People experienced changes they had never dreamed of. Nevertheless, the market mechanism was not only the accelerator of the economy but a double-edged sword. It relentlessly cut the moral linkage between individuals and various social groups and transformed people into creatures who pursued maximum interests in the market. When market forces turned the society into a market society, people who had previously depended on the collective, unit, and family were forced to start living on their own income. Paradoxically, however, modern society is full of risks, which makes it difficult for individuals (especially those who live in a substrate of society) to take care of themselves. When the fast transformation toward the market broke the traditional social safety net, it threatened to destroy the whole



society. Many people in China felt that, while the economy was prospering, all sorts of uncertainties were surfacing, and that the country was facing one crisis after another. Amid this background, protective countermovements against the market emerged. More people, including top policy makers, gradually realized that the market was not the ultimate goal, but at best the means to improve people's social welfare. The market is necessary, but the market has to be embedded in society. The government has to play an active role in the market economy to prevent a disembedded and self-regulated market economy. As Polanyi states, the expansion of the market triggers the countermovement to protect human beings, nature, and productive organizations; protective legislation and other interventions are the characteristics of this countermovement.

I have offered a great deal of data to show that a countermovement already started in China after its brief encounter with a "market society" in the 1990s. A social market is emerging in China. In the social market, the market is still the principal mechanism for resource allocation. However, through redistribution, the government will strive to re-embed the market into social and ethical relations. More specifically, the government will take effective measures to decommercialize the fields that are closely connected with human rights, and allow all social groups to enjoy the benefits of market operations while shouldering the costs of market operations. The recent policy changes show that the Chinese government has the political willingness and fiscal capacity to nurture a social market, even though both political willingness and fiscal capacity need to be further strengthened. Despite the fact that China still faces many serious problems, the eventual emergence of social policies marks a historic turning point, the significance of which can never be overemphasized.

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