

THE DEFINING MOMENT?

SOCIAL POLICIES OF CHINA'S EMERGING ECONOMY AFTER THE CRISIS

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There is probably no country outside the OECD where the global economic crisis has hit harder and sooner than in China. The impact has been most severe in the areas that were previously the most dynamic parts of the global economy. Hence in coastal China an estimated 20 million jobs have been lost, and tens of thousands of factories reportedly closed down throughout 2008. While there is public optimism about China being able to weather the crisis and (mid-2009) the economic downturn seems to be bottoming-out at least temporarily, it is likely that the impact will be severe and long-lasting.

The hypothesis this paper explores is that the crisis is likely to be a defining moment, in the way the Great Depression was. Review of early evidence elsewhere suggests that the crisis is likely to lead to a drastic departure from China's development model of the last two decades, and as such will have an impact on tens of millions of Chinese that have been involved in history's most dramatic economic transformation over the last decades. But China's response also has an enormous global impact, including on the rest of the Global South where development has been increasingly determined by China's rise. In the medium term, China – which currently maintains global financial stability as it continues in the short run to trust the dollar in which much of their reserves are held – will look to reduce the global financial imbalances alongside its domestic stimulus, and to play an ever larger role in the international financial institutions.¹

The focus of this paper is the domestic social policy response to the crisis, stressing that this is based in a careful balancing of national and international economic interests. It will assess the policy response along the social policy framework as proposed by UNRISD and used in my *Reclaiming Social Policy*,² exploring how these characteristics are articulated

¹ The empirical material on which this paper – particularly the second half - is based has been collected during my three years as DFID social development adviser based in Beijing, including the joint IPRCC-UNRISD-DFID workshop on social policy, and the workshop with the Development Research Center on social policy responses to economic crises. The current work at ISS is embedded in a research project co-directed with Peter van Bergeijk and Rolf van der Hoeven, on 'A Crisis of Capitalism? A Crisis of Development!'

² De Haan 2007 and forthcoming. Social policy is loosely defined as the broad set of public interventions and institutions that intentionally enhances well-being, and as complementary (rather than residual) to economic policy.

during the crisis, including the continued urge to build a more harmonious society now using the stimulus package, the radical change in model of economic growth, away from coastal-based export-promotion towards an inward-oriented model, the potentially increased tensions in the reproductive sphere, and the potentials of a radically an extended and more egalitarian social security system and associated institutional changes.

It is generally recognised that the current crisis is global as it is in nature and needs a global response, both to ensure that similar financial crisis do not occur again, and to ensure that people around the world are supported to deal with the impacts of the crisis. Because of the increased economic inter-linkages and associated risks,³ social policies are also increasingly inter-dependent. This paper hopes to contribute to balancing the current focus in the literature on financial and economic measures, and particularly to explore the congruence between old and new economic policies and newly emerging social policies.

1. The nature of the global financial crisis

The causes, manifestations and impacts of the global financial crisis that erupted in 2008 have been well documented.⁴ The 2008 financial crises started in the US but very rapidly impacted the rest of world, including emerging market economies, as discussed in the next section for China. "Global financial intermediation is broken", wrote Alan Greenspan in late 2008 (*The Economist*, December 20th 2008: 122). Cracks in the system had appeared in August 2007 with subprime mortgage problems, and this turned turning into a full-blown financial crisis in September 2008 with the default of Lehman Brothers. The stock market wealth may have declined by around 50 % in dollar terms, according to Morgan Stanley estimates. Global GDP is expected to decline by 3 % in 2009. In August 2009 news was getting a little better. The surprising news came out that France, Germany and Japan were exiting from recession and but with doubts whether this is a recovery of the real economy or driven by government stimulus and unemployment figures in the US also are starting to appear less bad as previously thought.

Of course, the impacts on the rest of world have been highly heterogenous, across countries, and within countries (Alan Winters 2009). Africa and parts of Asia are still expected to maintain positive growth. China expected to continue to grow by over 6 %: 6.1% in the 1st quarter and 7.9% in the 2nd (with export showing a slight recovery mid-2009). Officially China is maintaining a 8 % growth target, and as 2009 goes by it seems increasingly likely it might achieve this, but questions about reliability of the figures continue to exist. The crisis is expected to have a particularly negative impact in developing countries

³ Financial crises with an international dimension have been a common part of the current phase of globalization. The 1980s and 1990s witnesses about 70 financial crises, many with an international dimension, and often short-run (Adelman 2000: 1053). As in East Asia crisis, these usually started with increases in current account deficit and fiscal deficits, followed by drops in capital inflows that financed the deficits, reduction in countries expenditure, leading to recession.

⁴ For example in preparation for the UN Conference on the crisis in June 2009, by a Commission of Experts (www.un.org/ga/president/63/commission/financial_commission.shtml). The World Bank has produced many and timely reports on the crisis, and for example opened a "crisis talks" website (<http://crisistalk.worldbank.org/>). Krugman (2009) describes the 2008 crisis against earlier crises of the 1980s and 1990s.

where people have fewer resources to cope with the crisis, social policies are too weak to respond adequately, and economic policy instruments are limited. Countries' potentials for catching up and productivity enhancement may not be affected by the crisis (even though just like poor individuals' responses poor countries' potentials for adequate responses and adjustments may be limited). In any case, it is likely that cross-border lending and capital flows to developing countries will decrease. Given China's and other Asian countries' reserves, this is less likely to form a constraint than for many other countries.⁵

In 2009, global trade is expected to fall for the first time since 1982 (*The Economist*, December 20th 2008). In June 2009, the World Bank expects global trade volume to be contracting by 5-10 % during 2009 - while world GDP declines by 3 % - but to pick up again in 2010.⁶ Impacts on trade are of course expected to be very different across the globe, including because of the drastic changes in prices accompanying the crisis and following the preceding price spikes particularly of primary commodities like oil. East Asia's exports are expected to fall by 9 % in 2009, and recover the year after.

Global FDI may have declined by about 15% in 2008, as the financial crisis is transmitted through tighter credit, lower corporate profits, and eroded business confidence. Developed countries that are heavily affected include Ireland, Finland, and the Netherlands, where inward FDI contracted by 25% - across the EU members the picture has been mixed. FDI in Developing countries was still expected to see a growth of 7%, with the expectation for Asia at 6%.⁷ But in China, in the first 7 months of 2009 FDI saw a decline of 20% compared to the same period in 2008.

International (net) private capital flows to emerging markets alone reached \$929 billion in 2007, but are expected to fall to \$165 billion from the 2007 peak (*The Economist*, February 7th, 2009).

Migration too is expected to be impacted by the economic crisis, even though there is no large-scale return to countries of origin. World Bank estimates suggest that the remittances to developing countries had been growing rapidly in 2007 and most of 2008, to a record of \$328 billion, but started to slow down at the end of 2008, and a 5-8 % decline is expected for 2009, particularly in Latin America.⁸

Governments' responses to the economic crisis have been forceful, and apparently very different from the crisis of the 1930s, or indeed different from the advice that was given to East Asian governments after the 1997-98 crisis. The focus has been to restore global financial stability, through large-scale government interventions across the world, but a range of micro-level measures has been introduced in response to increasing unemployment, and for example to promote housing markets. In many countries, this contributes to an huge increase

⁵ Quoting a 2007 paper by Prasad, Rajan and Subramaniam, Rodrik (2009) highlights that in recent periods countries with high economic growth have on average been exporters of capital, with China as only one of the many examples (according to Rodrik investment demand in tradables has been the binding constraint).

⁶ See van Bergeijk 2009, who highlights the usual pattern of constant revision of projections, and the (unexplained) different estimates produced by different agencies.

⁷ According to UNCTAD data, quoted in Filippov and Kalotay 2009

⁸ <http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/Migration&DevelopmentBrief10.pdf>.

in public debt according to an estimate by *The Economist* (June 13 2009) of about \$50,000 per person in the ten richest countries, or 114% of GDP in 2014.

The impact of the 2008 financial instability which ended a short decade of stability and growth is as yet unclear, of course, though there is no doubt that the crisis once again highlighted the extent of global interconnectedness including for the emerging market economies, but also with a strong commitment – unlike after the 1929 crisis – to ensure global policy coordination, and attempts to avoid or limit protectionism. One of the big questions of the financial crisis is the role of the emerging economies. For a while there had been talk about the decoupling of emerging economies – though the term may not have been clearly defined at least there have been indications of diverging growth rates – which now has come back a little while after the onset of the crisis (Foreign Policy). Now again after the crisis, some observers see signs of greater independence of emerging economies, – deglobalisation according to Walden Bello, some arguing the crisis is a Western crisis, and a fair amount of Schadenfreude.⁹ While as indicated developing countries may be worst affected by the crisis – particularly if the international community fails to provide the required additional support – emerging economies may be able to overcome the (impact of the) crisis in a short period of time (Naudé 2009), as the crisis did not emerge because of their bad policies, their banks generally have not been directly impacted, because they have built up resilience after the 1997-98 East Asia crisis, and because the counter-cyclical packages put in place. The next section will discuss these issues with respect to China.

2. China's integration in the world economy

The figures of China growing global economic importance are well known. While still a lower middle-income country with a per capita income of around \$2000, it has experienced three decades of high levels of even though not uninterrupted growth. Recent years saw almost uninterrupted economic growth of over 10 % per year, and while the world economy is contracting in 2009 China still appears to be heading for a growth of 6-8 %. At a time when the cracks in the international financial system started to appear, China's economy was overheating, followed by a government response to slow the economy down.¹⁰ China has thus become one of the world's largest economies, and definitely the fastest growing one, even though tens of millions of people still live in extreme poverty.¹¹

In the East Asia context, China's performance over the last 30 years has not been exceptional (but it is in a broader historical perspective, for example compared to the gold standard era) – Japan and South Korea as growth champions in the 1950s/60, and 1970s/80

⁹ De Volkskrant, 27 June 2009, with commentary of Antoine van Agtmael, Parag Khanna, and May Chua. Van Agtmael (2007), claimed to have invented the term –emerging markets– in the early 1970s, describes the strategies of the new world-leading companies.

¹⁰ Talk about overheating existed since at least 2004. Efforts to slow down the economy (interest rates, lending, exchange rate) existed at least since 2006, were a high priority in 2008 (Wong 2008), and were criticised in the export-dependent areas (particularly adjustments to tax rebates?).

¹¹ Very different figures on poverty circulate, depending on poverty lines chosen (though the trend is the same for all lines): according to the official poverty line in 2004 26 million people lived in poverty, according to the \$1/day line the figure was 135 million while the new \$ 1.25 / day line puts the figure at an astounding 350 million (World Bank Poverty Assessment 2009).

respectively, with historically unprecedented growth of over 6 per cent per capita. According to Rodrik (2009), each of their growth performances was based on developing industrial capabilities (with strategic industrial policies, and using transfer of technology from foreign firms), becoming a manufacturing superpower in a short period of time. While agriculture and later rural industrialisation drove the restoration of China's economy in the 1970s and 1980s, exports have been a main driver of recent economic growth (alongside capital formation), forming over a third of GDP, about \$1,217 billion.¹²

China's world market share of trade was about 7 per cent in 2005. While exports have been mainly low technology, the share of high technology is growing and already substantial. Foreign investments in China have played an important role for its exports, and over time policy moved from joint ventures towards allowing wholly foreign owned companies. China developed an export bundle resembling a country that is four times as rich. These modern activities are generally tradeables, and China's development path has been directly linked to the world economy's phase of "supercapitalism"¹³ the expansion of the global economy met China, with its well-educated and healthy population, hungry for restoring its national economy after the economic and social disasters of the 1950s and 1960s (de Haan 2009). It remains a matter of discussion how important export is for China's overall economy; in any case exports of goods and services amounted to 40 % of GDP before the crisis, with those to the US forming about one-third of the total.¹⁴

China has had large surpluses in current, capital and financial accounts for many years, and accumulated huge international reserves (estimated at over \$2 trillion) which with the financial crisis have become a major concern and point of debate. But capital flows and exchange rates continue to be controlled. The limited openness of the financial sector has helped to reduce the direct impact of the global financial crisis on China, but the crisis did soon impact the real economy, not only through shrinking exports (Du Yang 2008) but also through the stock market through portfolio linkages.¹⁵ The Chinese banking sector appears to have been little affected, but Mingtai Fan (2008) highlights that faulty information may be distorting the picture.

Increasingly, and fairly suddenly, China has also become an important investor abroad, by both private and state companies, and supported by government policy. In recent years FDI from China has grown to a stock of 100 billion, in the sector of natural resources (where it has had a big impact on global prices before and after the crisis), but also through the creation of Chinese multinationals such as Haier and acquiring foreign enterprises or parts thereof such as Lenovo acquiring IBM's Think brand.¹⁶ Ministry of Commerce data suggest

¹² Siebert 2007; Du Yang 2008; the turning point is probably the economic downturn and civil unrest of the late 1980s (even though export promotion happened throughout the 1980s), followed by Deng's celebrated Southern Tour in 1992, and the 1997-98 East Asia crisis which strengthened the urge to build up foreign reserves. The secret journal of purged Premier Zhao Ziyang provides fascinating insight into the politics and changing economic policies in the late 1980s, with the Tiananmen Square protests and massacre at the centre.

¹³ Reich (2008). Amsden (2007) highlights how the developing world had less space to define their own economic policies after the 1970s, but China defined its own route, and started to change the rules of the game.

¹⁴ Prasad 2009: 120. According to Prasad, China's economic policies have reduced external risks, at the cost of increasing internal ones (Banking system, social instability).

¹⁵ Mingtai Fan (2008). The Shanghai stock market fell by 48 % between May and November 2008, compared to New York's and London's fall by 68 and 69 % respectively (in Sharma 2009: 2).

¹⁶ This is part of a broader emerging-markets trend. In 2003 31 companies from the emerging-market economies appeared in Fortune 500, in 2008 this rose to 62, and in ten years this may go up to one-third (*The Economist*, 18 September 2008).

that the number of Chinese companies operating abroad increased from around 3,400 in 2003 to over 6,000 by 2006.¹⁷ While rapidly growing, these outward flows are still a mere 1 per cent of total flows (and still only perhaps 2 per cent of China's total state investment) – but the trend is unmistakable, and is thus rapidly challenging the ways globalisation has been understood.

China's role in Africa has attracted much attention, even though the Asia region is much more important for China. Over the last few years, trade between China and Africa has been increasing rapidly, to over \$100 billion in 2008, which now makes China Africa's third largest trading partner (or fourth including the EU). China's main imports from Africa are oil and gas; Chinese exports to Africa include machinery, vehicles, textiles and manufactured products. Foreign direct investment in Africa has grown rapidly, to \$26 billion in 2007, even though it remains a small part of total FDI in Africa (3 per cent) and of China's total outflows (6 per cent). Largest recipients of FDI include South Africa, Nigeria, Algeria, Zambia and Niger.¹⁸

It is of course too early to form a view on the extent to which the crisis is changing China's insertion into the global economy. But in any case the judgement by the Economist (June 13th 2009) that we've witnessed the end of export-led growth has been shared by many Chinese officials, and the economic stimulus package that was introduced was seen not only as a temporary Keynesian-type effort to mitigate the downfall, but also a restructuring of its economic model. We turn to this government response later, but first turn to historical experiences of comparable crises.

3. Crisis: lessons of the past

History appears to enjoy a curious status among economists. The great development economist Michael Lipton once seems to have argued that history and mathematics are the (only) two subjects all universities should teach. But he seems to be in a minority. A brilliant US economic historian told me that after the financial crisis his knowledge was suddenly in great demand, by the same people that a few years earlier had shown no interest in hiring him. History usually enters the formal analyses of economists only through the medium of simple indicators and numbers. Whatever this may be, economic and other historians – alongside contemporary observers – have told very interesting stories that can help inform the understanding of the current crises and paths out of it. This section lists some of the lessons that appear pertinent, and this is based on a workshop I organized for DFID on request of State Council's the Development Research Centre, Beijing, February 2009.

First, from this workshop and review of literature it becomes apparent how much knowledge has been accumulated about crises responses. East Asia including China has drawn conclusions from the 1997-98 crisis (the 'class of 97', Stiglitz 2009). For example in South Korea as Huck-ju Kwon (2009) highlights there is now a feeling the country of much better prepared for a much deeper crisis in 2008. After 1997, although China was not as much

¹⁷ Quoted in Cook and Wing Lam (2009), which also emphasises that this process has included picking 'corporate champions' to become China's multinational firms.

¹⁸ Figures quoted in Cook and Wing Lam (2009), who describe the possible effect of the crisis on the impact of China on Africa, expecting the relative importance of China will continue to increase.

affected as it is now,¹⁹ the government concluded that it needed to enhance its fiscal position while avoiding the continued recession Japan fell into. In the US, as discussed by Kris Mitchener (2009), current policy responses are informed by the lessons learnt from the Great Depression. The burgeoning literature on social protection provides much evidence on what has worked and what not (Ravallion 2003, SMERU, EPRI).

Second, while the poverty literature emphasises that policies to mitigate the impact of crises need to be in place before the crisis hit, in practice this is of course problematic (if risks were well assessed, crises would be less likely to happen). But it is of course true that during crises there is insufficient time or administrative or fiscal capacity to design good policies. Natural crises often accompany economic ones, such as droughts during the both the Great Depression and the Asian Financial Crisis, and the food price crisis before the 2008 crisis. The evolution of the New Deal in the US during the 1930s illustrates the large number of initiatives and agencies that were established, and only few were successful (Mitchener 2009). Only when policies are in place when the crisis hits can they contribute to stabilising the economy – even in China where social security has gradually been expanded over the last few years it is thought unlikely that the fiscal stimulus will have an immediate impact. The lesson about the need for being prepared has now been internalised in Indonesia as well as South Korea, and the paper on Taiwan stressed the need for more imaginative and quicker responses.

Third, evidence from previous major downturns suggests crises are not merely cyclical phenomena. Right now, the US is clear it cannot return to its previous high levels of credit-driven consumption, and global financial institutions will be adapting to a new reality. China is expecting a watershed in its development model, as described in detail later. Lessons from earlier crises suggest they provide windows of opportunities and political commitment for change (even though policy advice tends to emphasise plans for policies need to be in place before the crisis hits). The New Deal in the US has meant a radical transformation, not only in terms of an increase of government as a share of GNP, but also the relationship between the federal and state and local governments was irrevocably altered by 1935, including improved coordination and public finance (Mitchener 2009). After 1997-98, Thailand put in place a wide range of supportive measure including expansion of health care and pensions for the poor, and mobilised civil society and the private sector (Waranya Teukul 2009). In Indonesia, the economic crisis was followed by social mobilisation which contributed to democratisation, while decentralisation and local decision making was strengthened. These institutional changes were critical to the new social protection measures put in place (Endah Murniningtyas 2009).

Fourth, we now know that measures put in place during crises have long-term implications – and this is a key to the idea of crises as defining moments. FDR's 1935 statement "I place the security of men, women, and children of the nation first" is a symbol of radically different public responsibility and policies. As narrated by Mitchener (2009) the impact of measures put in place in the 1930s are felt even today, through regulation in banking, labour, and farming. The New Deal radically transformed the US economy and society, not only in terms of government spending but also in terms of perceptions of state responsibility, and relations between central and local government. The East Asia crises in 1997-98 have led to a range of initiatives around monitoring impacts of economic changes, and new policies of social protection, many of which appear to be there to stay.

¹⁹ Jia Kang (2009) discusses China's 1997 response, after 10 millions jobs were lost, and Premier Zhu Rongji's promise to maintain 8 % growth, and (effective) use of fiscal stimulus.

Further, from a social policy perspective, crises are the time when the role of social policy alongside economic policy (rather than residual) comes to the fore, both as economic stabiliser and to address rising unemployment and citizens' disaffection. In South Korea there was a strong belief that economic policy was the best social policy, and this was proven wrong at the 1997 crisis, even though the notion of the welfare state as an instrument for economic development still exists. While the country's welfare state was under-going a longer term transformation, the crisis triggered a range of responses, including increasing social spending, and a rapid response to establish social protection instruments. The crisis and the surprise victory of the centre-left opposition in the presidential election cemented a new social consensus for economic reform alongside strengthening the welfare state, and new inclusive policy institutions such as a tripartite committee to promote the reform, an integrated national health insurance cooperation, and a notion of social rights under-building the welfare state (Huck-ju Kwon 2009). A key lesson thus seems to be that crises tend to galvanise the forces for better social policies, and to galvanise a social consensus for more inclusive policies. How these dynamics evolved in China is the subject of the next two sections.

4. China's social policy under 30 years of reform

This section very briefly describes China's social policies over the last 30 years, since the start of the economic reforms since 1978. For this, and for the subsequent section on the crisis response, I use the social policy framework as proposed by UNRISD (Mkandawire 2004, UNRISD 2006) and in my own work (de Haan 2007, de Haan and Sabharwal 2008, and forthcoming).

The literature on China's social policy is probably best situated in the East Asian social policy analysis tradition.²⁰ East Asian social policy has been characterised as predominantly corporatist, with a very strong 'productivist' focus, and a congruence between economic and social policy. Social policies have been pro-active 'but selective' designed to play a key role in its pattern of economic growth and entry to global markets. Despite ideas of an absence of social policy in the region, countries introduced (state-led) welfare policies at a lower level of development than OECD countries, with China of course showing a U-curve rather than linear path. Social policies have played a key role in nation-building processes. Egalitarian norms predominate in public debate, often under authoritarian practices and with a focus on productive opportunities, while at the same time policies are based on Confucian perception of the family as main provider of welfare. Finally, social spending has remained low and often skewed to particular sections of the working population, including in urban areas.

Social policy changes in China are driven by two sets of dramatic changes. First, the radical demographic shift from rural to urban areas. In the 1980s/1990s public policies came to focus on enabling moving out of agriculture, but current health and social security reforms also have strong rural components, alongside targeted anti-poverty programmes. Increasingly,

²⁰ Kwon (2005), Cook (2009). Jonathan London (2009) argues that Chinese *social* policies (similar to Vietnam's) can be characterised under a concept of 'Market-Leninist' welfare regime, because of the subordination of market institutions to political control. See further de Haan and Sabharwal 2008, using the comparative framework suggested by Gough 2008

ageing of population is playing a role, leading to priority attached to pensions reform. Second, the economic reforms of course have implied a radical and very conscious privatisation of the economy, and collapse of the social services previously provided through communes and state owned enterprises. Dramatic rises in incomes have been accompanied by a virtual collapse of public provisions, of education, health, and social security ó leading to extremely high rates of household savings, and probably substantial churning in poverty status as in particular health care costs became prohibitively high for large parts of the population. Social security coverage in the new and international enterprises remained low, uneven, and insufficiently regulated.

Urban di bao

The social assistance programme Minimum Living Standard Scheme was piloted in Shanghai in the early 1990s, and has been extended rapidly since the late 1990s, including different categories of poor households. Initially focused on income transfers, it has been broadened to education and health exemptions and housing. It is administered by the Ministry of Civil Affairs, and as other schemes is operated on a decentralised basis with local governments having space for regulation, including to set the minimum standard of living. The decentralised nature of the programme and the state of public finances of province and county administrations have led to much lower levels of spending in the poorer parts of the country. One of the key characteristics has been the administrative capacity to implement and target the programme, ensuring negative impacts like on labour supply are kept to a minimum, with neighbourhood communities playing a key role. The *hukou* system greatly influences new social policies like *di bao*: registration remains key for accessing health care and education, and migrants remain excluded – with exceptions, such as in Nanjing that integrates rural and urban *di bao* policies.

While the 1980s focused on privatisation and economic growth while accepting increasing inequality, during the late 1980s and 1990s the forces for strengthening government in public services started to grow, resulting in reforms in education, health, and social security ó the urban *di bao* programme is one of the examples for this.²¹ Social policy reforms under the ‘harmonious society’ banner are the Party’s response to fear of social unrest (though the protests are probably less the result of rising inequalities than perceived injustice around corruption or environmental disasters), and health crises like SARS that led to a push for more effective public policy.

The basics of China’s political system may have remained unchanged ó at least comparatively in the face of the collapse of the Soviet Union ó but policy makers are clearly responding to political and citizens’ pressure. While reform of the social security system involves addressing the needs and political pressure of various segments of the workforce, the focus on inequality and the creation of a ‘harmonious society’ is a political project, geared towards maintaining national and political stability.²² The evolution of social provisions is closely intertwined with the development of broader policy institutions, including the articulation of rights and citizenship. While many international observers have commented on China’s incomplete institutional transition, social policies have evolved in tandem with the

²¹ The broad range of China’s social security policies are listed in the White Paper published in English at www.china.org.cn/e-white/20040907/index.htm.

²² The recent effective Government of China’s response to the May 2008 earthquake illustrates a similar point, with its leaders finding their position and the country’s unity greatly strengthened.

very rapid institutional changes that are taking place, such as changing articulation of public and private spheres related to opening up of markets, power balances between ministries like health and civil affairs in the reform of health services; decentralisation including of public finance that came make funding for social provisions regressive (Zhang and Fan 2007); and for example the gradual reframing of rights for migrants workers breaking through the dualism of the *hukou* system created during the pre-reform decades.

A key aspect of policy reform in China is its gradual and decentralised nature. Policy reforms (such as for *di bao*) are piloted in specific areas, and scaled up when successful, and even then usually with locally-specific rules (such as the new health insurance, and *dia bao*). Policy making is strongly evidence-based, and development *de-politicised*. International influences also have been evident in the way Chinese social (and other public) policies have evolved. As elsewhere, the opening up of the Chinese economy, including in WTO accession, have contributed to more pro-active social policies. For example, China's signing of ILO Conventions have gone hand in hand with addressing rights of migrant, child, and bonded labour. International collaboration is pro-actively sought in all economic and public spheres; the recent openness with which China sought international collaboration after the Wenchuan earthquake consolidated this trend of (controlled) openness. Donor projects *ó* for example in health, education, poverty, migration *ó* are seen as important in experimenting with new approaches.

Reforms of social policies are as much a battle of ideas as a reconstitution of power balances. With health care to a large extent privatized in the immediate post-reform period, over an extended period discussions focused on the forms that social provisions had to take (national health care vs social insurance), in turn shaping the relationship between states and citizens as well as inter-departmental control. While some of the economic reforms like dismantling of SOE have made directions of restructuring of provisions inevitable, the policy debates show that ideas can play a relatively independent and crucial role *ó* for understanding the evolution of social policies it is central to chart the articulation of these ideas and underlying premises.

The way links between economic and social policies are integrated into public policy making show clear signs of the *productivist* orientation of social policy. Public spending, including in sectoral allocations to social sectors (to some extent seen as *non-productive*), are tightly controlled. Provisions are strictly targeted, with tight eligibility criteria, and supported by a very low poverty line (only recently increased). In financial terms, the East Asian experience appears to conform closely to the Washington consensus,²³ but in ideological terms in East Asia the state continues to be seen as the guardian of public welfare. Public policies around for example capacity building, and emphasis on adjustment to enhance returns from policy (for example in the approach to poverty alleviation programmes) also emphasize the productivity of public investments, rather than seeing it as merely residual spending. The state has maintained a strong steer of social policy alongside economic policy, and has strengthened this in response to macro-level transitions and crises.

²³ China's ratio of public spending to GDP is low by international comparison, but such comparisons are difficult. According to Song Li (2009) inclusion of extra-budgetary revenues would lift the fiscal revenue number above that of many OECD; moreover fiscal revenues doubled from 10 to 20 % between 1998 and 2008.

By 2008, Chinese policies were definitely moving towards universal social policies, while responding to China's great transformation, and inevitably shaped by institutions and power constellations, notably the urban-rural dualism. The policy shifts were based in and articulated strong notions of equity (or at least an idea of state responsibility for welfare for the entire population), and were an evident response to fears of social unrest. Fiscal prudence and an ideology of economic contribution rather than welfarism has continued to dominate the thinking about social policy. This set the scene for the immediate and impressive response to the crisis in 2008, which is described next.

5. China's response after 2008-09: a new social policy model ?

The single most important direct impact of the crisis on China is the decline in export opportunities. The economic crisis has had a visible – though not as far as I know clearly quantified – impact on employment. Graduate unemployment has been rising for some time. Large numbers of unskilled workers have lost their jobs. Estimates on unemployment are unclear. Urban unemployment was 4% mid-2008, and very slowly rising. The Financial Times based on government statistics reported 67,000 factories have closed during the 1st half of 2008, and local newspapers suggested 6.7 million jobs disappeared in Guangdong.

Most of the unskilled newly-unemployed workers are migrants, who – as was widely reported – were expected to return to their areas of origin. At the end of 2008, government officials in Chongqing estimated 10,000 migrants were returning every day – expecting to increase till Chinese New Year at the end of January. The generally accepted number for job losses became 20 million. This number seems to have been generated by the Ministry of Agriculture, who was concerned about large-scale returns of workers in a context where further agricultural development and reform envisages further transition out of agriculture. The estimate was produced through focus groups discussions led by a research group, which indicated workers thought 10-15% of migrants were returning, implying 15-20 million. Many migrants did not expect to get their jobs back.

The return of migrants was closely monitored, because of the fear of social unrest (which did not appear to have occurred on a large-scale, and protests appear to have been limited to factories, and arguably the ethnic tension and violence at the Guangdong toy factory was related to job losses). Observations suggested that young migrants were often not returning to their villages but to local county towns. Many workers returned early from the New Year's holidays in search for jobs, closely monitored by officials and police.²⁴ While numbers of unemployed are not clear, a distinctive trend of worsening labour conditions as a result of the crisis has been observed by China Labor Watch for example,²⁵ including measures to reduce statutory labour costs in an effort to maintain jobs as much as possible.²⁶ The crisis is likely to deepen some of the tensions in the reproductive sphere, because of

²⁴ <http://www.nytimes.com/2009/02/06/business/worldbusiness/06yuan.html>

²⁵ <http://www.chinalaborwatch.org/Li%20Qiang-%20Impact%20of%20the%20Economic%20Crisis.pdf>

²⁶ <http://flaglobalaction.blogspot.com/2009/05/china-answers-global-crisis-with-new.html>. In January the Ministry of Human Resources and Social Security issued a joint statement urging employers to avoid or reduce mass layoffs by reducing wage costs, placing workers on leave or 'flexible working arrangements'. In February the State Council advised local governments to cut employment costs temporarily by reducing or suspending social security premiums.

increased pressure on migrants workers with impacts on children and elderly, increased pressure on women in labour markets enhancing their burden, increased unemployment with possible negative impact of violence, etc. Finally, in mid-2009 some observers argued that the government was much less concerned with unemployment in rural areas than that of educated, urban workers (SCMP).

Throughout 2009, the early optimism that China would be able to weather the crisis has been maintained (World Bank, Prospects for the Global Economy, June 2009). Despite heavy blows to the export industry, China has the fiscal and macroeconomic space to implement a substantial stimulus. It does not rely on external financing, and the banks and their foreign investment have been relatively little affected. There are doubts about available data ó regarding GDP, bank information, figures on unemployment and new jobs ó but this does not seem to have a large impact on the assessment that China is managing the effects of the global crisis, and the optimism (and some nationalist sentiments) is consciously fuelled in the public debate.

Soon after the global crisis unfolded, and with impact on skilled and un-skilled employment felt even before that, China introduced a large stimulus package, of Rmb 4 trillion Yuan, \$586 billion over two years, by some calculations 12 % of 2008 GDP (or 6 % on annual basis).²⁷ Most commentators agree that the real size of the package is less clear than the precise figures in Yuan suggests.²⁸ First, there are doubts about how much of the money is new money, or public funding that had been committed earlier (including for reconstruction after the May 2008 earthquake in Sichuan). Second, the package is not entirely a financial injection from the central government, as central funding is matched by contributions from (semi-) private sources and lower-level government (World Bank, June 2009). Given the decline in value of assets associated with the global crisis, an injection of 6 % of GDP (on annual basis) may in itself not be sufficiently large to stabilize the economy. But an immediate impact was undoubtedly felt,²⁹ with a possible slowing down of the economy in August.

At the same time a range of other economic measures were introduced: reduction in taxes, changes in value-added tax rebates to promote exports (previously used to slow down the economy), a loosening of credit (according to some possibly leading to a bubble, and followed by reductions in lending mid 2009), and measures to stabilize housing and stock markets. Finally, the value of the (pegged) Rmb has been subject of much discussion, and even though the Rmb has appreciated over the last couple of years, its current level is still thought to be relatively low, supported by China's interventions to support the dollar, and contributing to promoting China's export. And around the Chinese New Year, people were offered vouchers for purchase of consumer goods.

The stimulus package has had a heavy emphasis on investment. This is understandable given the need to insert money into the economy quickly, and as investing in infrastructure of

²⁷ This would reduce China's reserves but still keep them well out of the red. China's current account balance was 10 % of GDP in 2008, and expected to decline to 7-8 % in 2010 and 2011. China's GDP was 28 trillion Yuan in 2008. Its ratio of public spending to GDP is low by international comparison, but such comparisons are very difficult.

²⁸ http://www.nytimes.com/2008/11/10/world/asia/10china.html?_r=2&hp&oref=slogin

²⁹ http://www.businessweek.com/globalbiz/content/apr2009/gb20090422_793026.htm

course has been one of the strengths of China's economic model. But this emphasis also came under criticism. Some noted that the country appears over-built already. China's growth model already has been skewed heavily towards investment (more than half of GDP in the decade), while households are saving about a quarter of their disposable income and private consumption is only about one-third of GDP.

The positive economic impact of investing in infrastructure is likely to be only temporary as this would promote supply and not demand. In the past, according to Du Yang (2008), physical investments has proven to have an insignificant effects on increasing employment. While investment growth in the first half of 2009 was over 30 per cent, increases in sales of (industrial) goods were negligible. Some have argued that investments surged into high-polluting and energy intensive projects.³⁰

At the same time, the government promised more than just more of the same in infrastructure. Reinforcing the belief in China's continued economic growth, and continuing to show leadership during crisis, Hu Jintao stressed: "Crisis creates opportunities, and we shall put more efforts in technological upgrading, and build up technology reserves for the future" (China Daily, June 30, 2009). The crisis has been seen or presented as an opportunity to invest in long-term objectives of skill development and green technology (but is likely to be challenged to absorb larger numbers of workers in the rural sector).

The stimulus package also contained much promises for social sectors, though too little for many commentators,³¹ and some argued that the investment in hard-ware might even reduce access to for example health care facilities (because of institutions' incentives to recover costs). It seemed the government over time responded to criticism by increasing or highlighting the commitments to social spending. In January 2009 the government announced spending of 123 billion to promote a universal health care system. Education, particularly vocational training and education of migrant workers was emphasised, for example, during the China Development High Level Forum in March 2009 (China Daily, March 21-22, 2009).

The directions for China's social policy post-crisis are not fundamentally different from those of the past, with some of the labour regulation in factor going in reverse (at least temporarily). There is thus much continuity, so far, driven by "apart from the fiscal reserves which enables the stimulus" the immediate government response, its perception of the close link between economic policies and a "harmonious society" and its tradition of learning-based and pragmatic reform (Zhang et al. forthcoming). The 8 % economic growth target continues to be central to social and economic objectives, social spending continues to be low, and weak social insurance and unemployment system can only be reformed in the medium term.

The expansion of services and slow but gradual universalisation of health and (primary) education was initiated well before the crisis. The investment in health services

³⁰ <http://www.eeo.com.cn/ens/feature/2009/07/10/143395.shtml>.

³¹ For example, Tang Min argued that funding for social welfare should go up to 35 % of government revenue (see the new CDRF report, quoted in China Daily, 3 April 2009). Guan Xinping suggested the government needs to invest more to educate and train youth and unemployed, speed up establishment of basic social security system, and strengthen public services (China Daily 24 June 2009). Ding Yuanzhu of CASS argued for creating of effective social demand permanent cure for crisis (China Daily 24 June 2009).

post-crisis in particular are made possible by the previous very cautious health reform, which have set in place the infrastructure which now allows absorption of increased funding. While the crisis brought concerns about conditions in rural areas (and probably a realisation that the envisaged rural-urban transition is likely to slow down considerably) it also merely reinforced the efforts over the last years to improve conditions there. These aspects are not likely to change ó yet there are some important differences.

China's stimulus package

	bln. Yuan	% of total package
Public infrastructure	1500	38
Earthquake reconstruction	1000	25
Social welfare	400	10
Rural development	370	9
Technology advancement	370	9
Sustainable development	210	5
Educational and cultural	150	4
TOTAL	4,000	

Source: NDRC March 2009; http://www.eeo.com.cn/ens/finance_investment/2009/03/07/131626.shtml

6. Is the crisis a turning point?

China's economic and societal models are directly linked to the form of political control, with legitimacy directly contingent upon continued improving well-being and continued growth (i.e. the 8 % growth target). During the crisis, and under the political pressure of the Chinese developmental state, links between economic and social policies are reformulated. The way this evolves in China not only will have an enormous impact on hundreds of millions of its citizens, particularly those that have recently escaped from poverty and those still suffering from chronic poverty, but also will have an impact on the global economy and will be cited as an example for the global South of the potentials to manage the fluctuations of the global economy.

Three aspects of the government's response suggest there is a turning point in China's development policies ó and crucially for the argument in this paper the three are inter-related. First, the global financial system is of considerable concern to China, and its strategy unlikely to be the same as in the past. While it is argued in China (as elsewhere; e.g., Stiglitz 2009) that the financial crisis was the fault of the US, China's accumulation of reserves was a considerable part of the system that fuelled the US's borrowing. Calls for an alternative reserve currency may be more symbolic than likely to be reality in the near future, but the new interdependence has been clearly demonstrated by the US's efforts to reassure Chinese partners of the safety of their deposits. The crisis did not cause this inter-dependence ó globalisation since 1978 has ó but it has made it remarkably clear, and helped to fuel much nationalism in China.

Second, the crisis has highlighted to China that its export-model of growth ó which started in the early 1990s and was reinforced after 1997/98 ó is no longer sustainable (Song Li 2009), not only because levels of demand will not return, but also because of shifting

production. The realisation was evident in the earlier efforts to slow down the export economy, and in some of the responses it seemed as if economic policy makers were already prepared for such a reversal, and that a new economic strategy could be the inevitable complement of its harmonious society. The optimism shown by China's leaders is of course political, but so far the strategy seems to hold.

Logically following this, third, is the emphasis on the promoting domestic consumption. While the expansionary fiscal policy has a strong focus on infrastructure, currently there is much more strongly felt the need and opportunity to expand social services, for which the foundations have been laid over the last few years. The next years will show whether China will be able to implement the necessary social policy instruments, under relative favourable fiscal conditions, and a nascent social policy system which *may be* able to absorb the kinds of new funding that is required, with the *potential* to enhance equality or at least halt the rapid rise of inequality of the last two decades, and with the *possibility* that this brings drastic changes to the current systems of by and large regressive fiscal transfers.

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