Jnl Soc. Pol., 33, 2, 267–288 © 2004 Cambridge University Press
DOI: 10.1017/S004727940300744X Printed in the United Kingdom

A Long Financial March: Pension Reform in China

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Abstract

In the context of rapid economic and demographic change, the People's Republic of China has attempted to reshape its public pension system. Although China's current pension system has drawn the attention of many policy analysts, no theoretically informed account on the politics of Chinese pension reform has yet been published. Grounded in a broad institutionalist perspective, this contribution analyses contemporary pension politics in China through the interplay of four main factors: (1) decentralisation and limited administrative capacity, which make it difficult to rationalise and transform the existing pension system; (2) feedback effects from previously enacted pension schemes that further complicate policy change; (3) liberalisation and economic reforms, which have created 'vested interests' in the newly established private sector, but which have lacked the strength to generate a mature financial system; (4) finally, the apparent dominance of the neo-liberal financial paradigm commonly associated with the World Bank. While this financial paradigm favours the *adoption* of new reform proposals, the economic and institutional factors mentioned above complicate their *implementation*.

Introduction

Since the 1980s, concerns about demographic aging as well as economic imperatives such as competitiveness and fiscal austerity, have favoured the adoption of various pension reforms around the world. Although existing pension commitments transform retrenchment into a risky business for politicians, numerous countries have restructured their public pension schemes, while some nations have gone as far as to privatise them. Despite European exceptions like Sweden and the UK, the most comprehensive reforms have been enacted in Latin America and, perhaps to a lesser extent, in Eastern Europe and East Asia (Bonoli and Shinkawa, forthcoming; Brooks, 2002; Hinrichs, 2000; Madrid, 2000; Myles and Pierson, 2001; Thompson, 1998; Turner, 2002; Weaver, 2003; Williamson and Pampel, 1993).

Economic restructuring commonly associated with neo-liberalism has been instrumental in maintaining pension reform on the global policy agenda. In the context of rapid economic and demographic change, the People's Republic of

China has also attempted to reshape its public pension system. China is the most populous country in the world, with 1.295 billion inhabitants in 2001 (CPIRC, 2001).[1] Because of its large population, the effects of the one-child policy, and also the dramatic increase in life expectancy over the last 50 years, population aging has become a central policy issue more quickly in China than in most developing countries. Since the 1990s, the academic publications dealing directly with Chinese pension reform generally have focused on current reform attempts from an economics, policy-oriented perspective (Munnell, 1999; Rosegrant, 1999; Smyth, 2000; Song and Chu, 1997; Wang, 1995; West, 1999). These contributions examine the features of past and current pension schemes while pointing out existing bureaucratic, economic, and social obstacles to reform. Some economists have also argued that the integration of private savings accounts with the existing system could reduce the financial burden on state-owned enterprises (Shen, 2000) and future generations of Chinese workers (Feldstein, 1998). Although China's current pension system has drawn the attention of many policy analysts, no theoretically informed account of the politics of Chinese pension reform has yet been published.[2] Considering the growing body of international literature on social policy reform, however, it is desirable to apply theoretical tools developed elsewhere to improve our understanding of pension reform in China.

Rooted in a broad institutionalist perspective, the following article studies contemporary pension politics in China while exploring the interplay of four main factors: (1) decentralisation and limited administrative capacity, which make it difficult to rationalise and transform the existing pension system; (2) feedback effects from previously enacted pension schemes that further complicate policy change; (3) liberalisation and economic reforms, which have created 'vested interests' in the newly established private sector but which have lacked the strength to generate a mature financial system; (4) finally, the apparent domination of the neo-liberal financial paradigm commonly associated with the World Bank. Before exploring the impact of these factors on pension reforms put forward since the 1980s, the first section frames a coherent theoretical framework adapted to our empirical task.

A broader institutionalist framework

Theories of social policy development tend to fall under two broad categories: societal accounts and institutional accounts (Béland and Hacker, 2004; Skocpol, 1992). On the one hand, societal accounts underline factors that are perceived as autonomous from political institutions (e.g. cultural values, social mobilisation and economic transformations). On the other hand, institutional accounts directly call attention to the characteristics of political institutions (e.g. administrative capacity of state organisations, the centralisation of political authority, and the transformation of party systems). Although some researchers have endeavoured to relate them (Hacker, 2002; Lieberman, 2002; Skocpol, 1992), clear differences of emphasis remain. While societal theorists view institutions essentially as products of external forces, institutional theorists depict them as autonomous structuring elements (Béland and Hacker, 2004). Instead of returning to this well-known debate, the following section frames an institutionalist framework adapted to the study of social policy development and, more precisely, pension reform in China. Although this institutionalist framework was first developed in democratic societies, general institutionalist insights about political structuration, if used appropriately, can improve our understanding of pension reform in an authoritarian polity like China. While focusing on institutional structuration, the theoretical approach sketched below also recognises the role of two main societal factors: economic interests and policy ideas. This acknowledgement leads to the formulation of a broader and multifaceted institutionalist framework, which seems adapted to the study of policy-making in China.

Historical institutionalism: administrative capacity and policy feedback

Formulated as an alternative to societal approaches focusing on cultural values (Lipset, 1990) and class politics (Esping-Andersen, 1985; Korpi, 1983), historical institutionalism is grounded in the assumption that political institutions and previously enacted public policies structure the political behaviour of bureaucrats, political officials, and interest groups during the policy-making process: 'This approach views the polity as the primary locus for action, yet understands political activities, whether carried by politicians or by social groups, as conditioned by institutional configurations of governments and political party systems' (Skocpol, 1992: 41).[3] Historically constructed institutions thus create constraints and opportunities for policy-makers (Immergut, 1998).

While recognising the relative autonomy of political actors towards socio-economic forces, institutionalist scholars explore how institutions structure political behaviour and interests (Béland, 2001; Kay, 1999). In her study of the politics of healthcare reform in France, Switzerland, and Sweden, for example, Ellen M. Immergut argues that the structure of the Swiss federal system reinforces the political influence of Swiss physicians, who can oppose legislation more easily than their equally well-organised colleagues in France and Sweden (Immergut, 1992). In the same vein, Antonia Maioni's book on federalism and health care reform in Canada and the United States shows how specific forms of political decentralisation – as related to institutions such as party systems – affect the policy-making process (Maioni, 1998). As will be demonstrated below, the recent movement towards decentralisation in China also has a strong impact on pension reform in that country. However, Chinese decentralisation is taking place in an authoritarian context, and the constitution of 'veto points' outside the party-state apparatus seems unlikely during the policy adoption process. Instead, interests tend to impact policy outcomes at the implementation level, where they directly interact with local and provincial bureaucrats, generally behind close doors. Considering this logic of decentralisation, it is thus essential to take into account the enduring contrast between policy adoption and implementation in Chinese pension reform (Huang, 2003).

In addition to decentralisation, administrative capacity is another institutional phenomenon that structures the logic of pension reform in China. From an institutional perspective, 'administrative capacity refers to the ability of states to deliver public goods, and services such as education and public health and to carry out the normal administrative functions of government such as government regulation, revenue collection and information management' (Lo *et al.*, 2001: 44). To implement comprehensive economic and social policies, the state must levy standardised taxes, keep systematic administrative records, and enforce uniform rules across its territory. Limited administrative capacity makes policy implementation problematic (Grindle, 1996). As discussed below, this is the case in China, a country in which decentralisation and significant regional variations exacerbate persisting administrative problems such as regulatory fragmentation and deficient tax collection mechanisms. The recurring inability to efficiently collect pension contributions is a striking example of limited administrative capacity that undermines policy implementation.

Policy feedback is another key institutionalist concept that could improve our understanding of Chinese pension reform. Referring to the structuring impact of previously enacted policies on decision making, this concept makes institutionalism 'historical' because it shows how policy makers must take into account vested interests attached to established public policies. The concept of policy feedback is also linked with the idea of social learning; that is, the process by which officials evaluate the performance of established policies (Hansen and King, 1999; Heclo, 1974). Through the process of social learning, existing policies influence policy-makers' perceptions and strategies. Before enacting new legislation, they generally take into account existing policy legacies related to decisions made years or even decades earlier. Present-day officials have to live with the decisions of their predecessors, which tend to reinforce existing policy paths (Skocpol, 1992; Pierson, 2000). For example, financial commitments at the centre of existing PAYGO (pay-as-you-go) schemes make the implementation of individual savings accounts problematic since it proves difficult to simultaneously finance current pension benefits while setting money aside in these accounts to supposedly guarantee the economic security of future retirees and increase the national savings rate (Aaron and Reischauer, 1998). As will be analysed below, transition costs linked to this type of reform also create institutional obstacles to the implementation of the financial paradigm in China. Moreover, the common Chinese practice of launching 'pilot projects' on a decentralised basis explicitly favours social learning, which can in turn impact the decision-making process at a later stage. Finally, although the absence of democratic institutions may eliminate many obstacles to reform present in other countries, enduring policy legacies complicate reform initiatives. As pensioners and workers have staged illegal demonstrations across the country to preserve their pension benefits (Hurst and O'Brian, 2002; Huang, 2003: 191), policy-makers have to take into account past pension commitments in order to preserve social order. The Chinese state does acknowledge that an effective social security system would enhance social stability through the mitigation of social conflicts and tensions (Ministry of Labour and Social Security, 1999). This provides additional ground for the institutionalist assumption that 'policy creates politics', even under an authoritarian rule.

Economic interests and policy ideas

In the second part, we will show how institutional factors such as state decentralisation, limited administrative capacity, and feedback effects from previously enacted policies have undermined the implementation of reforms aimed at reshaping China's fragmented pension system. Yet while these institutionalist insights constitute an excellent starting point to analysing policy-making in China and also in other countries, it seems essential to explicitly recognise the impact of two societal factors that consistently impact institutional politics: the structuring power of economic interests and the enduring role of policy ideas (Béland and Hacker, 2004). A discussion of these two factors leads to the formulation of additional theoretical insights that enrich our understanding of policy-making and, more precisely, Chinese pension reform.

Historical institutionalism begins with the perspective that party systems and state institutions mediate and transform economic interests. While acknowledging this institutional structuration, however, one cannot overlook the fact that socio-economic interests also create constraining 'rules of the game' in the field of social policy reform. In this context, it is appropriate to extend the concept of policy feedback to the private sector in order to understand how private 'vested interests' create opportunities and obstacles for reform (Béland and Hacker, 2004; Hacker, 2002). Never isolated from existing public policies, these vested interests, however, are generally related to tax incentives, legal regulations, or previously enacted economic reforms. The Chinese case in the era of economic liberalisation provides further ground for this claim. As privatisation and liberalisation-related measures have been enacted since the late 1970s, they have created powerful 'vested interests' in the emerging private sector. These vested interests tend to oppose state's pension reform initiatives in the context of administrative decentralisation and limited state capacities.[4] Paradoxically, state-sponsored economic reforms have thus favoured the emergence of business interests that reduce the state's capacity to successfully implement pension reforms. Moreover, the absence of a mature financial sector in China is another important economic factor that complicates the concrete implementation of specific reform initiatives tied to the financial paradigm that will be discussed below.

The focus on institutional processes should not lead institutional scholars to downplay ideational forces that largely shape policy choices (Béland and Hacker, 2004; Campbell, 2002; Cox, 2001; Lieberman, 2002). In the field of economic policy, Peter A. Hall has demonstrated that it is crucial to trace the development of competing policy paradigms in order to understand the genesis of political decisions. According to Hall, a policy paradigm is a 'framework of ideas and standards that specifies not only the goals of policy and the kind of instruments that can be used to attain them, but also the very nature of the problems they are meant to address' (Hall, 1993: 279). Being technical and ideological, paradigms constitute a relatively coherent set of ideological and technical assumptions of policy experts and state officials interacting within a constraining institutional environment. The recent literature on social policy underlines the role of ideas in policy-making (for example, Cox, 2001). In developing countries such as China, international organisations sometimes have become instrumental in providing decision-makers with coherent policy paradigms tied to the dominant neo-liberal creed (Brooks, forthcoming; Merrien, 2001). While state officials are not blindly following international trends, there is a clear convergence between reforms enacted in China during the 1990s and the policy paradigm associated with the World Bank. As we demonstrate, this international organisation helped Chinese policy-makers frame a more coherent reform paradigm without imposing it directly. While institutional factors and vested economic interests make policy implementation difficult, this paradigm has shaped recent state decisions related to pension reform. Thus, policy ideas especially matter during the policy adoption process.

In the following empirical analysis, we examine the interaction between institutional logics and the above-mentioned societal factors. As we argue, institutional factors like decentralisation, limited administrative capacity, and existing policy legacies, as well as societal tendencies such as vested economic interests and immature financial institutions, have slowed the implementation of a policy paradigm aimed at both centralising China's public pension system and favouring the development of advance funding and private savings accounts. Whereas this financial paradigm favours the *adoption* of new reform proposals, key economic and institutional factors complicate policy *implementation.*

The institutional logic of chinese pension reform

State-building, administrative capacities and public pensions in China

Organising a vast and populous country like China is a most problematic task. The collapse of imperial institutions during the first decades of the twentieth century radically exacerbated this problem. Indeed, prominent Chinese revolutionaries such as Sun Yat-sen and Mao Zedong recognised its scope at early stages of their political careers (Zheng, 1997: 7). While the Communist Party succeeded in imposing its hegemonic political authority upon Chinese society following the 1949 Revolution, the building of a coherent bureaucratic state represented (and still represents) a far more difficult undertaking. In fact, the Party's will to preserve its political hegemony posed a strong obstacle to systematic state-building efforts aimed at increasing the administrative capacities of the Chinese state: 'Because the revolutionary party and the state institutions followed different organisational rationale and logic, the development of the state inevitably challenged the leading status and power of the Party, which in turn prompted the Party's reaction or overreaction to suppress or even destroy the state institutions that the Party had initially built' (ibid.: 255). Party-led movements such as the Anti-Rightist Campaign of 1957 and the Cultural Revolution (1966–1976) inverted early state building and bureaucratisation efforts (Harding, 1981). Although state institutions were rebuilt during the 1970s, public authority remains extremely fragmented. Divided into many competing bureaucratic units, the Chinese state is the theatre of incessant bargaining processes and consensus building efforts. As a result of fragmentation, bargaining, and consensus building, the policy process is generally incremental in nature (Lieberthal and Oksenberg, 1988: 24; Duckett, forthcoming). Political and administrative institutions thus structure policy processes in a way that is coherent with the institutionalist perspective.

Considering the enormous size of the country and the state-building issues mentioned above, it would be difficult to administer a centralised, national welfare state in China. After the 1949 Revolution, the government did adopt an approach for 'digesting economic problems at the local level', and 'national support was only made available when crises occurred and when natural disasters cut across regional borders' (Fung and Ngan, 1996: 45–6). As a result, inflation control and guaranteed employment ('iron rice bowl') constituted the main sources of economic security for China's urban workers (ibid.).

This last remark points to the dual character of China's social policy system (Smart and Smart, 2001), in which little has been done to develop comprehensive pension programs in rural areas.[5] The state established the first Chinese public (urban) pension system in 1951 through the State Council's Regulations on Labour Insurance. The regulations applied to enterprises with more than 100 employees. The All China Federation of Trade Unions managed the system until 1966. After the abolition of this federation during the Cultural Revolution (1966–1976), supervisory responsibility was then transferred to the local labour bureaus, while the task of distributing benefits was passed on to SOEs. As a consequence of the Cultural Revolution, limited administrative capacity prevented the Chinese state from managing a coherent and centrally regulated public pension system. Considering the high level of fragmentation prevailing both at the administrative and the provision levels, the central state, through its different ministries, only issued general orders from time to time (Wang, 1995: 6).

After 1966, China's social security system (including the pension schemes) was, therefore, designed to deliver social services and benefits to employees and their families through SOEs (West, 1999). This PAYGO system offered defined pension benefits officially financed by the employers. Within this fragmented system, enterprises bore responsibility for providing retirees with pension benefits (although the state subsidised them before the economic reforms of the 1980s). SOEs thus paid pensions out of current income, and there were no pension reserves. Both male and female employees of SOEs were entitled to pension benefits. Before 1980, the average replacement rate was approximately 80 per cent, which is high compared with international standards that range from 40 per cent to 60 per cent of final salaries (World Bank, 1997; Qiu and MingCai, 1985). Since that date, the average Chinese replacement rate has declined to about 70 per cent, still a comparatively generous percentage. Normal retirement age was low by international standards: 60 for men, 55 for women occupying managerial positions and only 50 for non-managerial women (Rosegrant, 1999: 2). Because employees did not contribute to the pension plans of SOEs, these are better viewed as enterprise insurance schemes rather than social insurance ones (Lee, 1996). Potential financing problems related to this specific financial arrangement would materialise during the 1980s. This illustrates the effect of existing policy legacies on social and economic reforms.

Economic reforms and the crisis of the public pensions

In the previous section, we briefly underlined the impact of institutional structures (decentralisation and limited administrative capacities) and policies legacies (pension fragmentation) on social policy development in post-revolutionary China. These institutional logics structure Chinese pension reform. This being said, two main factors explain the emergence of severe financial problems: demographic aging itself and, more pressingly, the financial crisis that affects many SOEs, a phenomenon directly related to recent economic reforms. As we show, these reforms have also reinforced institutional tendencies like decentralisation that complicate pension reform efforts.

China's rapid increase in life expectancy, as well as the one-child policy implemented in 1978, have increased awareness concerning population aging and pension reform in that country. In 2000, one in every ten Chinese citizens was 60 years of age or older, and those beyond 65 made up more than 7 per cent of the national population (Zhang, 2002). Considering the sharp decrease in the birth rate (from over 30 per thousand in 1978 to about 15 per thousand in 1999) and the related growth of one-child families, there will be fewer workers entering the labour market in the following decades. In other words, there will be a decrease of young workers supporting the pension system while the number of retirees is increasing rapidly. Hence, pension expenditures will grow even more rapidly in the future.[6]

More important for the short term, recent economic reforms have negatively affected the financial situation of many SOEs and, indirectly, reduced their capacity to pay existing pension benefits to their former employees. Since 1978, the Chinese state has launched several waves of institutional and economic reforms (Zweig, 2001) related to what Deng Xiaoping called 'socialism with Chinese characteristics' (Tien and Chu, 2000: 13). China's economy has thus been gradually exposed to international competition and has moved towards a market economy. More precisely, these reforms have favoured three essential logics: decentralisation, marketisation, and privatisation (Zweig, 2001; Chao and Dickson, 2001).[7]

In the context of these reforms, decentralisation refers to the devolution of decisional authority from the central government to provincial and local authorities aimed at promoting regional innovation and reform initiatives. While nationwide application of standardised rules generally characterised the Mao era, post-Mao reform leadership has indeed supported 'the devolution of substantive decision-making authority in the allocation of fiscal and material resources' (Jae, 2001: 50). This trend reflects the fact that the fragmented Chinese state does not have the capacity to implement national norms and policies without the support of local and regional authorities. In contemporary China, decentralisation and administrative fragmentation also means that constant bargaining between individuals and organisations frames the relationship between local, provincial, and national governments. The central government thus deals with provincial and municipal resistance by means of numerous ad hoc agreements made after informal negotiation rounds (Starr, 2001: 69). Such a complex bargaining system does nothing to improve bureaucratic efficiency and administrative regulation in China, thus reinforcing institutional obstacles to comprehensive pension reform.

The two other logics associated with recent economic reforms are closely related. While marketisation refers to the weakening of state *dirigisme* as well as the promotion of market competition and self-regulation, privatisation means that private property and foreign capital have gradually increased their role in China's economy. Indeed, through the 1990s, the Communist Party gradually recognised the new role of the private sector resulting from the incremental economic reforms that had been enacted since 1978.[8] In this context, the private sector has grown phenomenally and has controlled nearly half of the national economy in many respects over the last two decades (Lau, 1999). By 2002, the private sector in China accounted for 33 per cent of the country's GDP, compared to a share of 37 per cent by the state-owned enterprises (*People's Daily*, 2002).[9] This expansion has created vested economic interests in the field of old-age pension because private businesses tend to have a younger workforce and, therefore, more modest pension expenditures. As we shall see, such an economic advantage explains why many private businesses oppose state efforts to unify the pension system. 'Vested interests' emerging in the newly created private sector thus have an impact on Chinese pension reform.

Economic reforms have also placed numerous SOEs in a difficult financial situation that calls into question their ability to guarantee the old-age security of urban workers. These reforms first required SOEs to make business decisions based on market signals while adopting profit making as their ultimate goal (Chen, Thomas and Ming, 2001).[10] Facing new competition from the emerging private sector and bearing the weight of demographic aging in a disproportionate manner (private businesses tend to have a younger workforce than public ones), the financial situation of SOEs – and their ability to provide social security benefits to their employees – has become a real concern since the 1980s. For instance, the proportion of industrial SOEs that were running deficits increased from 19.2 per cent to 38.2 per cent between 1980 and 1997 (Smyth, 2000). And because of the absence of pension reserves, SOEs have to pay pensions with the high pre-1980 salary replacement rate at about 80 per cent of current average salaries. To face their financial obligations, SOEs tend to lay off staff and borrow from China's state banks. The lack of pension planning, therefore, contributed not only to SOEs' financial difficulties, but also to the growth of non-performing loans in China's banking sector (Chen, Thomas and Ming, 2001). These financial problems, as well as the demographic forecasts mentioned above, convinced decision-makers to launch various reform initiatives in order to rationalise and guarantee the solvency of China's fragmented public pension system. In addition, the multiplication in recent years of illegal protests related to pension issues (Hurst and O'Brian, 2002; Huang, 2003: 191) certainly has reinforced the officials' traditional belief that economic security for urban workers is instrumental to the reproduction of their authoritarian political system. According to Hurst and O'Brian, Chinese retirees often consider public pensions as 'a symbolic recognition by state and firm of an employee's years of devoted service as well as a vital source of support for those who are too old to work' (Hurst and O'Brian, 2002: 350). Therefore, it seems politically dangerous to deprive massive numbers of urban retirees of their pensions, which are generally perceived as 'the ultimate entitlement' (ibid.: 353). In spite of an authoritarian rule that may facilitate the suppression of existing benefits, pensions carry much *political* weight in China. This further illustrates the significance of post-revolutionary pension legacies in contemporary policy-making.

Tied to economic imperatives as well as to general concerns about the preservation of social and political order, the major objective of pension reform is to strengthen coverage while spreading the financial burden associated with pension commitments across older and newer enterprises through social pooling. Because an enterprise's pension contribution is now based on its number of employees (instead of its number of retirees), SOEs tend to fare better under local or regional pooling systems. In 1984, the state carried out the first modern reform, which promotes experiments on pension pooling in provinces like Guangdong, Jiangsu, and Liaoning. SOEs participating in pooling programs put a portion of their total wages into a pension fund managed by a local old-age insurance bureau. Individual workers could voluntarily use their savings to supplement the pension fund (Song and Chu, 1997). However, pension reform was still at its experimental stage, and methods of pension pooling varied from place to place. This extreme fragmentation reflects the logic of decentralisation that has characterised the economic and institutional reforms enacted in China since the late 1970s.

In spite of the mixed results of these first reform attempts, the state rapidly took another step in pension reform by introducing the idea of employee contributions. The 1986 pension reforms, accompanied by employment reforms, indeed strengthened the emerging market logic and the role of economic privatisation. In fact, since late 1993, the Chinese state has maintained privatisation on the agenda. This question became a major issue during the Party's 15th Congress in September 1997 (Lau, 1999; Smart and Smart, 2001: 1856). With the establishment of contract labour, new employees were to be hired on a contract basis, while current employees would maintain their permanent status. Afterwards, contract workers were required to make individual contributions to existing pension schemes (World Bank, 1997). This reform aimed at separating city pension pools for contract workers and permanent workers; that is, contract workers had to make individual contributions, while permanent workers initially did not. In the late 1980s pooling was extended to workers in collectively owned enterprises in many cities. Since then, joint ventures, joint stock companies, and foreign enterprises have been brought into pension pools in some cities. This venture has the great advantage of bringing new workers and their contributions into the system 'without an accompanying heavy retiree burden' (Rosegrant, 1999: 9). Considering the 'vested interests' mentioned above, however, many private companies have refused to join pooled plans.[11] A paradoxical consequence of recent economic reforms, these fragmented private interests further complicate policy efforts aimed at increasing the level of integration within the Chinese pension system.

While pooling and rationalisation have been at the centre of governmental pension initiatives since the early 1980s, the State Council has also pushed for the development of individual savings accounts. In China's increasingly decentralised institutional context, a bottom-up reform strategy has been adopted, with cities and provinces conducting their own pension experiments under loosely defined guidelines emanating from Beijing. On 26 June 1991, for example, the State Council actually proposed a three-tier retirement insurance system for employees in urban enterprises. This system would be composed of three parts: (1) a basic retirement program managed by the state; (2) supplementary retirement programs funded by the enterprises; and, (3) individual savings retirement accounts chosen by each employee (Chao and Dickson, 2001). At this point, the pension system was relying heavily on the basic PAYGO pillar, which was to provide a minimum standard of living for retirees and was to be financed by the enterprises, the employees, and the government through a combination of pooled funds and individual accounts. This decision reflects the growing prominence of a specific policy paradigm that has become dominant in China and in many other countries since the late 1980s (Brooks, 2002; Merrien, 2001). Before exploring the major pension reforms enacted in China since the early 1990s, we will set out the policy paradigm that has inspired them directly, while emphasising the ideational role of the World Bank. Although this organisation has not imposed this paradigm upon Chinese policy-makers, it has provided them with the intellectual and technical support necessary to the crystallisation of a more coherent reform strategy oriented towards advance funding and financial investment. As discussed below, specific economic and institutional factors militate against the implementation of this financial paradigm.

The financial paradigm and the World Bank

Like neo-liberalism itself, the idea that pre-funded individual accounts must supplant PAYGO schemes as the main source of old-age security has gained ground in most regions of the world since the 1980s (Blackburn, 2002). Beyond the multiple models of individual savings currently available, one can outline the common paradigm that underlines them (Blackburn, 2002; Quadagno, 1999). Grounded in an individualistic vision of protection at odds with social insurance-type solidarity, this paradigm states that investing payroll contributions in equity is beneficial to future retirees, because it would create higher 'return rates' than PAYGO schemes. Moreover, new saving schemes would stimulate economic growth by boosting national savings rates. Despite the fact that neo-liberalism usually is grounded in the idea of 'free choice,' many economists and financial experts openly support forced saving as a pragmatic way to promote economic growth while implicitly acknowledging the institutional legacy of compulsory PAYGO schemes enacted in many countries since the Bismarckian reforms of the late nineteenth century. Neo-liberal economists generally cite the reform implemented under Pinochet's dictatorship in Chile as the most successful example of 'pension privatisation' leading to compulsory savings (Béland and Waddan, 2000).

During the 1990s, the World Bank contributed to the propagation of the financial paradigm at the international level. In 1994, the World Bank released *Averting the Old Age Crisis*, a report that depicts public PAYGO programs as 'financially unsustainable' schemes that exacerbate intergenerational conflict as payroll taxes increase to compensate for the changing ratio of active versus inactive citizens. As an alternative to what is described as an excessive reliance on the PAYGO 'public pillar,' the report advocates a 'multi-pillar pension provision' system that should fulfil the functions of distribution (1), insurance (2) and savings (3) at the centre of modern pension systems: '(1) a mandatory state pension, run on a pay-as-you-go basis, paid from taxes and acting as a safety net; (2) a mandatory privately managed pillar, in the shape of a personal or occupational pension, fully funded and managed by the financial services industry; and (3) personal savings of a voluntary character' (World Bank, 1994: 237). Because the second pillar is not a genuine social insurance scheme but a compulsory saving plan, this 'multi-pillar pension provision' model is nothing less than an attempt to favour the rapid growth of both forced and voluntary savings. This report embodies the neo-liberal financial paradigm discussed above.

The year following the publication of *Averting the Old Age Crisis*, the World Bank, among other advisers, prepared several reports that analyse China's short- and long-term pension needs. These reports propose the creation of a unified, all-China urban 'three-pillar' pension system relatively similar to the model defined in *Averting the Old Age Crisis*. This reform plan includes a mandatory pooled fund including all SOE employers, administered by cities or provinces; mandatory individual accounts managed by the cities or provinces, funded by both employees and employers (transferable and fully vested after 15 years and fully funded after about 40 years); and voluntary supplemental savings accounts set up by profitable enterprises (World Bank, 1997).

Because China has not depended on sizable loans from the World Bank, this organisation has lacked the necessary political leverage to impose a specific reform option upon Chinese policy-makers. Nevertheless, the intellectual and technical support it provided (for example, the formulation of sound actuarial projections) certainly contributed to the propagation of the financial paradigm in China during the second half of the 1990s.[12] This organisation offered actuarial and economic advice while promoting this paradigm through the organisation of policy meetings and the publication of papers and reports. Beyond the influence from the World Bank, Chinese experts have paid serious attention to the pension systems of Chile and Singapore. Moreover, foreign pension consultants and economists (for example Martin Feldstein from Harvard University) have visited the country to promote the virtues of financial investment. These efforts may have favoured the emergence of a more coherent reform strategy in China, yet it is difficult to measure the level of consensus prevailing within Chinese policy circles concerning the viability of the financial paradigm.

Despite this remark, the financial paradigm has certainly gained ground in China since the mid-1990s. In 1995, the State Council issued Document Number 6 in an effort to clarify the available reform options and encourage the development of pooling and individual accounts in a non-systematic manner. The Document formulates two general reform models after grouping together various policy experiments that had been conducted at the local and provincial levels. City and prefecture governments were left with the option of choosing a reform design according to their own situations. Plan I focuses on individual accounts while Plan II emphasises pooling and economic solidarity (Chao and Dickson, 2001). Thus, Document 6 failed to promote the formation of a coherent pension system in China. Giving local governments the power to select their preferred reform model actually increased fragmentation by creating incentives for these governments to differentiate their schemes in order to maintain their control over pension funds (Smyth, 2000).

In coastal provinces such as Guangdong, Jiangsu, and Shandong, economic and administrative decentralisation also favoured the emergence of local and regional constituencies that attempted to veto the implementation of policies detrimental to their perceived economic interests. Regional and local officials tended to maximise control over welfare funds that could be invested so as to expand employment opportunities and create profitable investments that would enable them simultaneously to advance their careers and boost their own incomes (Selden and You, 1997). Thus, local officials were more willing to implement pension integration and choose the pension model that seemed the most appropriate for their region. This further demonstrates the direct impact of institutional decentralisation on China's pension policy-making. Facing this situation, and lacking administrative capacity to implement reforms, the State Council acknowledged the fragmented standards across cities and provinces. The national guidelines of the abovementioned Document Number 6 required that specific localities align their enterprise and individual contribution rates. It also stated that all localities should conform to the uniform standards by the end of 1997. In practice, the adoption of these standards has as yet only been sporadic (Smyth, 2000). Moreover, local governments have faced many problems in adopting the standardised contribution rates due to the discrepancy of economic growth across localities. As a consequence, the differentiation has led to the creation of hundreds of schemes all over the country, seriously handicapping labour mobility from SOEs to private enterprises (Chao and Dickson, 2001).

It was only in 1997 that the Chinese government formulated a unified pension reform model to be implemented across the country. In July of that year, the State Council issued the 'Decision on Social Pension System,' and stipulated that each enterprise could not contribute more than 20 per cent of the total wage as social pension funding. Individual workers had to pay 11 per cent of their wages into their personal accounts (Chao and Dickson, 2001). In this sense, the state further recognised the essential role of private savings accounts in the pension system. However, the 1997 decree failed to stipulate penalties for non-compliance (Huang, 2003: 189). This phenomenon can be understood in the general context of limited administrative capacity discussed above.

In practice, it proved difficult for cities to adjust to the required national contribution rates: authorities needed time to increase individual contribution levels and, therefore, to get SOEs' contribution rates down (Smyth, 2000). Even though the 1997 decree stated that individual pension accounts should be made portable, only some cities have adopted the policy. For instance, cities such as Tianjin now permit workers to withdraw their contributions from individual accounts if they move to another area; but this is far from being a universal practice. Thus, institutional decentralisation and economic fragmentation related to the reforms launched since the late 1970s meant that the 1997 decree could not favour the prompt development of a more coherent and integrated pension system in China.

Nevertheless, the establishment of the Ministry of Labour and Social Security (MOLSS) in 1998 illustrated the central government's apparent commitment to develop a more comprehensive social security system in China. In order to fight accumulated deficits in established pension pools, MOLSS and other responsible ministries have considered an increase in the proportion of social security expenditures in central and local authorities' budgets, issuing long-term government bonds for designated uses, selling state-owned assets to obtain cash, and raising money through lotteries (MOLSS, 1999). Some of these reforms have been implemented. For example, the State Council decided to increase the capital for basic pension in both municipalities and provinces (MOLSS, 2001).[13]

But these initiatives cannot hide the modest results of the pension reforms enacted during the 1990s. Overall, one must acknowledge that more than six years after the 1997 'Decision on Social Pension System', massive regional variations remain despite the fact that the old-age pension system – which generally excludes rural workers – covers a limited proportion of the overall population (Huang, 2003: 190). Unable to systematically promote bold pension pooling and advance funding, the Chinese government has been conducting various experiments or pilot projects. Among these initiatives is the pilot plan launched in the Liaoning province in December 2000. Confirmed by Premier Zhu Rongji in November 2001 (*People's Daily*, 2001), the plan includes both components of social pooling and individual accounts, which confirms the dominant policy path discussed above (Chen, Thomas, and Ming, 2001). It is probably too soon to evaluate the long-term results of this project.

In general, the implementation of the financial paradigm that has been promoted in China since the 1990s remains highly problematic in the current institutional and economic environment. According to this financial paradigm, individual savings accounts are supposed to provide the underpinning for a funded pension system and, through active investments, to generate the additional funds needed for future pensions. Most of the money paid into the individual pension accounts, however, does not reach independently managed investment funds, but is used to meet pooled funds' current pension deficits (the government sets the rate of return, which is lower than those on government bonds). Although the central state has recently sought to prevent local governments from using individual accounts to pay for current pensions, the funded individual account often appears as notional. Since 1999, more than 1 trillion Yuan has been taken away from individual accounts to pay for existing pensions (Huan Qui Shi Chang Shen Xi Dao Bao, 2003). This situation is related to the fact that it is difficult to find the economic resources to 'simultaneously cover current obligations and fund the individual accounts, especially when the existing pension system was running a deficit' (Rosegrant, 1999: 13). The institutional legacy of existing PAYGO schemes makes it difficult to implement the financial paradigm defined above. This feedback effect from previously enacted pension policies is especially strong considering the pressures to limit the increase in payroll contributions. Indeed, Chinese workers and employers could probably not finance the transition between PAYGO schemes and a fully funded system of individual accounts. Under the present situation, it actually seems problematic to just accumulate significant pension reserves, especially since the state lacks the administrative capacity to uniformly collect taxes from private and even public firms (Huang, 2003: 182).

Until 2001, funds could only be invested in banking deposits, government bonds, and a limited level of stock fund investments. It was only during that year that the state allowed pension funds to be invested into stock markets (People's Republic of China, 1998; Jing Ji Guan Cha Bao, 2003; Smyth, 2000). But these pension funds need more efficient capital markets in which to invest, and China's banking system and the stock and bond markets are not mature enough to offer an efficient capital market for operating a fully funded pension system (*The Economist*, 2002).[14] Inefficient, costly, and sometimes corrupted management is perceived as another source of pressure on the pension system (Selden and You, 1997).[15] In managing pension funds, China could obtain better results since it has a much smaller pension debt and much greater financial capacity to finance this debt than most other 'transition countries' (World Bank 1997). But the complexities of the current, decentralised Chinese policy-making system appear to create more obstacles to pension reform implementation. If provincial governments own SOEs, for example, only the central state has the power to issue debt, while local governments tend to control fiscal resources (Zhao and Xu, 2002). Hence, decentralisation and limited administrative capacities have hindered the Chinese authorities from investing pension funds in capital markets. Although societal factors such as demographic change, economic reforms, and the apparent domination of the financial paradigm have increased the need to reform existing pension arrangements, powerful institutional logics have complicated the effective implementation of pension-related measures adopted in China since the 1980s.

Conclusion

Despite the fact that China is an authoritarian regime different from democratic countries in which institutionalist theory was first framed, this article demonstrates that institutionalist insights about political structuration, if used adequately, can contribute to the study of Chinese pension reform. The article also shows how economic interests and policy ideas interact with institutional structures in determining policy outcomes. Through the analysis of pension reform in China, the close relationship between state capacity, previously enacted policies, and changing economic interests is explicitly revealed. Although there is a significant push for reform related to the financial paradigm reconstructed above, powerful economic and institutional forces decelerate or even deter effective policy implementation.

The impact of institutional variables on policy implementation is clear. China's relatively decentralised administrative system allows for local and provincial autonomy in the implementation of public policies, in that case, pension-related measures adopted by the central state. Thus, local and provincial governments have the power to shape policy outcomes at different stages of the implementation process. In this institutional context, economic inequalities between various provincial and local governments have an impact on administrative decisions that structure the implementation process. Overall, limited administrative capacity also creates obstacles at the implementation level while limiting the options for future reform. These prevailing administrative problems have largely hindered the concrete realisation of the pension reform decrees issued during the 1990s. As the increasingly dominant financial paradigm has justified the adoption of new reforms, specific institutional forces have made their implementation difficult.

Economic factors have also complicated policy implementation in the field of pension reform. In fact, the existence of notional individual accounts and high transition costs related to the shift from PAYGO financing to fully funded schemes represent strong economic and institutional obstacles to reform connected to previously enacted policies. Vested interests related to economic reforms enacted since the 1980s have also generated more obstacles to the successful implementation of state's pension reform initiatives. Private or non-state enterprises are less willing to participate in the pension system because they seek to preserve the economic advantages derived from marketisation.

In sum, administrative problems and feedback effects from economic reforms have exacerbated the fragmentation of the Chinese pension system rather than unifying it. In this context, the future of the world's largest pension system is largely tied to the construction of more effective administrative and supervisory infrastructures to operate it. The failure to implement sound pension reforms while effectively guaranteeing the economic security of urban workers and retirees may exacerbate social discontent, which in turn could undermine the authority of China's party-state.

Notes

1 China carried out its fifth national population census on 1 November 2000. Since the 1990 Census, the average annual rate of population growth has been 1.07 per cent.
The following article deals almost exclusively with the issues of aging and pension reform in urban settings only. Despite the creation of old-age insurance schemes in some rural areas, the rural pension system that has been sketched since the early 1990s is still relatively modest.

2 For a recent and partial exception: Huang, 2003.

3 For Hall and Taylor (1996), there are three types of 'institutionalism': historical, sociological, and rational choice. Although these approaches share some basic assumptions, they form three distinct perspectives on politics and policy. This article deals only with historical institutionalism, which is at the centre of current theoretical debates concerning welfare state politics.

4 According to Jane Duckett (2001), vested economic interests also play a central role in the implementation of urban health insurance reform in China.

5 On the one hand, various pension programs cover less than 10 per cent of the rural population. On the other hand, pension schemes cover almost 95 per cent of the SOEs (urban) workers. However, in non-state enterprises (collective or private), pensions cover only about half of the workforce (Smyth, 2000; Munnell, 1999).

6 In 1978, there was one retiree for every 30.3 employees, but the ratio has now climbed to one retiree for only 3.7 employees. If the current retirement ages remain unchanged, the ratio will increase further to one retiree for 2.4 workers by 2030 (Zhang, 2002). In 2001, for example, the central government spent 349 billion Yuan to subsidize basic pension expenditures due to insufficient capital in the pension system. This type of governmental subsidy will increase in the future (Huan Qui Shi Chang Shen Xi Dao Bao, 2003).

7 Among these, the scope of decentralization has been the greatest, while privatization efforts have been quite limited (Chao and Dickson, 2001).

8 During the 15th Party Congress of September 1997, President Jiang Zemin actually vowed to accelerate the pace of SOE's reform by making it ideologically legitimate to use a shareholding system to convert many medium and small enterprises into companies with mixed public–private ownership. In 1999 the NPC declared that the private sector was no longer just a supplement to the state-run economy but a key element of the national economy (Zweig, 2001).

9 As the Party further recognised the private sector's leading role in the economy during the 16th Party Congress of November 2002, there will be a significant increase in the number of shareholdings in the private sector (New York Times, 2002).

10 Many state-owned industries were money-losing enterprises before 1980 (Goldstone, 1995).

11 The compliance rates of private enterprises are low, particularly in foreign-funded firms. It is because local and provincial authorities are especially lax toward foreign enterprises, as they fear that strict compliance rules may convince these firms to relocate. To a lesser extent, relocation is also an issue concerning Chinese (private) firms, which may decide to move to another city or province to avoid high contribution rates. This logic is similar to the 'race to the bottom' prevailing in some federal systems (for example: Théret, 1999).

12 Interview with a senior economist from the World Bank, Washington, DC, May 2003.

13 In order to expand pension coverage, the Chinese government is still supporting a more extended participation of non-state enterprises (collective firms, private firms, foreign-funded firms, and Sino-foreign joint ventures) in the system. However, the governmental plan offers few incentives but a high contribution rate for the non-state firms (Zhao and Xu, 2002). Indeed, the first disincentive is the first pillar's 13 per cent payroll tax. The second and the most important disincentive is the low return rate on contributions to personal accounts. In 1999, the return rate was set to equal the 3-month time deposit rate (MOLSS, 1999: 106), which was 1.9 per cent. By the end of January 2003, 40 per cent of the social security fund (including pension money) was invested in the stock market (Jing Ji Guan Cha Ri Bao, 2003).

14 SOEs' difficulties have created another major problem within China's banking and financial system: the growth of non-performing loans in China's banking sector. The non-performing loans of the four largest state banks rose in recent years, from 20 per cent in 1994, to 22 per cent in 1996, to 25 per cent at the end of 1997 (Tien & Chu, 2000). Despite the 15th Party Congress finally making a commitment to address the problems of the banking and financial sector with some urgency, the banking system is still facing many difficulties which directly affect the restructuring of enterprises and stall the pension reform. The banks cannot restore their solvency unless SOEs' performance improves substantially; however, the high level of non-performing loans still makes it difficult for banks to provide the funds that enterprises need to restructure and improve their performance.

15 The accumulated pension funds had reached 30.5 billion Yuan but interests on the funds represented only 2.17 billion Yuan by the end of 1994. This constitutes an interest rate of only 7.9 per cent, which is far below the Bank of China's one-year savings rate of 11.0 per cent.

Acknowledgements

The authors wish to thank Sarah Brooks, Jane Duckett, Michael Hill, Jinxin Huang, Stephen Kay, Angela Kempf, Patrik Marier and two anonymous reviewers for their comments on earlier drafts of this article.

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