

## **TOWARDS AN INCLUSIVE LABOUR MARKET IN CHINA**

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## **I. INTRODUCTION**

In this paper, I assess the extent to which China's labor market has successfully made good job opportunities available to workers throughout the country. I first review the historical evolution of China's labour market, and then introduce a framework for thinking about inclusivity of the labour market. Following this framework, I analyse how market developments and institutional reforms have influenced the extent to which China's labour market has become more or less inclusive. A final section concludes with policy lessons for other developing countries.

## **II. THE EVOLUTION OF CHINA'S LABOUR MARKET**

### **1. Legacies of Socialism**

Let us set the stage with some economic history. After the establishment of the People's Republic of China in 1949, China's new socialist leaders emphasized the development of heavy industry, and the government installed a planning system featuring prices set by the state and administrative allocation of products and inputs, including labour. All workers were matched to jobs and employers by the Bureau of Labour and Personnel, and there was virtually no job mobility. Prices were set to extract resources from agriculture to support industry, and urban workers were paid a subsistence wage and generous non-wage benefits such as housing, health care, child care, and pensions, which were not made available to rural households.

In rural areas, collectivization of agriculture was nearly universal by 1956-57. Rural households were organized into production teams, brigades, and communes. Given the unequal treatment of urban and rural populations, it was necessary to control population movement. The household registration (or *hukou*) system assigned agricultural or non-agricultural status to each person, based primarily on place of birth. In 1958, the central government discouraged population mobility by requiring that migration be pre-approved by both origin and destination governments, with limited temporary stays outside of one's place of residence.

### **2. Economic Reform: Industrialization, Urbanization, Migration, Privatization**

Since economic reforms began in 1978, the Chinese labour market has undergone a set of remarkable transformations that have dramatically affected the working lives and welfare of China's citizens. As a transition economy, China shifted gradually from planned allocation of labour in state-sector jobs to a more open labour market with increasing

numbers of workers employed in the non-state and private sectors. At the same time, like other rapidly growing developing countries, China experienced rapid structural change featuring a steady flow of labour from agriculture to industry and services, and from rural areas to urban areas. From 1978 to 2011, the share of labour employed primarily in agriculture fell from 71 percent to 35 percent, the share of labour working in urban areas increased from 24 percent to 47 percent, and the share of urban labour working in the state-owned or government sectors fell from 78 percent to 19 percent.

Although the large magnitudes of these changes are impressive, reform of the labour market has been halting, uneven, and difficult, with much additional reform required. Many of the challenges of labour market reforms have been related to the political difficulty of moving away from a set of socialist institutions that privileged the welfare of urban workers and imposed strict restrictions on population mobility. Pressures to reform the system arose from the shift in industrialization strategy from heavy industry led by state-owned enterprises to export-oriented, labour-intensive industries led by non-state firm, exploiting China's comparative advantage after China opened up to the outside world. This required bringing rural labour to work in factories located in coastal regions, which meant that large-scale migration and rapid urbanization had to be facilitated.

As the Chinese coast rapidly emerged as the world's factory, China witnessed the world's largest internal migration on historical record. Annual rural survey data collected by the National Bureau of Statistics shows that employment of rural migrant workers, nearly all working in urban areas, nearly doubled from 84 million in 2001 to 163 million in 2012. In contrast to conventional definitions of migration based on how long one has lived in one's current area or residence, in China migrants are defined as those who live in a place different from their place of household registration regardless of duration. The 2010 census found that over 220 million persons lived in a city different than their place of household registration. Rural household surveys with broad regional coverage found that by 2007, over 90% of labour market participants below age 25 and over 70% of those aged 25 to 40 were engaged in off-farm work (Rozelle et al., 2008).

Initially, migration was mostly seasonal and circular, by young, single adults, but over time rural migrants have gotten older, and more of them have migrated with family members, increasingly to settle permanently in cities. According to a large survey of 128,000 migrant households conducted by the National Population and Family Planning Commission in 2011, 78.3% of rural migrants were married, 74.3% had at least one child, and of those with children, 71.9% had at least one child living in the city (Demurger et al, 2013).

Rapid economic growth in China also was supported by expanded investments in education, large investments in infrastructure, regional decentralization that incentivized local leaders to support growth, and especially market and trade liberalization. In terms of human capital, China passed a compulsory schooling law mandating 9 years of education for all children in 1986. According to NBS rural household surveys in 2011, 23.4% of rural non-agricultural workers had educational attainment of high school or above, 60.3% completed middle school, and just 15.8% had less than a middle school degree. Illiteracy was virtually eradicated. A critical factor in rapid industrial productivity growth was an open competition policy which allowed relatively unregulated private and community-owned enterprises to flourish, which also put competitive pressure on state-owned firms to reform or go bankrupt. This eventually led to aggressive restructuring (including closure and widespread privatization) of state-owned enterprises in the late 1990s, with tens of millions of SOE workers laid off.

### **3. Challenges of Rising Inequality and Informality**

Sustained rapid growth led to massive reductions in poverty, but one adverse consequence of the unleashing of market forces was a dramatic increase in income inequality. China went from being one of the world's most egalitarian societies in the early 1980s, with a gini coefficient of around 0.30, to being one of the world's most inegalitarian countries, with an official income gini coefficient of 0.47 in 2012 (Yao and Wang, 2013). Increases in urban-rural inequality contributed the greatest amount to the rise in income inequality over most of the reform period (World Bank, 2009), suggesting that despite increased migration the economic opportunities available to rural workers remained highly circumscribed compared to urban workers. The magnitude of urban-rural income gaps in China, plotted in Figure 1, is very large in comparison to other countries.

Another emerging challenge was the rise of informal employment. Because of China's socialist legacy, the starting point for economic reforms was nearly universal formal employment in urban areas. Under planning, urban workers enjoyed guaranteed employment, housing, pensions, and health care. However, during the reform period, the rise of a dynamic but relatively unregulated private sector, the aggressive restructuring of state-owned enterprises which led to layoffs of millions of state-sector workers, and a surge in rural to urban migration all have led to an increasingly large number of workers in urban areas who are self-employed or who lack formal labour contracts with their employers (Park and Cai, 2011).

As is well-known in India, the prevalence of informal employment raises policy concerns because informality is often associated with poverty and social vulnerability. However, informal employment can also be voluntary, for example when there are high economic returns to self-employment, or when the perceived costs of participating in public social insurance programs are greater than the perceived benefits (Friedman et al., 2000; Maloney, 2004). Thus, the nature of informal employment and its relationship to labour regulations and policies is complex and depends on the historical and institutional context.

According to the 17th International Conference of Labour Statisticians (ICLS), informal wage jobs are those in which the employment relationship “is not subject to national labour legislation, income taxation, social protection or entitlement to certain employment benefits (advance notice of dismissal, severance pay, paid annual or sick leave, etc.)” As just noted, multiple forces led to a rapid rise in informal employment in the late 1990s and early 2000s. In 2002 and 2003, the share of urban workers who were “missing”, measured as the gap between the number of employees estimated from labour force surveys and the number reported by employers, reached a peak of 39 percent before declining somewhat thereafter (Figure 2) (Park and Cai, 2011). Figure 2 also illustrates the rapid rise of the private sector and the decline of state-owned enterprises.

In a recent co-authored paper analysing data from the China Urban Labour Survey conducted in 6 large cities in 2010, we provide the first estimates of the extent of labour market informality in urban China based on standards established by the International Labour Organization (ILO) (Wu, Park, and Du, 2013). We employ two criteria for measuring informality--whether you lack coverage by the main social insurance programs and whether you lack a formal labour contract. We find that one quarter of urban workers in China do not have access to pension, health, or unemployment insurance, and about thirty percent of urban workers are employed in the private sector but have no formal contract. While these rates of informality are relatively low by international standards, they are similar to other transition economies such as Russia, Romania, and Moldova that also originally had universal formal employment under socialism (Charmes, 2009).

However, the overall low rates of informality mask significant heterogeneity. In particular, a large share of migrant workers, approximately 60 percent, are informally employed. While the share of migrant workers that signed formal contracts has increased in recent years, in part because of the passage of a new Labour Contract Law, less progress has been made in providing migrant workers with social insurance coverage.

### **III. TOWARDS AN INCLUSIVE LABOUR MARKET IN CHINA**

#### **1. A Framework for Inclusiveness**

Over the years, development organizations have paid great attention to the goals of growth with equity, pro-poor growth, and inclusive growth; most recently the World Bank's newest slogan is to promote "shared prosperity" (World Bank, 2013). All of these notions reflect a desire for economic growth to benefit those at the bottom of the income distribution. Today, I want to focus attention on three dimensions of inclusivity in the labour market. The first is inclusiveness of employment demanded by the market, which primarily reflects the fundamentals of labour demand and labour supply, and is influenced by a country's overall growth strategy and the human capital of the population. In particular, how does growth and structural change affect the earnings opportunities of low skill workers relative to high skilled workers? The second dimension is inclusiveness associated with labour market integration and labour mobility, which focuses on equality of access to jobs available in the economy. And finally, the third dimension of inclusiveness is equitable access to high quality jobs; where I define high quality jobs as being formal jobs rather than informal ones. A formal employment relationship provides workers with a measure of security due to legal protections and access to social insurance programs.

#### **2. Key Role of Economic Growth and Labour Demand**

At the heart of China's increasing demand for labour is China's stellar record of consistently high rates of economic growth. While the expansion of exports has been an important part of China's growth story, it cannot account for most of China's economic growth during the reform period. After China's WTO accession in 2000 and prior to 2008, China enjoyed a period of very rapid growth and rising real wages, especially in the years just prior to the crisis. Unlike in the 1990s, wages grew not just for skilled urban workers, but also for unskilled workers, especially rural-urban migrants. In the 1990s, the unskilled factory wage reportedly was relatively flat, although this conclusion is based primarily on anecdotal evidence. In 2006 and 2007, the years prior to the crisis, real wages of migrants grew by about 10% per year. It should be noted that throughout the 1990s and early 2000s, the returns to education, especially higher education, grew steadily (Zhang et al., 2005). Thus, despite recent concerns about rising unemployment of college-educated workers, through the mid-2000s the wages of those with higher education on the whole increased faster than those of unskilled workers.

Starting in the early 2000s, there were occasional reports of shortages of migrant workers in parts of southern China, where China's labour-intensive manufacturing is concentrated. However, many viewed these shortages as temporary phenomena that could be alleviated through better market integration that brought new migrants from more remote, interior regions to coastal areas. As the real wages of migrants started to increase more rapidly in the mid-2000s in the years just prior to the economic crisis, and reports of labour shortage became more frequent, serious debates started to emerge both within and outside China over whether the era of low-wage "surplus" labour in China had ended--debates which continue to the present day.

By 2003, according to NBS rural household survey data, migrant and total non-agricultural income accounted for nearly 30 and over 50 percent of rural incomes, migrants accounted for over 20 percent of the potential rural labour force, and over 40 percent of the rural population lived in households with at least one migrant (World Bank, 2009).

The evidence suggests that labour markets had deepened substantially in the years prior to the economic crisis. But if there were any doubt about the persistence of labour shortage in the Chinese economy, they have been put to rest by China's post-crisis experience. The economic crisis struck in October of 2008, leading to an estimated loss of 20 million jobs, or nearly 15% of all migrant jobs, almost entirely borne by migrant workers. National and local governments worked hard to protect the employment of urban residents through the crisis through an array of supportive policies, including a massive stimulus package, wage subsidies, suspension of tax and social insurance contribution payments, credit access, and retraining programs. But there was much less concern about protecting the jobs of migrant workers, who returned to their home villages in droves during the months just before spring festival 2009.

What is remarkable is how quickly the employment of migrant workers rebounded along with the overall economy.<sup>1</sup> One survey found that two thirds of migrants who lost jobs due to the crisis were re-employed by the summer of 2009 (Huang et al., 2011). NBS annual estimates of migrant employment showed an increase in total migrant employment of 2.9% between 2008 and 2009, the year spanning the crisis. More strikingly, several national surveys by different government agencies confirm that the real wages of migrant workers increased steadily in 2008 and 2009 (Figure 3). Figure 4 plots the annual growth of real annual wages of urban formal employees and rural migrants over the past decade (2002 to

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<sup>1</sup> This discussion of employment impacts of the crisis draws heavily upon Giles, Park, Cai, and Du (forthcoming).

2012). It shows that from 2002 to 2011 the real wages of urban formal employees increased by nearly 14% per year on average, with some year-to-year fluctuations. The wages of rural migrants increased at a somewhat slower average rate over this period (12.1%) but the rate of increase has accelerated over time. While the rate of increase of rural migrant real wages was lower than that of urban formal employees in all years through 2007, since then it has been higher in every year except 2009 the year that 20 million migrants lost their jobs after the onset of the global financial crisis. From 2007 to 2012, rural migrant wages increased by an average of 17.1% in real terms. Figure 5 plots the ratio between the average monthly wages of rural migrants to that of urban formal employees. Consistent with the wage growth patterns described earlier, it shows that migrant wages declined sharply relative to urban formal employee wages from 2001 to 2007 before reversing. In 2011, rural migrant monthly wages were 58.8% of that of urban formal employees.

Wage regressions using repeated cross-sectional data on urban households in 9 provinces find that the returns to a year of schooling increased rapidly from 1988 to the early 2000s, but have remained relatively stable since then (Li et al., 2012). In 2009, the return to an additional year of schooling was 9.5%, very close to the world average of 9.7% (Psacharaopoulos and Patrinos, 2004).

The relatively greater demand for unskilled labour also may be contributing to reversing the long-standing trend of rising gaps between rural and urban incomes per capita despite large migration flows. For much of the reform period, rising rural-urban income inequality has been the most important contributor to rising overall inequality in China (World Bank, 2009). The ratio of urban to rural per capita increased from less than 2.5 in 1997 to more than 3.4 in 2009. Since then, the ratio has declined for three consecutive years (2010-2012), providing hope that there has been a more-than-temporary reversal of this major dimension of inequality (Figure 1). But the ratio still remains above 3.0, reflecting large disparities in urban versus rural living standards.

Thus, robust labour demand has finally pushed China past the Lewis turning point and started to create large gains in incomes and living standards for less-skilled workers, making growth more inclusive. However, the rapid growth in wages also creates challenges for employers who must adapt to much higher costs of labour. When wage increases outstrip productivity increases, as appears to have happened in recent years, it negatively affects firm profitability; in fiercely competitive sectors this can lead to failure or forced relocation to lower-cost regions or countries.

China may be challenged to establish the legal, financial, and research institutions that can enable producers to innovate and shift to higher-value added goods and services in line with dynamic comparative advantage. The role of government in anticipating and managing this adjustment process will be at the center of policy debates for some time to come.

### **3. Labour market integration**

The fact that labour demand has been so robust in China in recent years has been like a rising tide that lifts many boats. But it does not ensure that all individuals have equal access to available employment opportunities. Both efficiency and key dimensions of equity may be promoted by a well-functioning labour market in which workers can move freely to find the best employment matches to their interest and abilities. We expect that as the labour market deepens and becomes highly integrated, individual differences in non-productive factors (such as location, hukou type, gender) should become less important in wage determination while the returns to productive factors such as education and experience should increase. This means that freer movement of labour should make the labour market more inclusive with respect to differences in non-productive factors but less inclusive with respect to productive factors.

Increasing empirical evidence supports the hypothesis that labour markets have become increasingly integrated over time in China. Corresponding with the surge in migration, regional wage differences narrowed in the early 2000s even after controlling for human capital differences, after widening during much of the 1990s (Park, Cai, and Du, 2010). In most villages, even in interior areas, people know what the market wages are in coastal areas and have confidence they can find work if they decide to migrate. There do not appear to be any prohibitive barriers to migration, and yet the treatment of urban versus rural residents remains unequal in important dimensions that impact migration decisions.

The regression results of wage regressions using the 2010 CULS data also reveal that the wage discount for being a rural migrant after controlling for education and experience increased from 24.1% in 2001 to 42.2% in 2005, but declined to just 13.1% in 2010 (Nan and Park, 2013). The recent decline is consistent with improved labour market integration. When we add controls for sector and firm ownership type, the results are similar but the coefficient on the rural migrant dummy is very small and no longer statistically significantly different from zero in 2010 (Nan and Park, 2013). This means that by 2010, rural migrants were not systematically paid less within the same sector and ownership type; lower wages for rural migrants were due to migrants' working in lower paying sectors and ownership types. This

contrasts with studies of earlier periods that found strong evidence of differential treatment of migrants within occupations and sectors (Meng and Zhang, 2003).

Despite encouraging evidence of more equitable pay for migrants, there remain important institutional factors that influence the migration decision and may inhibit free movement of labour. First, rural households have use rights but not ownership rights over their land, which means they cannot use their land as collateral to finance investments in businesses or housing purchases elsewhere. They may even fear the loss of land use rights if they migrate. Second, institutional rigidities create high costs to moving to cities with dependent family members. Children may have to pay extra fees to attend local schools in urban areas, or be unable to take the college entrance examination in the migration destination (so must return home to complete high school). The elderly may be unable to get reimbursements for health expenditures in hospitals that are not located near their official place of residential registration. Finally, the rollout of new rural social insurance programs (rural pension and health insurance programs) that are subsidized, voluntary, and not linked to employment, may undermine incentives for migrants to participate in social insurance programs provided by their employers.

The reforms announced at this year's 3<sup>rd</sup> Plenum meetings by the Xi-Li government address some of the current institutional failings. The government announced plans to clarify and commercialize farmers' land use rights, and eliminate the use of agricultural and non-agricultural hukou in small- and medium-sized towns. These are steps in the right direction, but much remains to be done.

#### **4. Broadening Access to Quality Jobs: Labour Regulation, Social Insurance, and Informality**

On January 1, 2008, China implemented a new Labour Contract Law with provisions widely considered to be highly protective of workers. The passage of the new Law reflected the government's recognition of the rising aspirations and expectations of Chinese workers and the political importance of ensuring fair employment practices to avoid labour unrest. Since the mid-2000s, the government also has moved aggressively to expand coverage of key social insurance programs, especially pension and health insurance programs. One can view these measures as an attempt to increase the quality of jobs for all of China's citizens, and reverse the trend of increasing labour market informality.

As is well understood in India, such efforts are not without risks. Prior to the Law's passage, business leaders and many commentators inside and outside of China expressed

concern that the Law would increase labour costs of enterprises, reduce employment, and undermine international competitiveness (Gallagher and Dong, 2011). Before its passage, heated debates occurred over the Law's merits, engaging leading public intellectuals and receiving significant media attention. In 2006, the National People's Congress opened a thirty-day period of public consultation on the draft law that attracted more than 190,000 comments, more than any other draft law in recent history (Liang 2008). The debate reflects disagreements over the potential benefits and costs of labour regulation. In its 2013 World Development Report (World Bank, 2013), the World Bank suggests that there is little consensus on what labour policies are optimal but advises that countries avoid “the two cliffs”—one of excessive regulation that slows job creation and growth, the other of excessive lack of regulation that fails to provide voice or protection to vulnerable workers. How well China has struck this balance?

Two important aspects of the new Law were regulations on the nature of contracts that employers were obligated to provide workers and increased severance payments to fired workers. Under the new Law, after a worker completes two fixed-term contracts, or ten years of employment, employment contracts should be made open-ended. Employees with open-ended contracts must be terminated for cause. With respect to severance conditions, the new Law requires 30-day written notice when terminating workers through non-extension of a fixed-term contract, severance pay equal to one month's pay for each year of service, and double severance pay for unfair dismissal. The Law also provides significant penalties for failure to sign written contracts, pay wages on time, or provide required social insurance benefits; increases the power of workers to participate in decision-making regarding rules and regulations that bear on employee welfare; and enhances the power of enterprise-level trade unions to ensure compliance with labour regulations (Article 78).

Given all of these provisions, China's new labour regulations now look very strict in comparison to other countries. If the measure of Employment Protection Legislation (EPL) strictness that has been applied to OECD countries (OECD, 2004) were applied to China's new Labour Contract Law, China would rank third among OECD countries in terms of the overall strictness of its EPL.

How well has the new Labour Law been implemented and have stricter labour regulations adversely affected employment outcomes? In recent papers, I investigate these questions with coauthors (Gallagher et al., 2012; Park, Giles, and Du, 2012). In a national survey of over 2000 manufacturing firms in 2009 and in the 2010 CULS in 6 cities, we asked respondents to assess how well the new Law has been implemented. At the time of the

survey in 2009, 24.6% of firm managers report that enforcement of the Law is very strict and 71.3% say it is strict; only 4.0% say it is not strict. Among individuals interviewed in household surveys conducted in 6 cities in early 2010, over 50% of respondents say that implementation of the law is satisfactory or good, with most of the rest expressing ambivalence (less than 5% say it is poor).

These results provide evidence that the implementation of the new Labour Law was taken seriously. The Law was well-publicized so that many workers became aware of its provisions and used the Law to seek redress from employers not in compliance with the regulations. Legal statistics show a sharp spike in labour disputes following the implementation of the Law. One reflection of the Law's impact was that according to household surveys conducted in the same 5 cities in 2001, 2005, and 2010, the share of workers without formal labour contracts declined in the late 2000s after increasing in the early 2000s. For migrant workers, the share of workers without contracts fell from 85% to 53% from 2005 to 2010 while for local residents the informal share fell from 31% to 26%.

Has the efforts to enforce strict labour regulations affected the willingness of enterprises to hire workers? As noted in the previous section, aggregate employment of migrants continued to increase from 2008 to 2009, so any negative effects of the Law on employment were not sufficient to negate the overall robust demand for new workers. However, when asked about the impact of the Law on labour costs, 11% of firm managers say that it increased labour costs substantially, 68% said it increased costs somewhat, and only 21% reported no increase. In addition, 31% of managers said the law had reduced firing, and 16% said it reduced hiring. According to econometric analysis using the firm data from 25 cities, cities with relatively lax enforcement of labour regulations prior to the implementation of the Labour Law saw a greater increase in enforcement of the law and slower employment growth compared to cities with initially more strict enforcement (Park, Giles, and Du, 2012).

Overall, these findings suggest that the Labour Law is negatively affecting employment in manufacturing firms, but that this is not leading to absolute reductions in overall employment or real wages. In an environment of labour scarcity and robust labour demand, firms realize that they must improve workers remuneration or compete on other margins such as working conditions and compliance with labour regulations. At the same time, policy reforms that improve the portability of pension and other benefits, and the increase in aspirations of migrants to remain permanently in cities, may be increasing the

demand for formal employment by migrants. Given this context, China may have chosen a propitious time to move forward with stricter enforcement of improved labour regulations.

However, we should be cautious not to conclude that the Labour Law will not impose large costs on the economy in the future. First, many of the more onerous provisions of the Labour Law, especially the requirement to grant permanent employment contracts, have not yet become binding. Second, the lack of employment flexibility in the future could impose high costs on firms in times of fluctuating market conditions, especially in times of depressed labour demand. In the future, more and more rural workers will migrate permanently to cities with their families, and unlike the past will not be able to return to rural areas when jobs are scarce, creating greater prospects for higher unemployment rates for migrants in times of downturn. If the law becomes more burdensome to employers, a tradeoff between quantity and quality of jobs could arise and incentives for evasion will increase. The history of unemployment in developed countries suggests that stricter labour regulations passed during times of economic expansion may have large negative employment effects years later during times of recession (Pissarides, 2013).

In addition to enforcement of new labour regulations, China has sought to build a more complete social insurance system by undertaking a variety of reforms to establish modern pension, unemployment, and health insurance systems, and expand coverage among both workers and dependents. However, it has not enacted a law governing social insurance programs, which leads to greater local discretion in implementation. Factors contributing to continued low rates of social insurance coverage among migrant workers include high contribution rates, skepticism about the benefits of insurance, lack of portability of benefits across provinces, and access to rural health insurance and rural pension programs in their home villages.

The large payroll charges for social insurance programs create a disincentive for both employers and employees to participate. Employers must pay contributions for pensions, medical insurance, unemployment insurance, and other programs equal to 30% of wages, while workers must contribute 11%. A worker who withdraws from the pension program only receives back his own contributions (8%) (Giles et al., 2013).

The programs are usually run by city governments and until recently, the contributions (and claims to future benefits) to a scheme in one city could not be transferred to other cities or regions, a fatal flaw for making the programs attractive to highly mobile rural migrant workers. Unfortunately, integrating the social insurance system through higher levels of pooling requires overcoming problems of political economy since prefectures and

provinces at different levels of development also differ significantly in their capacity to finance social insurance programs. Overall, the government has made great efforts to increase the formal nature of employment but the value of program benefits varies widely across groups and some groups, especially migrant workers, remain left out.

#### **IV. Conclusions**

Given what we have learned today about the evolution of labour markets in China, what lessons can we draw, if any, for how other countries can create more inclusive labour markets?

1. The first obvious point is that growth that drives labour demand must be the engine that creates enough employment opportunities to benefit a large share of a country's workers and so be inclusive. For most developing countries, there does not appear to be a viable substitute for manufacturing as a growth sector that can generate large numbers of low-skill jobs and achieve high rates of productivity compared to agriculture. China's recipe for success in manufacturing was straightforward: open market competition, relatively unregulated export-oriented small- and medium-sized firms, a literate disciplined labour force, infrastructure, special economic zones, and supportive local governments. Many measures that are needed to get manufacturing going merit top priority and are not directly related to the labour market.

2. Making broad-based investments in human capital and encouraging higher rates of labour market participation can help some groups, such as women, share more of the benefits from employment opportunities generated by growth;

3. Public policies should promote labour mobility by removing obvious institutional impediments to migration, such as lack of benefit portability, high costs of transportation or information, discriminatory treatment, adequate provision of public services for dependents, etc.. Wages should be market-determined to avoid job rationing and labour market segmentation;

4. Labour regulations must avoid the "two cliffs" of excessive regulation (especially at early stages of industrialization) and lack of regulation. Regulations must balance the goals of increasing the quality of jobs and creating a sufficient quantity of jobs. Robust labour demand facilitates implementation of new regulations, but does not guarantee against large negative impacts on employment during future recessions;

5. Social insurance programs should be thoughtfully designed in order to be implemented successfully, avoiding high payroll contributions (perhaps in favour of more

general revenue financing or defined contribution systems), making benefits portable, and integrating potentially competing programs to avoid distortionary incentives (e.g., employer-provided versus voluntary subsidized programs).

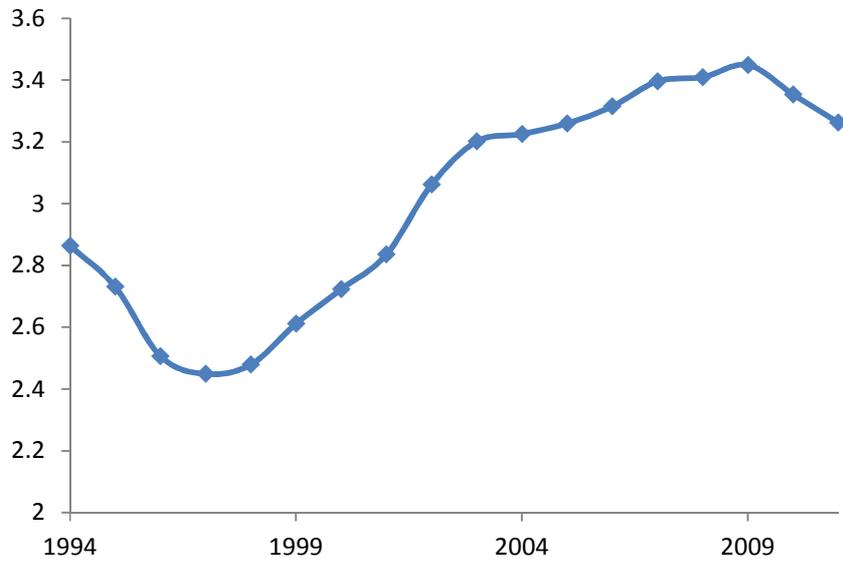
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Figure 1

**China Real Urban-Rural Income Ratio, 1994-2011**



Note: Ratios reflect 1994 prices. Source: China Statistical Yearbook (various years)

Figure 2

Composition of Urban Employment in China, 1990-2009

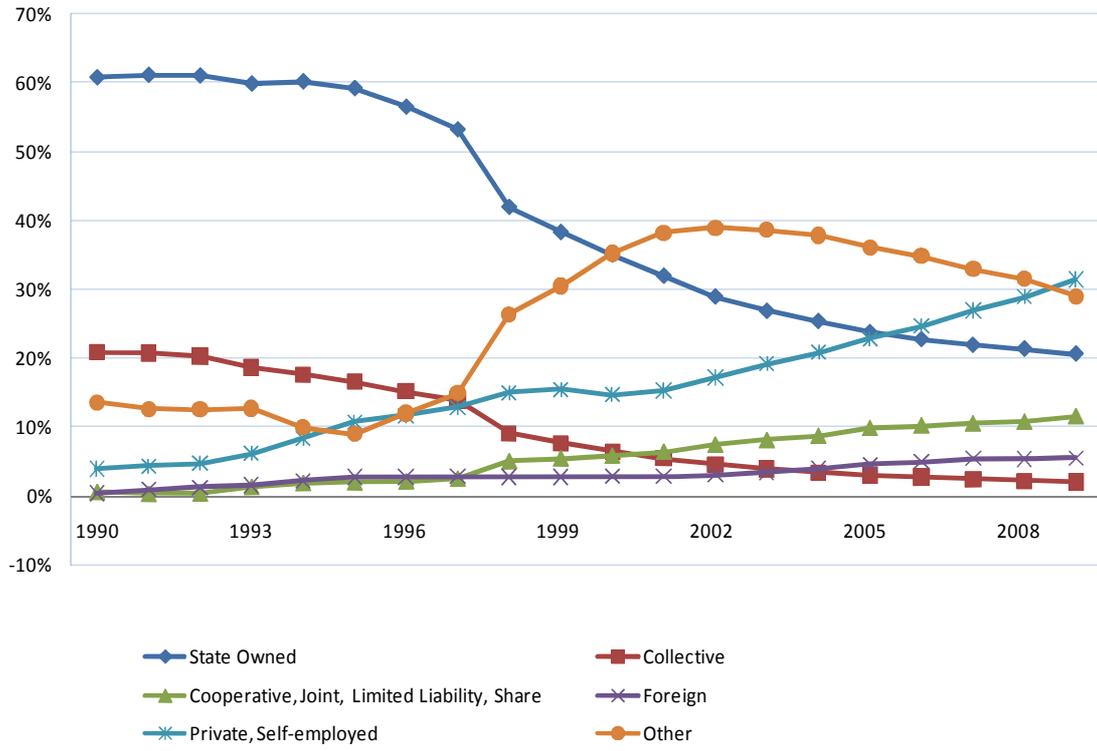


Figure 3

**Real Rural Migrant Wages in China, 2001-2009**

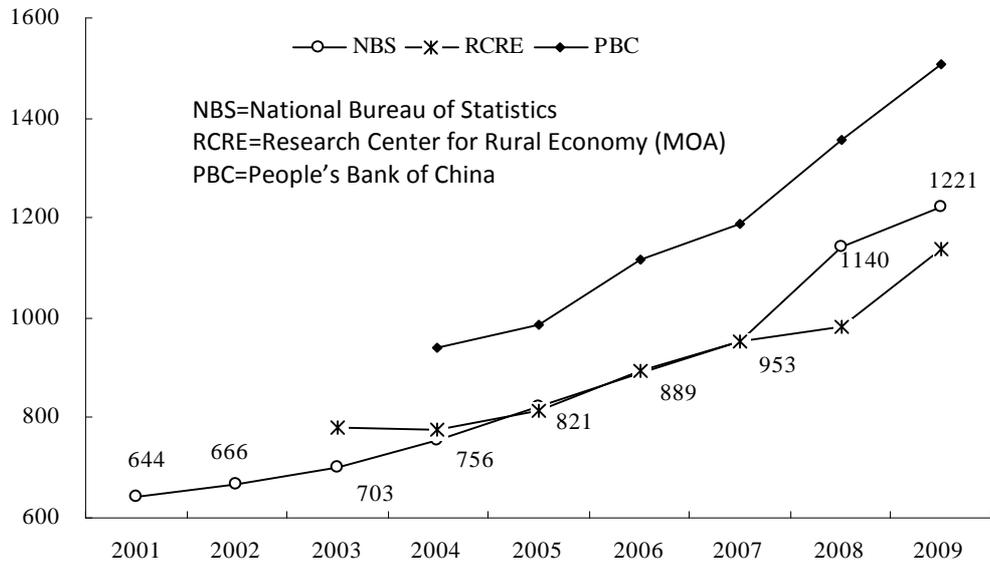
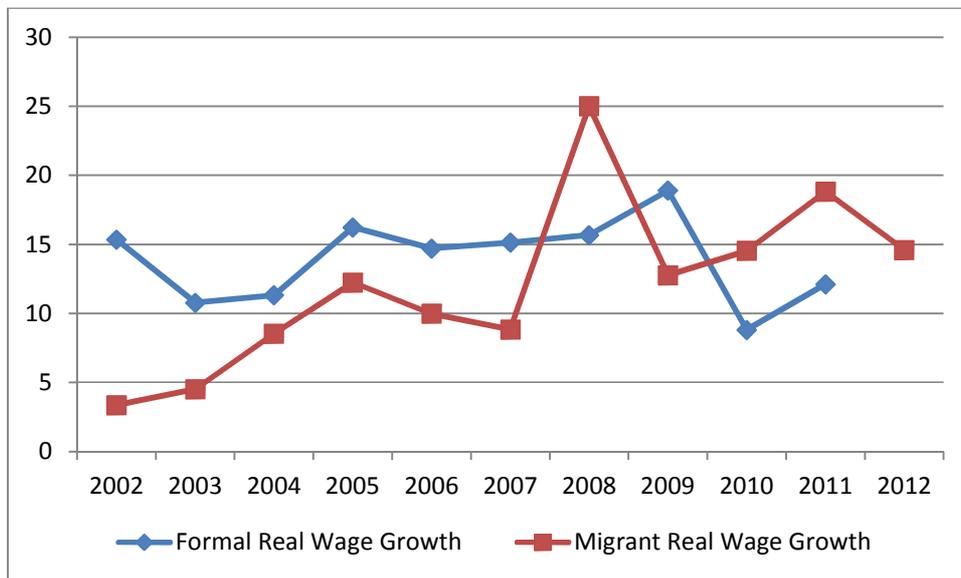


Figure 4

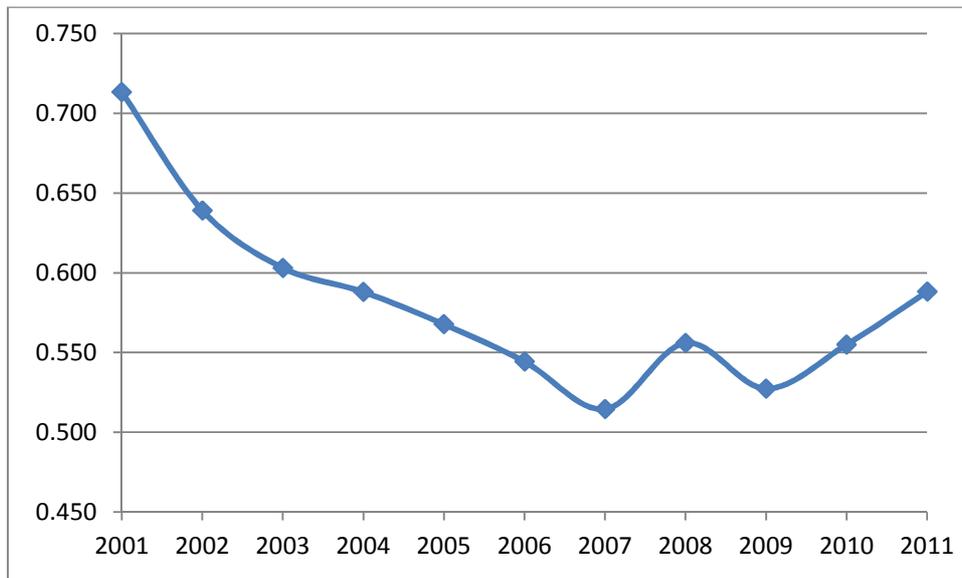
**Annual Growth in Real Wages of Urban Formal Employees and Rural Migrants in China, 2002 to 2012**



Source: National Bureau of Statistics. Formal real wages are average urban wages reported in China Statistical Yearbook (2012), rural migrant wages are from NBS rural household surveys and rural migration monitoring surveys. Nominal wages are deflated by the urban consumer price index.

Figure 5

**Relative Wages of Rural Migrants and Urban Formal Employees in China, 2001 to 2011**



Source: National Bureau of Statistics. Formal real wages are average urban wages reported in China Statistical Yearbook (2012), rural migrant wages are from NBS rural household surveys and rural migration monitoring surveys.

Figure 6

**Wage Distribution in Formal and Informal Employment, China and India, 2010**

