The Chinese Way of Pension Reform: Why is the Chinese Pension System Extensive and Localised?

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Abstract

Pension reform in China has two puzzling characteristics. The first one concerns about the different approach to reform. Most developing countries choose to protect the privileged segments of the workforce by preserving corporatist welfare arrangements when they reformed their welfare regimes in the 1980s. By contrast, China abolished its socialist enterprise-based welfare system, which once covered millions of the elite industrial workers in Maoist period, and transformed it into an urban-based social insurance arrangement with extended coverage. As a result, China performs much better in extending the coverage of pension programs than other large developers like India and Indonesia (OECD 2011: 41). Hence we have a puzzle: Why does the Chinese government, unlike its counterparts in the developing world which entrench the interests of the privileged social sectors, choose to dismantle the social protection arrangements of old-age income security for what was its core power resource, the industrial workers, and to expand the pension program to cover larger segments of urban population? In other words, what is the driving force behind the rising coverage rate of the new Chinese urban pension system?

The second puzzle is about the structure of China's pension system. China, after three decades of market reform and welfare system building, has no unified, national scheme for its pension program. The regulation and administration of the contribution and benefit distribution of pension remains the domain of local authorities. This pattern is unique in the world: None of the major welfare states, Agarwala (1998) reports, be it unitary or federal, large or small, have their public old-age insurance system fragmented on a regional basis. This becomes more intriguing when we compare China with other large developing countries like Brazil and India. On a similar stage of economic development, these federal democracies, in which more veto points are to be expected, nevertheless have achieved the national integration of their public pension systems. It is China, a constitutionally unitary country led by a Communist party, that fails to have its basic pension schemes unified. This constitutes a second puzzle about China's pension reform: What thwarts the efforts of the seemingly formidable Chinese party-state to centralise the pension system?
This research attempts to account for the two characteristics within one coherent

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framework. In China it is municipal leaders who are responsible for implementing pension policies. Following historical institutionalism, agent's preferences and strategies are assumed to be constrained by institutions. In the Chinese context, two institutional arrangements are poised to shape and constraint municipal official's preference over and behaviour towards pension reform. The first one is bureaucratic tournament promotion, an institutional setting under which office-seeking municipal leaders compete to maximise their chances of getting promoted to provincial posts by promoting local economic development. The localised pension arrangement, in which workers' pension benefit package is not portable across localities, is therefore extended by municipalities to retain skilled workers within their jurisdiction to enhance local competitiveness. The incentive of municipal leaders to compete for promotion is in turn dependent upon the second institution named as Chinese-style political decentralisation, in which central government systematically appoints insiders, i.e. officials who rise from municipalities within the province, to the top provincial leadership posts in some provinces, while parachuting outsiders from Beijing or other localities to these posts in other provinces. Therefore, it is predicted that in province dominated by insiders, where the promise of bureaucratic promotion by central government is more credible, anticipating that their efforts are more likely to be rewarded municipal leaders in these provinces have more motivation to foster regional economy by extending pension program coverage and retaining the localised pension structure, than their counterparts in provinces governed by outsiders, where the municipal leaders' enthusiasm for local economic development is frustrated by the prospects that no matter how well they may perform in economic terms the prize of provincial posts will not go to them.

This hypothesis is tested by a panel dataset of 31 provincial-level jurisdictions from 2000 to 2010. Using Beck and Katz's (1995) technique of ordinary least squares with panel-corrected standard errors (OLS-PCSE) and a first-order autocorrelation correction (AR1), after controlling for various structural factors like demographic pressure and marketisation, the estimation supports the predicted association between the career background of provincial party secretary and the pension coverage rates and the level of old-age risk pooling. The hypothesised relationship also survives several robustness checks. By doing so, this study contributes to our understanding of the political dynamics of China's pension reform. Moreover, it sheds lights on the functioning of Chinese political institutions by using pension policy as an example to illustrate how Chinese polity shapes political actors' preference and behaviour and produces policy outcome.