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**China:
Prospects for full employment**

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Foreword

This paper by Dr. T. Rawski of the University of Pittsburgh provides an up-to-date picture of employment developments in China. He points to China's extremely high rates of growth in recent years and the massive amounts of structural change this has involved. At the same time the reform process, which has been hesitant, is only gradually encouraging the development of a market economy. Unexpected outcomes of the reform process have been conspicuous in the labour sphere, taking the form of steep employment growth in township and village enterprises, a large contribution most recently of private enterprise to incremental job creation, the flight from farming and finally urban lay-offs. In that last respect, China is reflecting the experience of European, formerly centrally planned economies. As in those countries, but in a far less tragic manner, employment relations are changing and far greater flexibility on the one hand, but insecurity for some on the other, is being introduced. However, China is still very marked by an urban-rural divide demonstrated by the illegality of much rural-urban migration.

Dr. Rawski sees a conflict between the desire of China's leaders to absorb the increasing number of open unemployed, whose numbers are much understated by official data, and China's longer term objectives. Current short-term policies are postponing the separation of government from business, especially in the banking sector. China's longer term prospects should lie in the direction of giving greater encouragement to private enterprise and avoiding financial market repression. This should be linked to a strong effort to reduce the current urban bias and to produce a "level playing field" for urban and rural economic activity.

This paper was commissioned as part of ILO's efforts to take stock of the progress of national commitments towards the promotion of full employment entered into at the World Summit for Social Development (Copenhagen, 1995).

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I. Introduction

During the past two decades, China has enjoyed the fastest growth of any major nation. This prolonged growth spurt has brought massive gains in every aspect of material welfare. Rapid expansion of job opportunities and maintenance of high levels of employment are prominent aspects of China's long boom that now appear endangered. Chinese sources tell of mass layoffs, large-scale urban unemployment, and backlogs of surplus rural labour. What are the circumstances surrounding the world's largest national labour force? This report surveys China's prospects for full employment.

Chinese reform is characterized by gradualism and experimentation. Chinese policies and institutions differ widely from orthodox prescriptions of liberalization, deregulation, and privatization known as the "Washington Consensus." Broad agreement on the objective of creating a market system is itself an outcome of the reform process that appeared only in the 1990s.

China's reform has produced many surprises. Unexpected outcomes are particularly notable in the labour sphere, where reform has both created and extinguished immense amounts of employment. The biggest contributions on both sides of the ledger: steep employment growth in township-village (TVE) enterprises, large contributions of private enterprise to incremental employment, flight from farming, and, most recently, mass urban layoffs, are unanticipated consequences of reforms that did not target employment or labour markets.¹

Although official plans and "approvals" retain great influence in China's semi-market economy, recent history demonstrates that the forces impinging on employment outcomes extend beyond the control and understanding of policy-makers.

II. Overview of Chinese labour markets

Demographics

Tables 1-4 summarize basic information on population, employment, and unemployment since 1980. A nation-wide regimen of population control, which generally limits urban families to one child and rural households to two, has achieved a gradual, but irregular decline in the rate of natural increase, which is now approaching one per cent (Table 1). During the past two decades, labour force growth has considerably outpaced demographic expansion, raising the participation rate from 43 to 56 percent between 1980 and 1997 (Table 1). In international terms, these figures

¹Main elements of current reform include: restructuring of small and medium state-owned enterprises under the slogan "retain the large state enterprises and release the small ones" (zhuada fangxiao), continued furlough of surplus workers and other reforms aimed at resolving long-standing difficulties in the state enterprise sector by the year 2000, efforts to reform and recapitalize the four huge state-owned banks, a housing reform that gives urbanites the choice of purchasing their apartments at concessional prices or paying sharply higher rents, sweeping administrative consolidation that has eliminated numerous central government ministries and promises large reductions in the national-level civil service, and an unprecedented effort to end the involvement of military units in business operations and to curb corrupt practices within various police and military organizations.

are unusually high (Hu Angang 1998). They reflect an age structure that is “highly conducive to rapid economic growth,” with a high proportion of working-age adults and relatively low proportions of dependent children and seniors (Banister 1996). Demographic projections indicate that this circumstance will continue for several decades (Li Yining et al 1994, p. 55). These forecasts also show (and recent developments confirm) that past concerns with absorbing new labour-force entrants will give way to focus on employing adult workers and providing for a growing elderly population.

Table 1. Basic data on population and employment, 1980-1997 (millions)

	1980	1990	1997	Annual growth rate 1980/97
1. Population	987	1143.3	1236.3	1.33
2. Increase %	1.19	1.44	1.01	
3. Labour force	423.6	639.1	696	2.96
4. Urban formal employees	104.4	140.6	146.7	2.02
5. Labour force composition				
5A. Primary	291.2	384.3	347.3	1.04
5B Secondary	77.1	136.5	165	4.58
5C Tertiary	55.3	118.3	183.8	7.32
Shares (per cent)				
Participation rate (3÷1)*100	42.9	55.9	56.3	
Female workers	43.4	45	45.7*	
Primary (5A÷3)*100	68.7	60.1	49.9	
Tertiary (5C÷3)*100	13.1	18.5	26.4	
Secondary (5B÷3)*100	18.2	21.4	23.7	
Sources: Survey 1998, pp. 30-34; Labour 1997, p. 15; Women 1991, p. 2390; Women 1998, pp. 322-323.				
* data for 1995				
Note: Primary sector: agriculture, forestry, animal husbandry, and fisheries. Secondary sector: mining and quarrying, manufacturing, utilities, and construction. Tertiary sector: transport, communication, commerce, services, culture, entertainment, social services and all other activities excluded from the primary and secondary sectors (See Labour 1997, p. 589; Survey 1998, p. 168).				

Overstatement of farm employment is associated with understatement of the non-farm work force in construction, transport, and trade. For example, information from urban and rural budget studies suggests that actual 1992 employment in retail sales of food beverages, and tobacco could easily amount to seven times the figure of five million workers reported in China's 1992

census of the service sector (Rawski and Mead 1998, p. 775).

These errors are not widely recognized. Studies of productivity and income distribution continue to use the standard figures. Hu Angang's comprehensive summary dates the decline in farm labour from the 1990s, posits an annual outflow of five million farm workers, and cites Zhou Qiren's conclusion that the annual influx of rural migrants into China's towns and cities is five million (1998a). This picture seems to misstate the timing as well as the scale of labour outflows from farming, particularly in light of reports indicating rates of net departure from farm work as high as 6.9 per cent in 1993 and 9.3 per cent during 1992/93 (Chen Zhiping 1994).

Whatever the exact figures, unrecorded exodus from farming and large-scale migration to the cities have two important implications for the present study. First, references to vast backlogs of surplus rural labour (figures of 100-130 million or more are often mentioned - e.g. Quan 1996, Challenges 1997), appear considerably exaggerated. Second, statements about China's retarded development of labour markets and the "failure" of labour reform (e.g. Korzec 1992) overlook the smooth transfer of enormous numbers of farm workers into new occupations, a phenomenon that indeed amounts to the largest migration in human history, and one mediated almost exclusively through spontaneous market mechanisms.

Formal employment

During the period 1980-1997, urban formal employment, designated by the term *zhigong*, which (until recently) carried the implication of tenure, rose at an average rate of 2 per cent, or slightly less than annual labour force growth, which averaged nearly 3 per cent (Table 1). Table 2 presents an enlarged total of formal employees that includes workers in rural township and village enterprises (TVEs), who are sometimes (e.g. Village Yearbook 1997, p. 327) but not always (e.g. Labour 1997, p. 401) described as *zhigong*, meaning formal, regular, or permanent employees. Explosive growth pushed the TVE workforce ahead at an annual rate of 9.2 per cent during 1980-1997. The enlarged total of formal employees achieves annual growth of 5.2 per cent, far larger than the corresponding labour force totals.

Table 2 provides data on urban employment. These data present a number of problems. First they represent a wider category than that given in Table 1, ie. *congye renyuan* rather than *zhigong*. *Congye renyuan* might be translated as gainfully employed. Second in the statistical source from which the data in Table 2 are taken the components do not add up to the total. However, the first three components of urban employment in Table 2, ie. state, collective and other tally exactly with the data in Table 1 for 1980 and 1990 and diverge slightly for 1997. Presumably a distinction is being drawn on the basis of contractual status between public and private sector workers together with some uncertainty shown on the number of the latter.

Table 2. Formal employment, 1980-1997 (millions)

	1980	1990	1994	1995	1996	1997
State	80.2	103.5	112.1	112.6	112.4	110.4
Collective†	24.2	35.5	32.8	31.5	30.2	28.8
Other	0	1.6	7.6	8.9	9.6	11.1
Private	0.8	6.7	15.6	20.4	23.3	26.7
Urban	105.2	166.2*	184.1*	190.9*	198.2*	202.1*
TVEs ‡	30	92.6	120.2	128.6	135.1	135.1#
Total	135.2	258.8	288.3	302	310.6	312

† Urban collectives ‡ Township and village enterprises (*xiangzhen qiye*)

* total exceeds sum of components; source provides no explanation for this discrepancy.

assumed unchanged from 1996. A Ministry of Agriculture official reports that TVE industry's 1997 "absorption of surplus rural labour declined by 4.58 million" persons from 1996 achievements, suggesting a small rise (Jiang Yongtao 1998, p. 9). However there are also reports of layoffs: "Last year [i.e. in 1997] 4.58 million workers in rural industries were laid off and went back to the fields" (Chen Chunmei 1998, p. 2).

State sector: firms "owned by all the people" (*quanmin suoyouzh*) and responsible to the central government. Many state firms operate under the direction of provincial or city governments.

Collective firms (*jiti suoyouzh*), like state firms, are part of the public sector (e.g. Bing LAN 1998). They report to local authorities rather than to the central government. The collective sector includes urban enterprises and rural firms, known as "township and village enterprises" or TVEs, that operate under the supervision of local governments in rural areas. Firms outside the state and collective sector are often combined into the heterogeneous category of "Other" ownership (*qita suoyouzh*). This table breaks this category into two components:

Other: joint enterprises (e.g. domestic joint ventures between state and collective or state and private entities); shareholding enterprises (including firms listed on Chinese and overseas stock exchanges); firms with partial or full foreign ownership; and a small miscellaneous category.

Private: domestic private firms including "private" firms with 8 or more employees and smaller "individual" firms.

Sources: Survey 1998, p. 32; Labour 1997, p. 401.

In the early 1980s, excess demand in formal labour markets pulled millions of workers from China's farm economy even as rural reforms reduced long-standing income differentials favoring urban workers. During the past decade, continued excess demand, now reinforced by renewed expansion of the urban-rural income gap, produced increasing labour flows into cities and towns, leading Chinese authors to write of a "human tide" of migrants.

The data in Table 2 suffer from two shortcomings. First, workers, who are furloughed or laid off (*xiagang*) without being formally dismissed are counted as "employees" even though they may be partially or completely idle. These layoffs, discussed below, mainly affect the state sector. The number of workers in this category, which emerged during the early 1990s, rose from 3 million (1993) to 9 and 12 million in 1996 and 1997 (Hu Angang 1998a, Table 1). At the same time, urban industrial enterprises, again mainly in the state sector, employ large numbers of rural migrants as temporary workers. These migrants are paid much less than regular employees, receive few or no fringe benefits, and appear to be omitted from standard compilations of employment and wages. Figures for the 1990s appear to overstate actual formal employment by a small, but

growing amount. The margin of error, however, remains modest - if we ignore the temporary workers and assume that none of the 12 million workers on furlough (*xiagang*) at the end of 1997 was dismissed, that half were re-employed, and that half remained completely idle, the resulting (generous) error margin would amount to only 2 per cent of the 1997 formal employment total shown in Table 2.

If the totals in Table 2 are roughly accurate, we can use them to analyze patterns of labour absorption. Table 3 contains figures for labour absorption in various segments of formal employment calculated as percentages of increments to the national labour force. The residual of labour force increments that are not matched by increases in formal employment, is assigned to the “informal sector,” which includes self-employed farmers and unemployed persons as well as casual workers.

Table 3. Contributions to labour absorption, 1980-1997

	1980/90	1990/94	1994/95	1995/96	1996/97
Labour force increment (millions)	215.5	32.9	7.5	9	7.5
Absorption (Per cent)					
Formal sector	49	147	183	96	19
State	11	26	7	-2	-27
Collective	5	-8	-17	-14	-19
Other	1	18	17	8	20
Private	3	27	64	32	45
TVE	29	84	112	72	-1
Informal* sector	51	-47	-83	4	81

Source: Calculated from Survey 1998, p. 32 and Tables 1 and 2.

*Residual, including self-employed farmers and unemployed workers.

Table 3 provides a clear overview of changes in China's national labour market. There are three distinct periods:

- (iii) During the 1980s, formal employment absorbed half of the labour force increment, with new positions in TVE firms and in urban formal employment each equivalent to roughly one-fourth of the labour force increment.
- (ii) During the first half of the 1990s, expansion of formal employment jumped far ahead of labour force growth.
- (iii) Conditions changed abruptly after 1995, as a gradual slowdown of domestic growth, exacerbated in 1997 by the Asian financial crash, slashed the demand for new workers. The annual increment to formal employment plunged from 13.7 million in 1994/95 to 8.6 and 1.4 million in 1995/96 and 1996/97. With downsizing continuing in China's central government, state enterprises, and urban collectives (First Quarter 1998, p. 6) and with TVE as well as state-sector firms choked with surplus workers (see below), virtual stagnation of formal employment will continue for some time. Hu Angang (1998b) predicts

that open unemployment in China's cities will reach 8-9 per cent in 1999.

Table 3 also highlights the surprising emergence of China's embryonic private sector as a major source of formal employment growth during the 1990s. China's formal private sector remains small, accounting for 2.6 per cent of formal employment in 1990 and 8.6 per cent in 1997. Its impact on employment growth, however, is far larger. The figures show that new formal employment in officially-registered domestic private enterprises (including "individual" enterprises with fewer than eight employees and "private" firms with eight or more workers) accounted for 37.6 per cent of incremental formal employment at the national level during the years 1990-97. If we limit the comparison to new urban formal employment, the share of the domestic private sector rises to an astonishing 55.7 per cent. The data show that China's domestic private enterprises added more workers during 1995/97 than the combined total for state, collective, and TVE firms. With some private enterprises "reluctant to register ... for [fear of] ... being taxed" (Zhu Qiwen 1998) and others disguised as urban or rural collectives, these very large figures surely understate the contribution of domestic private undertakings to Chinese job creation in the 1990s. Despite its small size, the formal private sector evidently deserves careful attention in the making of Chinese employment policy.

Unemployment, furloughs, and surplus labour

The sudden and unexpected slowdown in formal job creation, which coincides with reform-induced downsizing in industry, commerce, government, banking, railways, and the military, has propelled unemployment to the forefront of Chinese policy concerns. Official data on unemployment appear in Table 4. These figures show the proportion of registered urban residents whom local labour bureaus have identified as jobless. They make no provision for unemployment among persons who do not hold urban residence permits (*hukou*). Short- and long-term migrants who have moved into urban areas are excluded from both the numerator and denominator of official unemployment rates.

Chinese researchers have shown that the standard figures underestimate open unemployment among registered urban residents by a large and growing margin. The State Statistics Bureau's surveys indicate that the actual rate of urban unemployment was 3.5 and 4.0 per cent in 1994 and 1995 (vs. published rates of 2.8 and 2.9 per cent; see Song 1996). The reason: the official figure "comes from looking only at people who register as unemployed with the labour departments" (Quan 1996).

Table 4. Official and alternate figures on urban unemployment, 1980-1997

Year	Number (millions)	Youth unemployment (%)	Official data		
			Urban unemployment rate (%)		
			Official data	Alternative data	
				*	**
1980	5.4	70.6	4.9		
1990	3.8	81.6	2.5		
1991	3.5	81.9	2.3		
1992	3.6	82.4	2.3		
1993	4.2	79	2.6	3.3	3.7
1994	4.8	63.2	2.8	3.6	4.1
1995	5.2	59.7	2.9	4	4.7
1996	5.5	--	3	4.9	5.9
1997	5.7	--	3.1	5.7	7

Source: Survey 1998, p. 36; Hu Angang 1998a, Table 1.

Note: Alternative estimates of urban unemployment include furloughed workers, who are not included in the official figures of urban unemployment.

* assumes that 60 per cent of furloughed workers have obtained new jobs.

** assumes that 40 per cent of furloughed workers have obtained new jobs.

Prior to 1995, urban unemployment was concentrated among young school-leavers. “Awaiting employment,” the Chinese euphemism for joblessness, accurately described the behavior of many youths who remained idle in the hope of obtaining advantageous opportunities in the state sector.

Recent developments have altered both the scale and the character of urban unemployment. For many years, officials pressed enterprises to employ excessive numbers of workers in order to provide the entire urban populace with jobs and associated benefits (housing, medical care, etc.). This practice of labour hoarding continued well into the reform period. The cumulative result was an accumulation of surplus employment widely thought to encompass as much as 30 per cent of the work force in state industry as well as lesser, but substantial elements of the work force in collective, TVE, and even foreign-linked firms (Overview 1996, p. 12). Official resistance, social pressures within enterprises, and long-standing taboos against layoffs prevented the dismissal of redundant workers even after the 1992 regulations for the operation of state enterprises that specifically delegated control of the work force to enterprise managers (Regulations 1992, pp. 30-31). A succession of policies identified surplus workers and attempted to shift them to alternate employment without necessitating layoffs. These practices include shunting redundant workers into subsidiary enterprises (typically hotels, restaurants, and other service establishments), creating “labour service companies” that seek external markets for unneeded labour, and the sale of land-use rights to finance employment-creating diversification or expansion projects. These efforts continue, but the repertoire of Chinese managers has expanded to include a new alternative: large-scale furlough of redundant workers.

Soon after 1990, local governments in regions where rapid growth provided ample employment opportunities allowed managers to attack the redundancy problem by sending unneeded workers home at greatly reduced pay. This new policy, known as “furlough” (*xiagang*), sharply reduced the incomes of affected workers without severing ties to their employers. Workers subject to *xiagang* remain on the rolls as “employees” (*zhigong*); they retain access to employer-provided housing and eligibility for social benefits linked to the workplace. The actual package of compensation and benefits provided to workers undergoing *xiagang* varies widely. Furloughed workers receive cash payments amounting to a modest fraction (typically below 50 per cent) of normal wages. Arrears are not unusual. Access to fringe benefits is often truncated: instead of full payment for medical costs, furloughed workers (also active workers, especially in loss-making enterprises) may be expected to pay their own expenses in anticipation of partial, often delayed reimbursement.

The new practice of furlough represents a sort of on-the-job layoff. *Xiagang* encourages redundant workers to seek alternative employment without subjecting them to outright dismissal. Large-scale furloughs appeared in Shanghai, the apparent leader in this new practice, in 1993 (Shanghai 1998, p. 100), and spread rapidly to other jurisdictions. By 1996, furloughs had emerged as a major feature of the national labour scene. As often occurs in China, implementation was far from uniform: representatives of the (heavily overmanned) Anshan steel complex did not utter the word “*xiagang*” in three days of interviews during May 1997.

Hu Angang has compiled revised estimates of urban unemployment that include furloughed workers. Hu provides alternate totals by assuming that either 60 or 40 per cent of furloughed workers are re-employed (Table 4). Hu’s figures, which still cover only registered urban residents, are clearly preferable to the official data. The gap between the two measures of urban unemployment has expanded rapidly during the past 5 years. By 1997, urban unemployment had risen to approximately 6 per cent, or twice the official rate, with further increases apparent during 1998. Even these figures may be too low: about 7 million people were idled by the full or partial closure of enterprises in 1995 (Quan 1996); the number affected by plant closures has surely increased since then. All of these figures exclude involuntary idleness among persons classified as rural residents, including short- and long-term migrants located in China’s cities and towns.

Emergence of large numbers of furloughed workers, who now account for half or more of urban unemployment, has altered the composition of jobless urban workers. Compared to the registered unemployed, furloughed workers are older, less well-educated, and predominantly female. Observers comment on the “two highs” (age and female proportion) and the “two lows” (education and technical skill) among furloughed workers (Yang Jingbo 1996). The concentration of women workers among those selected for furlough is widely remarked: women accounted for 42.0 per cent of 1996 formal employment in mining, manufacturing, and utilities (Labour 1997, pp. 16, 21); according to a large-scale 1996 survey, the proportion of women among furloughed workers, most from industry, is 59.2 per cent; in Shanghai, 68.9 per cent of *xiagang* personnel are female (SSB 1997; Shanghai 1998). The 1996 survey showed that only 11 per cent of furloughed workers are under 25 years of age.

Chinese unemployment may be divided into three categories:

Cyclical unemployment was unknown in pre-reform China. Under China's pre-1978 plan system, new entrants into the labour force became members of local people's communes (in rural areas) or were assigned to (mainly urban) work units (*danwei*). There was little choice for employers or workers. The matching of workers and units was bureaucratic, mandatory, (mostly) permanent, and largely unrelated to preferences, productivity, or financial outcomes. This system had obvious defects. There was one offsetting benefit: a near-zero level of cyclical unemployment.

Gradual expansion of market forces has introduced Keynesian unemployment to China's economy. Growing involvement in offshore markets creates employment when exports boom, but extinguishes jobs when sales decline. Increasingly commercial patterns of domestic behavior have the same effect. Big regional differences in employment opportunities illustrate the growing interaction between aggregate demand and the (formerly administrative but increasingly market determined) demand for employment. Shanghai officials allowed local firms to shed workers because they (correctly) anticipated that most affected workers could find new employment in the dynamic local service economy. When competitive forces brought furloughs to rust-belt cities in China's northeast region, the result was an increase in what might be called "transition unemployment."

Transition unemployment, a phenomenon unique to economies undergoing systemic transformation, is the result of institutional change that devalues the contribution of workers formerly regarded as productively employed. Until recently, governments at all levels pressured enterprises to employ workers whose contribution to profit was zero or negative. Even after profit-seeking came to dominate managers' concerns, lingering socialist taboos insulated millions of redundant employees from market forces. By the mid-1990s, when managers acquired genuine power to dismiss surplus workers, the backlog of redundant workers had grown large. Chinese writers routinely indicate that roughly 30 per cent of the 40-odd million workers in state industry are superfluous (Survey 1998, p. 34); Hu Angang cites 1996 figures identifying 22 million (just over 20 per cent) of the work force in state and urban collective enterprises as redundant (1998a, p. 11). TVE enterprises suffer from similar difficulties: surveys in Suzhou (Jiangsu province) indicate that enterprise restructuring is likely to reduce labour requirements by 23 per cent (Chen and Qian 1998, p. 8). Many workers remain trapped in enterprises that cannot meet the market test. The "Third Front" investment program, which sought to reduce China's vulnerability to external attack by establishing industrial facilities in remote locations, created many uneconomic firms. Under these conditions, removal of subsidies and/or restrictions on commercial behavior may suddenly create large pockets of joblessness. This sort of unemployment, which is essentially unrelated to the underlying balance between labour demand and labour supply, has no clear counterpart in market systems.

Structural unemployment arises from a long-term mismatch between the number and qualifications of workers and the availability of complementary resources. In China, as in other populous low-income nations, structural unemployment appears in rural areas with unfavorable man/land ratios, limited infrastructure, and low per capita levels of physical and human capital. As noted above, widely cited figures appear to massively overstate the dimensions of rural surplus labour. Ng et al (1998), cite numerous studies claiming that surplus workers amounted to 30-40 per cent of the rural work force during the late 1970s and 1980s; their own analysis, based on surveys of 60 Jiangsu and Sichuan villages covering 1978-92, assign a maximum of 4.35 per cent (Jiangsu, 1984) and 3.07 per cent (Sichuan, 1986) of village workers to the labour surplus category.

The demise of industries that were systematically overbuilt under the plan system of the 1950s-1970s and/or the undisciplined investment boom of the 1980s and early 1990s may reveal pockets of structural unemployment in China's cities. Areas of China's northeast, which developed a large industrial base under a series of domestic and semi-colonial non-market regimes dating back to the decade 1910-1920, face the greatest danger that the "transition unemployment" of the late 1990s may conceal more difficult issues of structural unemployment.

China's labour markets

Not surprisingly, large expansion of formal employment was accompanied by rapid growth of wages. Data on average money wages in urban formal employment and in TVE enterprises appear in Table 5. Among domestic enterprises, money wages are consistently highest in the state sector, where workers also enjoy the largest fringe benefits. Wages in the "other ownership" sector, which includes firms with foreign participation, have replaced state units at the top of the wage ladder. All categories show rapid growth of both money and real wages.

Table 5. Annual money wages for formal employees, 1980-1997 (current yuan)

	1980	1990	1995	1996	1997	Index for 1997 (1980=1)
1. State	803	2284	5625	6280	6747	8.4
2. Urban COE	623	1681	3931	4302	4512	7.24
3. TVE	398*	676*	3618*	4195	n.a.	10.54#
4. Other	n.a.	2987	7463	8261	8668*	n.a.
5. Price Index	100	203	392	427	440	4.4

Sources and notes:

* calculated from separate figures for wage payments and number of year-end employees

index is for 1996, taking the 1980 figure as 1.

Data for 1997 are from Survey 1998, pp. 35 and 39.

n.a = no data available

Line 1: Yearbook 1997, p. 123

Line 2: data for urban collective units from *ibid*.

Line 3: for 1996, TVE Yearbook 1997, p. 121; for 1995, Village Yearbook 1996, pp. 337, 340; for 1980 and 1990, TVE Yearbook 1987-87, p. 569.

Line 4: Yearbook 1997, p. 123. Wage data for formal employees in "other" ownership categories include individual, private, and shareholding entities, domestic joint ventures, and foreign-invested firms.

Line 5: index of urban retail prices from Yearbook 1997, p. 267; Survey 1998, p. 70.

Economists studying the Chinese labour scene cannot agree on the degree to which these data reflect market outcomes. Debate focuses on wage determination in state industry.

- Some see rising wages as evidence of continuing non-market behavior (e.g. Woo 1996, p. 164). On this view, which draws support from Chinese economists' complaints about excessive wage increases, wage escalation signifies a failure of labour discipline (e.g. Liu and Wang 1993; Lin Xiongbo 1994). Continued wage increases despite mass layoffs and falling consumer prices lend credence to this view (First Quarter 1998). At the same time, near-constancy of the ratio of money wage payments to gross output value in state industry – the ratio rose from 7.0 to 8.2 per cent between 1980 and 1995 – seems to undercut the

“wage indiscipline” argument.

- S** Chinese managers may use pay increases to raise the effort level of their employees. Furthermore, managers may authorize general wage increases to prevent the departure of key employees without creating socially divisive pay differentials. From this perspective, trends in employee compensation may reflect some sort of “efficiency wage” pattern.
- Dong and Putterman (1997, 1998) argue that state enterprises behave like labour-market monopsonists, hiring fewer workers than would be expected from participants in competitive markets. This perspective clashes with casual observation of overmanning and with widespread reports, noted above, that up to 30 per cent of state enterprise employees are redundant. The key empirical argument, panel data analysis demonstrating that the marginal cost of labour falls systematically short of labour’s marginal product, appears to underestimate non-wage labour costs. Enlarging labour costs to include a plausible estimate of the present value of pension rights (see World Bank 1997), for example, might reverse the conclusion that marginal revenue product exceeds marginal labour costs, effectively demolishing the monopsony interpretation.

Despite these disagreements, considerable penetration of market forces is evident even in the conditions surrounding employment in China’s state sector:

- insecurity has risen sharply with the effective abolition of employee tenure.
- turnover has expanded rapidly. Job mobility is particularly evident among young workers with high levels of education. In the state sector, annual separations, which fluctuated between 1.5 and 2.3 million during the 1980s with no upward trend, nearly tripled to 6.5 million (or 5.9 per cent of the work force) between 1990 and 1996 (Labour 1991, p. 321; Labour 1997, pp. 18, 290). The 1996 total, which excludes the (large) state-sector component of 12 million furloughed workers, amounts to 5.9 per cent of the year-end state-sector work force (Labour 1997, p. 18). A study by the State Statistics Bureau reports that in 1995, 11.93 million workers “left jobs in one unit to move to another, making a turnover rate of 8 per cent” for a large, but unspecified universe of 149 million (Overview 1996). This separation rate begins to approach levels observed in market economies. (Abstract 1995, p. 419).
- researchers find that reform has created links between profitability and compensation (e.g. Rawski 1994). Earnings are increasingly linked to group (if not individual) effort.
- ongoing reforms in such areas as housing, health care, and pension funding have produced slow but important progress in “unbundling” employer-worker relations. There is clear movement toward simplified employment relations based on the exchange of labour services for money wages.

To summarize: formal employment outpaced labour force growth throughout the reform era before falling abruptly after 1995. The locus of new labour demand has shifted from the state enterprises to rural collective (TVE) firms and, most recently, to the private sector, which has suddenly emerged as the primary source of new employment. Despite the obstacles posed by long-established institutional arrangements surrounding urban employment, pressures arising from the liberalization of commodity markets have resulted in a gradual commercialization of the (derived) demand for labour even within China’s state sector. Once we look beyond the state sector, it is evident that the majority of Chinese workers, including virtually the entire rural populace, face labour markets imbued with important “free market” characteristics including high degrees of mobility, flexible wages and employment terms, etc. In general, the extent of market arrangements seems considerably greater than expected. As noted above, unregulated markets have mediated the transfer of vast numbers of workers from farming to a variety of industrial and service occupations. The process is so smooth that as many as 100 million transferees have escaped the notice of China’s statistical agencies. China’s wage system begins to display familiar market-

economy phenomena, including education-based income differentials (previously notable for their absence; see Li Weizuo 1998) and gender wage gaps (Maurer-Fazio et al, forthcoming).

III. Determinants of market evolution and employment outcomes

After two decades of reform, employment outcomes for China's immense work force primarily reflect market forces rather than government decisions. The relative importance of market influences will continue to increase. In a context of growing market influence, the central government's multiple objectives, limited fiscal and political resources, and relative inattention to affairs outside the cities (where the majority of the labour force lives and works) mean that the main impact of official actions on employment outcomes will arise from the labour-market consequences of general economic policies and structures. We begin with general policy arenas that appear particularly important for labour market outcomes, and move on to a brief review of policy affecting specific sectors.

Labour-market consequences of general economic structures and policies

Relative price structures. Chinese sources, echoed by some international writers, often refer to a historic policy of "low wages" for urban workers (e.g. Wang Dongjing 1995, p. 16; Selden 1995, p. 205). Such discussion is more reflective of the aspirations of urban residents than of economic realities. In a study focused on the year 1987, Jefferson and Rawski found evidence that "distorted factor prices encourage managers at all levels to use machines and materials to replace workers" (1992, p. 62). They found that wage-rental ratios and wage-electricity cost ratios uniformly higher for China than for India. In extreme cases, the Chinese wage-rental ratio exceeded comparable figures for the United States.

Steep wage increases during the past decade (Table 5) have not outpaced labour productivity: as noted above, the ratio of wage costs to gross output in state industry has hardly changed over two decades. Non-wage labour costs remain high, particularly in the state sector, for former state firms now restructured as shareholding corporations, and in firms with foreign investment. Ongoing reforms in the areas of housing, pensions, and health care hold the promise of reducing the social burdens previously assigned to employers of urban labour.

The cost of capital, including depreciation and interest costs, remains low. Depreciation ratios continue to reflect physical deterioration of assets rather than economic obsolescence. Unpublished data from China's State Statistics Bureau show low ratios of depreciation to original value of productive fixed assets. For state industry, the ratio rises from 5.1 to 6.1 per cent between 1985 and 1996. For collective industry (excluding village-level units) the ratio declines from 7.6 to 6.8 per cent during the same period.

The long-standing policy of maintaining low interest charges and channeling loans to favored borrowers (mostly in the state sector), draws sharp criticism from Chinese economists (e.g. Xie Ping 1992). Bank authorities hesitate to hike rates because higher interest charges threaten the solvency of heavily indebted state enterprises and, by reducing profits, threaten government fiscal revenues as well (Zeng Kanglin 1994). Table 6 provides a crude but effective measure of real interest rates by subtracting the inflation rate for industrial goods from nominal interest charges on 3-5 year industrial loans. There is a clear cyclical pattern: real rates turn

strongly negative during years of peak inflation (1988, 1993) and turn positive as inflationary pressure is quelled (1990, 1996/97). The long-term trend of real rates emerges from the five-year moving average compiled in Table 6 and Figure 1. The moving average shows an increasingly steep trend. Even so, real rates have been low: the five-year moving average of real rates remains negative in nine of 11 years from 1985.

In addition to cheap rates, privileged borrowers, especially state enterprises, frequently delay or avoid repayment. “Some large state-owned enterprises delay paying off loans because of their own poor performance and national banks can impose few restrictions on them.” This is because national leaders continue to insist that the banks “need to provide money-losing enterprises with a revolving line of credit” as part of “a greater effort to free State-owned enterprises from their present difficulties” (*China Daily* 5 September 1998, p. 4 and 27 June 1998, p. 3).

Figure 1. Chinese real interest rates, five-year moving average, 1982-1996

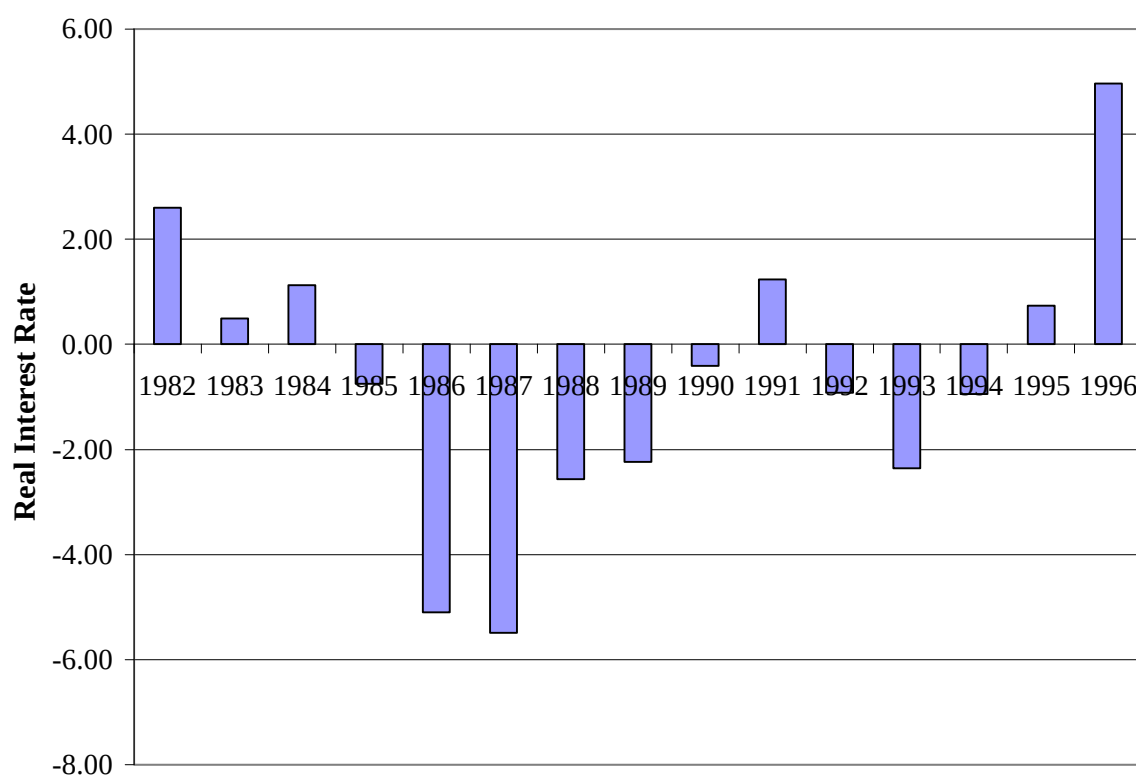


Table 6. Interest rates and inflation

	Interest rate	Inflation rate	Real rate of interest	
			Annual rate	Five year moving average
1980	5	2	3	
1981	5	6.6	-1.6	
1982	6.5	3.5	3.0	0.52
1983	6.5	4.1	2.4	0.1
1984	6.5	3	6.2	0.23
1985	9.4	16.9	-7.5	-0.15
1986	9.4	7.7	1.7	-1.02
1987	9.4	15.8	-6.4	-1.1
1988	9.4	28.7	-19.3	-0.51
1989	14.4	10.2	4.2	-0.45
1990	11.2	4.1	7.1	-0.08
1991	9.5	6.2	3.3	0.25
1992	9.5	6.8	2.7	-0.18
1993	12.9	24.0	-11.1	-0.47
1994	12.9	19.5	-6.6	-0.19
1995	14.8	14.9	-0.1	0.15
1996	13.3	2.9	10.4	
1997	10.8	-0.3	11.1	
1998	9	-1	10	
1980-97	9.8	9.7	0.1	
1980-89	8.1	9.6	-1.4	
1990-97	11.9	9.8	2.1	
1980-84	5.9	3.3	2.6	
1985-89	10.4	15.9	-5.5	
1990-94	11.2	12.1	-0.9	
1995-97	13.0	5.8	7.1	

Sources: for 1980-88, Jefferson and Rawski 1990, Table A-1, which uses nominal interest rates for 3-5 year fixed asset loans and inflation measures based on World Bank figures for industrial goods sold at market prices.
For 1990-97, nominal interest rates from Lardy 1998, p. 108, using figures for 3-5 year capital construction loans and averaging quotations for years with multiple rates; inflation measured by the index for ex-factory prices of industrial goods from Yearbook 1997, p. 283 and Survey 1998, p. 70.
Data for 1997 are estimates.

Prices of energy and materials are now much closer to international levels than was the case a decade ago. Nonetheless, price concessions favoring large-scale (and typically capital-intensive) industries continue. Electricity rate schedules for 1993, for example, reveal price concessions favoring large-scale (i.e. capital-intensive) industries. Customers of the Northeast Power Grid with service requirements above 35 kV classified as “common industrial” pay 0.264 yuan per kwh; similar customers classified as “large-scale industrial” pay 0.187 yuan, a discount of 29 per cent (Energy 1996, VI-27).

Despite beneficial changes resulting from decontrol of commodity prices, reforms aimed at freeing employers from responsibility for social benefits, and modest increases in real interest costs, the relative price of urban labour remains high. The efforts of city governments to reserve jobs for urban residents by erecting administrative or economic barriers to the employment of rural migrants (e.g. Shanghai’s imposition of fees amounting to RMB 890 for employing one man-year of nonresident labour; see Shanghai 1998, p. 105) threaten to undo some of the benefits of

recent reforms. Even without these new restrictions, China's price structure continues to inhibit the growth of employment. Hu Angang aptly summarizes the current situation: "The distorted factor price for capital stimulates the modern industrial sector to utilize capital-intensive production technology and reduces its capacity to absorb labour" (1998a, p. 11). Circumstances facing TVE industry are identical: artificially low capital costs and escalating wage costs systematically reduce the growth of employment (Chen Jianbo 1997, pp. 376-380).

Capital allocation mechanism. Chinese writers and enterprise managers constantly complain of "insufficient funds." If funds are scarce, enterprises that gain access to investment opportunities should reap large rewards. In China, however, profit rates have declined almost monotonically since the early 1980s. The decline in profits is too large to be attributed to tax evasion or fraud. Falling profits, although most widely remarked in the state sector, extend to all classes of enterprises. The improbable combination of scarce funds and low returns signals the presence of major defects in China's capital allocation mechanism.

The problems extend far beyond the underpricing of funds. The chief difficulty is that access to bank loans, a key source of investment finance, and to the nascent stock and bond markets, is often reserved for large borrowers who have a record of making poor investment decisions. China's capital markets display an unfortunate combination of poor project selection by borrowers and weak monitoring by the banks. As a result, many new projects fail completely. China's 1995 industrial census, conducted in a year of strong growth, found that "there are nearly 500 kinds of products being manufactured at less than 60 per cent of capacity" (Zhou Kan 1998b; for details, see Yearbook 1997, pp. 454-455). Widespread excess capacity, much of it arising from recently-completed investments (e.g. 1995 capacity utilization of 33.5 per cent for home air conditioners, 22.1 per cent for color film, 46.0 per cent for photocopiers), mirrors the accumulation of unrepayable bank loans. Both reflect long-standing shortcomings in China's capital allocation mechanism. These defects artificially limit the capacity of China's economy to create productive employment.

Urban bias. As in many other developing nations, Chinese government policy reflects a deep and long-standing urban bias. At every level of the administrative hierarchy, official policy channels benefits and opportunities toward urban residents (and within the urban sector, to residents of larger cities) and shifts burdens away from them. Policy documents announce that "China should always give agriculture top priority for the development of the national economy" (Rural 1998), but investment statistics tell a different story. Between 1981 and 1995, agriculture absorbed 2.2 per cent of investment spending by state and collective units (Investment 1997, pp. 47, 364). Social safety nets focus almost exclusively on the welfare of urban residents. Thus the annual living allowance for laid-off workers in Beijing is 2,400 yuan, or 15 per cent above the average net income for rural residents (*China Daily* 23 September 1998, p. 3; Survey 1998, p. 83). Jobless workers without urban registration (*hukou*) receive nothing. The residual nature of official concern for the rural economy is readily visible in a press report stating that "Stagnant growth in the urban consumption market. . . has turned the eyes of policymakers and business people to the rural market" (Zhou Kan 1998a).

Under normal conditions, officials tend to neglect rural affairs. As a result, explicit instructions from the State Council or from China's top leaders often have little impact in the countryside (for examples involving farm inputs, see Zhu Shizhen 1995, Yang Fangxun 1995). Segmented (often chaotic) markets for farm inputs and products; inflated costs; and arbitrary (often illegal) quotas, fees, taxes, and fines systematically reduce the productivity and profitability of rural production, and with it the demand for rural labour. With restrictions on internal

migration in disarray, urban bias magnifies the scale of migration into China's towns and cities.

Opening China's economy. China's experiments with "open door" policies to expand international trade and foreign investment ignited an unexpected surge of export-led growth along China's eastern seaboard. Rising wages and land costs are bringing this episode to a close (with an extra jolt from the Asian crisis of 1997/98). Whether improvements in domestic transport and communication will permit interior provinces to take advantage of trade-linked growth opportunities as coastal regions outgrow them depends on domestic policies as well as international market conditions. Despite slow progress toward Chinese enrollment in the WTO, further opening will occur. Expanded trade threatens the viability of particular firms and industries, but greater openness focuses investments on projects and technologies that mesh with Chinese resource endowments. China's leaders recognize that in the future, as in the past, trade offers large opportunities for employment creation.

Property rights. Inadequate support of property rights affects every type of business in China. Negative consequences for private enterprise – the most dynamic source of new employment in the 1990s – are most serious. A 1996 survey of large (and presumably well-connected) private groups in Beijing documents problems with access to credit, unfavorable tax policies, and denial of urban residence permits. Although these firms report that formal legal discrimination no longer exists, their most serious difficulties arise because "Enterprise assets, brand names, even the persons of the investors, do not enjoy effective protection for their legal rights and interests" (Private 1997, p. 19).

These difficulties are not unique to the capital. Since only 7-8 per cent of bank loans go to small and medium-scale enterprises (Shao 1998), bank lending to private firms is evidently minuscule. Even in Guangdong, no private firm outside the special export zones has received the right to conduct direct trade with international partners (Private Business 1998). The key question: will Chinese policy actively promote private enterprise, or merely extend the current policy of grudging toleration, as when Shaanxi officials are "asked to refrain from discriminating against private enterprises. . . as has been done in the past, and try harder to provide better service to them" (Ma Lie 1997). The outcome will have major consequences for the pace of employment creation.

Policies affecting specific sectors

State enterprises. Chinese leaders have long believed that state enterprises should occupy the "commanding heights" of the economy. However the range of desired state-sector dominance has declined steadily. Special preference for state firms contributes to the rationale for concessional interest rates and segmented capital markets, which in turn bias investment choices toward capital intensive projects and sectors. Continued erosion of the preferred position assigned to state enterprises moves the economy in the direction of full employment.

Domestic transport and trade. China's reform has brought a revolution in transport, communication, and information that brings new opportunities to the doorstep of formerly isolated communities. The effects parallel the consequences of China's growing openness to international trade and investment. There are numerous reports about barriers to domestic trade (e.g. Dong Fureng 1992, p. 6), but serious difficulties appear limited to cases involving price controls. With price controls in steep decline, domestic trade barriers appear more episodic than

systematic. Despite negative short-term consequences, as local industries formerly protected by geographic or information barriers wilt in the face of new competition (this hurts many formerly successful TVE operations), these changes bring new opportunities in the longer term, because local resources can move into cost-effective occupations that serve enlarged markets.

Local development strategies. Local governments (and their constituents - who increasingly elect local leaders) see their main task as delivering growth. Over the past two decades, successful outcomes, concentrated in coastal regions, were built on the expansion of TVE industry - rural collective firms mostly directed and controlled by local government. Interior provinces now hope that development of TVE industry will allow them to replicate the achievements of coastal areas. This seems improbable. Local governments in coastal areas - the same administrations that achieved enormous success in building TVE firms in the semi-market environment of the 1980s - are now eager to retreat from direct control of enterprises because they fear the growing risk inherent in an economy increasingly dominated by market forces. True separation of government from enterprises (*zhengqi fenkai*), in which managers achieve genuine independence and officials eschew direct interventions and devote themselves to administration, is a newly emergent phenomenon in China's southern provinces that is likely to spread. While rising costs along the southern coast create opportunities for interior regions to absorb labour-intensive industries that are now uneconomical in Shenzhen or Shanghai, the next few years are likely to reveal TVE industry as a transitory phenomenon rather than a long-term fixture in China's economic structure.

Education. As noted above, education-linked income differentials are increasingly common in China's economy. Twenty years of economic growth has brought a steep escalation of quality requirements imposed by foreign and domestic buyers of intermediate and final goods. Producers whose goods meet these rising quality requirements will prosper. Low-quality output is dumped into China's large but stagnant market for inferior goods, where ferocious price competition allows little or no profit, little chance to accumulate funds for restructuring, and declining access to bank credit (the banks have begun to "redline" firms in this category). Firms (and workers) that can only deliver routine products and services are prime candidates for failure (and joblessness).

In this environment, human capital of all sorts is a key determinant of economic prospects. Urban parents understand this clearly. They voluntarily limit family size to increase the quality of their offspring and invest heavily in their children's education by purchasing computers, educational travel, and tutoring. Rural outcomes are more dependent on the efforts of local governments to upgrade the quality of teachers, raise the proportion of children attending middle-school and high school, and expand networks of libraries and other information services.

Agriculture. The experience of Taiwan (China) and Japan suggests that appropriate government support can help the farm sector to generate substantial gains in output, productivity, and employment well into the middle stages of industrialization. Available information indicates that support in such areas as agricultural extension and distribution of farm inputs is often limited by an urban policy bias that systematically channels resources (especially trained personnel) out of the rural economy. There is considerable scope for official actions that could increase labour demand in farming and other rural occupations at modest cost. Employment creation in this sector will be larger to the extent that:

S government refrains from manipulating the prices of farm inputs and outputs to suit the convenience or the finances of government agencies, urban consumers, and non-

- agricultural industries.
- government effectively controls the official and informal taxes and levies that systematically erode the incomes of farm households and rural enterprises (TVE firms reportedly lose 20 per cent of their profits to “unfair fines and tariffs”; see Zhao Huanxin 1998).
- government expands availability of credit for farming and agri-business.
- government stabilizes and expands networks for the collection of farm products, and the distribution of material inputs and technical information for farming.

IV. Summary and conclusion: China’s prospects for full employment

For two decades, China has enjoyed the world’s highest rate of economic growth. This growth spurt coincides with a gradual and incomplete shift from socialist planning that has moved important segments of China’s economy, including the mechanism for allocating and compensating labour resources, a considerable distance in the direction of a full market system. The combined impact of China’s long boom and gradual reform has delivered many benefits to the world’s largest national populace, none more important than large increases in real wages and employment opportunities. These changes stimulated a vast and largely unrecorded exodus of workers from agriculture and from China’s villages. They allowed a remarkable interlude during 1990-94 in which China’s economy temporarily achieved the closest approach to full employment that any populous low-income nation has ever accomplished.

The recent economic history of East Asia provides convincing evidence that dynamic economies can deliver large gains in output, productivity and welfare while burdened with costs imposed by flawed institutions, obsolete structures, and unwise policies. China’s strong record of providing employment and income for its immense work force against a daunting backdrop of per capita resource scarcity represents an important addition to this record. Although China’s leaders understand both the need to accelerate labour absorption and the dangers of joblessness, rapid expansion of labour demand has occurred in the face of policies that systematically limit the capacity of China’s economy to create new employment.

The major constraints on employment growth are not the result of policies designed to retard labour absorption. Instead, they reflect the unintended consequences of long-standing policies inherited from China’s pre-reform system of economic planning. Artificially low capital costs and restrictions that effectively channel most loanable funds to favored borrowers in the state sector tilt project selection toward capital-intensive sectors and technologies. The same complex of distortions permits vast expenditures on empty structures and idle factories that deliver no benefits whatever. Urban bias is another historic component of Chinese public policy that permeates the entire economy, accelerating the population shift from villages to towns, forcing urban communities to respond to the pressure of successive waves of migrants, and exacerbating tensions between newcomers and privileged urban residents.

This survey pinpoints China’s emergent private sector as an important source of new employment. The failure of government agencies at all levels to actively promote, rather than merely tolerating, the expansion of private enterprise represents another legacy of China’s socialist past that must now be recognized as a significant obstacle to the expansion of employment.

This review shows an abrupt decline in the demand for labour beginning in 1995/96. The timing of this shift is particularly unfortunate because it overlaps with the current Asian crisis and with long-delayed action to remove tens of millions of redundant workers from what had long

been regarded as life-time positions in China's state-owned industrial enterprises, government agencies, banks, and railways. Although China has escaped the worst consequences of the current Asian downturn, the crisis has shattered public confidence and halted the growth of exports and foreign investment, formerly the most dynamic sectors of China's economy.

The cumulative impact of domestic slowdown, the Asian crisis, and mass furloughs means a sharp reversal away from full employment. Instead, China faces the danger of recession (or worse) arising from a daunting combination of short- and long-term challenges. The difficulty centers on long-standing weaknesses in the mechanism of capital allocation that cause low investment returns and generate immense quantities of bad debt. These difficulties may terminate China's long boom. Even if this does not occur, China now confronts a slump in employment growth that seems certain to continue until the year 2000, if not longer.

Under these conditions, China can no longer enjoy the luxury of rapid employment growth despite (unintended) anti-employment policies embedded in the wage-rental ratio, and the capital allocation mechanism as well as a wide range of preferences favoring state enterprises and the urban sector. If China's government wishes to avoid a protracted slowdown in employment growth and correspondingly high rates of open and hidden unemployment, strong measures to reverse long-standing constraints on employment growth seem imperative. The main components of policies to expand the economy's job creation potential follow directly from the foregoing discussion:

- move toward scarcity pricing of capital; avoid a retreat from the currently positive real rates toward the past pattern of negative real rates for favored borrowers;
- dismantle entry barriers surrounding formal capital markets; push toward the objective of allowing all would-be borrowers to compete for funds on the basis of profit prospects and ability to repay;
- further reduce (and eventually eliminate) policies favoring the state sector;
- mount a concerted effort to reduce urban bias and move in the direction of a "level playing field" for urban and rural-based economic activity;
- establish an economy-wide policy of actively encouraging the formation and expansion of private enterprise.

These are long-run policies to promote long-term growth of employment. I conclude with an observation regarding the current policy environment.

China's leaders fear the social consequences of mass unemployment. As reports of joblessness mount, their natural and completely understandable response is to implement policies that promise short-term increases in employment. Unfortunately, the main instruments they have chosen - multiple reductions in interest rates, measures to bolster state enterprises, and new infrastructure spending to push the economy toward the official 8 per cent growth target for 1998 - are in sharp conflict with China's medium- and long-term reform objectives. Current short-term policies perpetuate the sheltering of state enterprises, reverse the trend of declining official interference in market processes, postpone the separation of government from business, delay the commercialization of banking, and erode the banks' already precarious financial position.

The push for 8 per cent growth is a costly initiative that is unlikely to deliver substantial employment gains. An alternative strategy focused on promoting private business could easily match, and perhaps surpass the immediate employment benefits associated with the drive to attain 8 per cent growth. Such an alternative would promote, rather than obstruct, the longer term reform objectives to which China's leaders remain committed. The choice of Keynesian policies rather than reform-enhancing institutional change in response to a short-term threat of mass unemployment represents a major policy error that will reduce the capacity of China's economy to approach a variety of objectives, including full employment.

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