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## **Dualistic Economic Structure and Unemployment in China**

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**Abstract:** China's red-hot economic development in the past three decades can not cover its serious unemployment problem in both urban and rural areas. Poor rural labor surplus keeps flooding into cities to join the employment competition with more than 20million unemployed urbanite already in the unemployment cadre. Such process compels municipal governments to establish barriers and reinforces the segmentation of rural and urban labor markets. Immediate and effective solutions to unemployment should be taken to facilitate the transformation of Chinese economy from a dualistic one to a unitary one.

**Key words:** unemployment, China, dualistic economy, rural and urban laborers

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## **Dualistic Economic Structure and Unemployment in China**

### **Introduction: The Reality of Unemployment in China**

Initiating its far-reaching opening and economic reform from 1978 and achieving an average GDP growth of 9% per year, China's booming economy seems to have painted a spectacular future for the largest population of the world. It is true that reforms in agriculture, urban housing, taxation, medical care and state-owned enterprise have created numerous jobs and considerably enhanced people's living standard. However, the scenery behind the rosy picture is not so stimulating. According to the statistics from World Bank, China's labor force accounts for 26% of the total labor population in the world, while the proportions of China's natural resource and capital resource are less than 10%.<sup>①</sup> Because of the complexity of China's economy structure, during the transition from a central-planning economy system towards a market-oriented one, the demand of various job seekers in both urban and rural areas of China significantly outstrips the supply of new employment opportunities. At the same time, many job openings can not find enough qualified candidates to match them. Severe unemployment situation, both in the rural and urban areas, has reinforced the segmentation between China's urban and rural labor markets and such ingrained division in turn impedes the free flow of labor force from agriculture sector into industrial

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<sup>①</sup> China Labor E-Bulletin. 2004 "An Overview of Unemployment in China 2003"  
IssueNO.16 .<http://www.china-labour.org.hk/public/contents/article?revision%5fid=18273&item%5fid=8544>

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sector.

On one hand, municipal governments have already faced complicated urban unemployment problems. On the other hand, driven by prospects of higher pay and better life quality in cities, rural surplus laborers continuously flood into urban areas. In the long run, it would become more and more difficult for China's current dualistic economy to transform into a healthy unitary one. Therefore, strong and effective measures should be taken to tackle the unemployment problem in both side of Chinese economy.

Generally speaking, the unemployment rate is defined as the percentage of unemployed workers to the total labor force. However, the inaccuracy of statistical data tends to heavily underestimate the unemployment problem in China. According to the Ministry of Labor and Social Security of China, during the recent 6 years, the official unemployment rate has risen from 3.1% in 2000 to 4.2% in 2005<sup>②</sup>. Actually, considering the calculation terms and method, these official statistics can be misleading and this data can only be labeled as official urban registered unemployment rate, which is based on local governments' monthly or annual report of labor rather than on scientific surveys. Unemployment populations in several important sectors are omitted. First, and the most important, the great number of laid-off unemployed workers who are receiving minimal living benefits from state-owned enterprises (SOEs) and collectively-owned enterprise (COEs) is not counted.

Second, these data only covered the unemployed who were 16-45 female and 16-50 male and those who had officially registered at local administrative agencies in urban China;

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<sup>②</sup> Wang Nan.2006. "Some thoughts about China's unemployment problem". Contemporary Economics and Finance. March Issue. 39-41

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and third, the official data also exclude the 150 million rural surplus workers, who are just holding temporary or seasonal jobs or still looking for employment in cities. According to several scholars' estimation and inner governmental data, the real urban unemployment rate in China has exceeded 10%<sup>③</sup>.

Serious and complex unemployment is a universal problem in less developed countries (LDCs). However, unlike periodical unemployment in developed countries, which is generated by the lack of aggregate demand, manifested by periodical economic crisis, and can be successfully solved through the expected recovery of economy, unemployment in LDCs has more structural reasons and can not be simply alleviated by rapid economic growth. In the case of China, a striking growth of GDP seems to be incapable of promoting employment. For example in 2003, although its economy growth rate reached a 10% height, facing a 240 million of new labor supply, China was only able to satisfy the employment need for 80 million people.

The main purpose of this paper is to analysis the interaction between China's unemployment situation and dualistic economy structure in rural and urban areas, primarily using Lewis Model of dualistic economy. It also defines the types of unemployment in China, presents relative data, and identifies the specific reasons to each one. In the final part, this paper brings out several policy suggestions to tackle the unemployment problem.

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<sup>③</sup> Li Shi, Hiroshi Sato(editors) 2006 "Unemployment, Inequality and Poverty in Urban China" Routledge Studies on the Chinese Economy volume 19. Taylor and Francis Group

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## **Section 2: Lewis Model of Dualistic Economy and Labor Markets Segmentation in China**

### **(1). What are the Main Arguments of Lewis Model of Economic Development?**

In 1954, American Economist Arthur Lewis (Princeton University, and Nobel prize Winner in Economics) published his famous paper “Economic Development with Unlimited Supplies of Labor” and brought about the model of dualistic structure economy. Lewis claims that there are two distinct economy sectors in a typical developing country, the traditional or agriculture sector and the modern or industrial sector. The former is characterized by abundant labor force, low labor productivity, subsistence level wage rate, slow growth of output and great dependency on natural conditions. The latter one is characterized by advanced technology, fast growth, the positive marginal product of labor and above subsistence level wage rate. In this model, there are serious hidden unemployment and underemployment in the majority of developing countries. It would be beneficial for the available labor force to join high capital labor ratio industries. Economic development results from structural changes and the expansion of the industrial sector, which entails a continuous influx of labor force from the agriculture sector.

There are several important assumptions in Lewis Model that we should clarify before further explanation is given. ① The agriculture sector mainly uses labor and land as production factors, while industrial sector uses labor and capital; ② There are apparent

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labor surplus in agriculture sector, which provides unlimited labor force for the growing industrial sector; ③Differences in wage rate is the major reason for labor migration ;④ Increment in total product would be reinvested by industrialists for future industrial expansion.

For economic development to happen, the higher wage rate in industrial sectors keeps attracting surplus labor force from the traditional sector without affecting the total product output in it. Then positive marginal product of labor in manufacturing sector increases the total industrial product and brings more profit to industrialists. Industrialists reinvest in their factories and provide more employment opportunities, which continue absorbing the redundant labor force in agriculture sector. This cyclic process will keep going until surplus labor force in agriculture has been fully transferred to the industrial sectors and marginal product of labor, wage rate in both sectors have reached the same level. In the long run, the proportions of savings, profit and capital accumulation in gross domestic product will all go up. Finally, such a dualistic structure in economy will disappear. Based on the observation of history, Lewis Model can be empirically verified. If deep structural economic reform and a health economic growth are desirable, the free flow of labor force between rural and urban labor market should never be harnessed and the creation and allocation of employment opportunities would never be over-emphasized.

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## **(2). Formation and Current Situation of China's Dualistic Economy:**

With a more than 75% rural population and distinctions in the production and lifestyle between the traditional sector and modern sector, Chinese economy is a typical dualistic one. In the rural area, where labor is the primary factor of production, people make a living by participating agricultural or handcraft work and sometimes sell their product in the markets of cities and towns, receiving a miserable and unstable income. In the urban area, where industrial infrastructures have been fully developed during the past 50 years and capital is more available, workers in factories and employees in companies enjoy a much higher wage rate as well as necessary welfare and benefits provided by their employers and the government.

Tracing back contemporary Chinese history, the formation process of China's dualistic economy can be owed to the adoption of Soviet Union Model and heavy industry-oriented development strategy, which was pursued vigorously during the central planning period. After the foundation of PRC in the 1950s, besieged by domestic socioeconomic turmoil and isolation by western powers, the central government identified urgent needs to establish a reliable and complete modern industry to ensure the solidity of a newly-born regime. Yet at the beginning of industrialization process in China, the proportion of industrial output in GDP was so low and the industrial product categories were so limited that it was impossible to accumulate enough capital for further development by solely depending on industrial production itself. Therefore, the dominant traditional agriculture of China became the main

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source to accumulate capital for generating the industrial sector. Considering there were no existent means to transfer the capital through market-embedded channel, the procurement of capital could only be realized by implementing a biased transfer policy. Such policies include restricting and cutting down the prices of agriculture product, limiting rural residents consumption with subsistence level of wage rate, and taking advantage of the huge scissors gap between industrial and agriculture products. According to National Bureau of Statistics (NBS), from 1953 to 1978, the government received 510 billion Chinese yuan (about 63.75 billion dollars) from the scissors gap between prices of industrial and agriculture products<sup>④</sup>. China's government high-intervening development mode has succeeded in establishing its basic industrial system within a surprising short time. What was to blame is government's unawareness to shift its strategic focus to other economic sectors after the establishment of industrial sector. Under this circumstance, the agriculture sector was so heavily deprived of that the formation of two separate economy sectors was inevitable.

Based on economic development analysis of the world, there are mainly three ways for the transformation of dualistic economy into a unitary one. The first one is called the natural industrial growth mode, which was implemented by the US and Britain. In their cases, along with continuous economic growth, dualistic economy would automatically and eventually disappear. The second way is through input of large amount foreign capital into the productive industrial sector. Development policies concentrated on the growth of the modern sector, while leaving the rural area still undeveloped. This mode is illustrated in Brazil. The

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<sup>④</sup> Wikipedia, the free encyclopedia "Economic History of China"  
[http://en.wikipedia.org/wiki/Economic\\_history\\_of\\_China#The\\_First\\_Five-Year\\_Plan,2C\\_1953-57](http://en.wikipedia.org/wiki/Economic_history_of_China#The_First_Five-Year_Plan,2C_1953-57)

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last way is intensifying government's intervention in economic development. In which agriculture and manufacturing, urban and rural sectors appear to be two completely separate domains, firstly traditional sector is heavily deprived of, and then it is saved by a mature and productive modern sector. China fits into this model well<sup>⑤</sup>.

### (3). The segmentation of China's urban and rural labor markets

Above analysis informs us that for the elimination of dualistic economy structure in LDCs, the influx of labor force from agriculture sector into industrial sector is a crucial and necessary historical phase. Yet there exists evident segmentation between China's urban and rural labor markets, which have markedly impeded the flow of rural labor into the urban economic sectors. Although rural and urban sectors are forcefully connected by the potential gains from trade between them, the two labor markets are still treated as separate entities. The division between state and non-state ownership sectors, social security (including medical coverage, pensions and unemployment insurance), and related topics such as housing, education, and other social services all differ drastically between China's rural and urban economies.

Motivated by income and welfare incentives, many redundant rural laborers began to flood into urban area. However, facing the heavy burden of existing urban unemployment, municipal government laid out a series of restrictive policies to reinforce the barrier between rural and labor markets. Some characteristic policies include imposition of various taxes and fees on migrant laborers, implementation of enormous discrimination employment policies in

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<sup>⑤</sup> Heping Gan, Zhong Jian. 2005 "Using Lewis Model to analyze the transformation of Chinese Economy" Value Engineering No.2 19

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urban area and strict administration of urban household registration system. Details of each means are given below.

①Arbitrary enhancement of labor cost by local government. Financial deprivations have always been viewed as most instrumental measure to check the migrant labor flood. Many fast developing cities of China have formulated regulations and policies to charge directly rural labor or indirectly their employers different items of fee and tax, such as fee for the issuance of employment license, temporary residence fee in cities, mandatory physical check-up fee and migrant population birth control fee. For instance, a survey conducted by economic research center in Beijing University in late 1990s found that, enterprises in Shanghai are requested to pay the government, for each rural worker they hire , an annual miscellaneous fee amounted to 890 yuan, equal to 20% of a worker's annual wage. What is even worse is some municipal authorities manipulate these policies to extract migrant workers' income⑥. So many enforcements deteriorate the life quality of migrant laborers and greatly enhance the employment cost for urban employers.

② Government has also implemented discriminatory employment policies to exclude migrant workers from certain professions in urban sectors. In some cases occupational stratification has been institutionalized. On one hand, some municipal governments have implemented regulations to protect urban residents by reserving specific job categories for them and make sure they are not underpaid compared to outsiders. This is especially true for employment opportunities in those profitable monopolistic professions such as power supply

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⑥ Xuguan Feng. 2001 "Segmentation of China's labor markets and hidden unemployment in rural China"  
Economics Scholars, Fudan University

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and telecommunication, where urbanites enjoy preemptive rights to get hired. For instance, in late 1990s, the labor bureau of one of Beijing's district stipulated that at least 35 types of jobs should not be opened to migrant workers<sup>⑦</sup> On the other hand, the range of employment opportunities for rural labor has been restricted to positions featured by "four most undesirable" (most tiresome, most dirty, most dangerous and most humble) for urban citizens. And usually, migrant workers receive a much lower wage compared to urban workers holding similar jobs.

③ Implemented as a traditional basis of social system since ancient China, strict regulation of household registration also plays a vital part in the segmentation of labor markets. In the central-planning economy period, even for visiting urban relatives, peasants should apply for permission letters from the administration office in their villages, let alone for job-hunting in the cities. Nowadays, a more market oriented economy still has inherited such a powerful regulatory means. Without an urban household registration, migrant workers would encounter numerous unexpected difficulties in their urban life. Such examples are getting into qualified primary or middle schools for their children, or receiving adequate medical benefits from employers and government. As a result, rural and urban labor forces are actually participating in a gravely unfair competition for limited jobs.

All in all, the governmental actions to control the flow of rural labor are generated by a purpose to allocate more jobs for urban workers and give priority to solve urban unemployment problems. Thus, to clarify the scenario behind such a severe segmentation

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<sup>⑦</sup> Shuifeng Song.2003 "Policy Issues of China's Urban Unemployment". Contemporary Economic Policy. Volume 21,NO.2.

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between rural and urban labor markets, analysis should be made in both terms of the rural labor supply and demand of labor in urban sector. Not only rural unemployment but also urban unemployment have contributed to the perplex problem. The following section will concentrate on the issues of unemployment in both traditional and modern sectors, and further identify the reasons of each type of unemployment within China's transformational economy structures.

### **3. Analysis and Classification of unemployment in rural and urban China**

With a huge population base, the annual increment of new laborers (those who become legally old enough to be counted into labor force) in recent China is estimated to be 9 million, almost equal to the population of a medium-size European country. Also considering 11 million laid-off workers and 150 million redundant rural laborers, China is experiencing unprecedented heavy unemployment pressure.

### **Four Types of Urban Unemployment of Contemporary China:**

#### 1) Systematic Unemployment:

Laid-off workers from State-owned Enterprises (SOEs)

One of the main causes of unemployment in China today stems from the restructuring of SOEs. Before the reform, state ownership was dominant in the modern sector. These relics of the planning economic system once promised cradle-to-grave job security for their employees, and enjoyed massive state funding and support. China used to be proud of its low urban unemployment rate in the former central-planning economy, when employment was

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wholly arranged by the administrative dictation from government and operational aim of all-level enterprises was the maximizations of employment and output. In this sense, by sacrificing business profits, enterprises (mainly the SOEs) undertook the responsibility of allocating employment which was supposed to be adjusted by a market system, Consequently, redundancy and saturation of employment in SOEs brought vital drawbacks such as debt burdens, corruption, outdate production and most seriously, large amount of hidden unemployment into Chinese economy. Since China's strategic introduction of market economic mechanism, SOEs' vulnerability in fierce market competition became more apparent. The transformation of operational aim to profit maximization entails previous hidden unemployment inside SOEs to change into open unemployment. Thus, trimming excess staff stood out to be the first step for SOEs to establish modern management system and prepare for competition with private enterprises, joint ventures and foreign-funded companies in a globalized market. From 1998 to the end of 2002, the accumulative statistical number of laid-off workers is 26 million, many of whom are women workers, workers older than 45 and those with limited skills.

For example, China's two largest oil producers, PetroChina, has cut about 63,000 jobs since 2000. China Petroleum has also cut 22% of its workforce<sup>⑧</sup>. These people have lost not only their so called "iron-bowl" (food and clothes expenses source) but also social security benefits all together. Although re-employment assistance centers were founded ( but later removed in 2004) in the majority of SOEs to help laid-off workers seek new employment,

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<sup>⑧</sup>China Labor E-Bulletin. 2004"An Overview of Unemployment in China 2003" Issue NO.16 .<http://www.china-labour.org.hk/public/contents/article?revision%5fid=18273&item%5fid=8544>

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only a small minority have received substantial help (e.g in-time training for new skills) from re-employment institutions. Although massive amounts of state funding have been allocated to SOEs to slow the process of laid-off restructuring and to alleviate the hardship of laid-off workers' life conditions, pervasive corruptions in management led to the rare materialization of retrenchment compensations for laid-off labor. The re-employment rate among laid-off labor has not exceeded 50% in recent ten years.

② Structural Unemployment due to industrial updating and global competition.

Structural unemployment is defined as the mismatch between job requirement and skills or availability of labor force. Frequent adjustment in industrial structure, which includes continuous emergence of new industries and the washout of old industries, always accompanies rapid economic growth. For contemporary China, especially after its entry into WTO, such extensive adjustment has aggravated unemployment. The phenomena “lack of jobs for many people” and “lack of people for many positions” coexist in some professions. First, China's traditional resource-consuming production mode has resulted in the unduly exhaustion of many natural resources.

For example, among China's 426 mineral-based cities, more than 50 have been fully utilized by 2000. Some munitions factories and old industrial bases also went bankruptcy because of inadequate supply of raw materials and isolated location. Secondly, demand of domestic competent professionals is very urgent in some brand new industries such as international trade, finance and banking, biological engineering and informational technology, where job openings are usually occupied by imported qualified talents from abroad. Last but not the least, operating on the principle of fair competition, a WTO membership has forced

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China to face the reality of international specialization of labor. Those industries which do not have comparative advantage over foreign competitors, such as automobile and software industries, have encountered most significant impact from the shrinkage of their market share and short of innovation impetus. Employment in these industries has reduced.

③Frictional Unemployment (especially common in young job-waiters)

This type of unemployment is always present in an economy, resulting from temporary transitions between jobs, professions and locations made by workers and employers or from workers and employers having inconsistent or incomplete information. Currently, the most severe and complicated frictional unemployment happens among fresh college graduates. Since the reform of high education system in 1999, dramatic enlargement of public colleges' enrollment (almost with an annual increment of 0.7 million) and proliferation of private colleges have made college education much more available. Nevertheless, limited qualified faculty, outmoded infrastructure and obsolete curriculum have not secured the competency of college graduates in their future careers. On one hand, high college tuition and traditional self-esteem idea as social pillars among college students increase graduates' expectation of future jobs (e.g in propensity of location, salary, social status, welfare). On the other hand, the absence of career planning instructions results in graduates' inefficiency of job hunting and unrealistic self-position. Requirement of previous work experience from employers and lack of position mobility inside some enterprises have also contributed to the employment trap for college graduates. For instance, this year 4.13 million college and university

graduates from flooded into employment, yet by this July, only 49% of them have registered as employed. According to the statistics from Ministry of Education, the unemployment rate among 2005 college graduates has reached 30%, 7% higher than that of 2003. Together with veteran youth and other youth lower-diploma holders, currently there are 3 million unemployed youth in urban China, constituting 23% of a 13 million urban unemployment population.

④ Voluntary Unemployment related to the above three types of unemployment

This category of unemployment consists three parts: laid-off workers who hold a traditional central distribution view about employment and passively wait for jobs regulated by government or their former “work unit”; workers in less competitive industries who are unwilling to acquire new skills for future employment; recent college graduates and other migrating labor who would rather stay idle than to work in rural areas, at a so-called disgracing social status, or with a much lower salary rate compared to their expectations.

Following is the recent calculation and estimation of urban unemployment rate (1995-2002)<sup>⑨</sup>

Population (million)    Rate( percent)

Year	1995	1996	1997	1998	1999	2000	2001	2002
<b>Registered Unemployment (Population/ Rate)</b>	<b>5.20 2.9%</b>	<b>5.53 3.0%</b>	<b>5.77 3.1%</b>	<b>5.75 3.1%</b>	<b>5.95 3.1%</b>	<b>6.30 3.6%</b>	<b>6.81 3.6%</b>	<b>7.70 4.0%</b>

<sup>⑨</sup>Angang Hu. 2002.05.17 “the Largest Employment Competition in the World: Gravity of China’s Unemployment”. Century China. <http://www.cc.org.cn/>

<b>Laid off unemployment Population</b>	<b>3.38</b>	<b>3.56</b>	<b>8.15</b>	<b>8.77</b>	<b>9.37</b>	<b>10.0</b>	<b>11.0</b>	
<b>Migrant workers unemployment population</b>	<b>0.55</b>	<b>0.60</b>	<b>0.88</b>	<b>0.93</b>	<b>1.06</b>	<b>1.00</b>	<b>1.2~1.50</b>	
<b>College and university graduate unemployment</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>0.70</b>	<b>0.80</b>	
<b>Actual unemployment Urban Population</b>	<b>8.01~9.13</b>	<b>9.66</b>	<b>14.73</b>	<b>15.41</b>	<b>16.18</b>	<b>17.65</b>	<b>18.81~19.11</b>	<b>19.00</b>
<b>Actual Unemployment Rate</b>	<b>4.1~4.7%</b>	<b>5.0%</b>	<b>6.2%</b>	<b>7.5~8.5%</b>	<b>7.9~8.9%</b>	<b>9.0%</b>	<b>9.1~9.5%</b>	<b>10.5%</b>

## (2). Hidden Unemployment in Rural China

Hidden unemployment is defined as phenomenon that workers maintain nominal labor relationship with employers, but actually do not work at all or do not work for enough hours. The fundamental roots for unemployment in rural areas of China, basically hidden unemployment, are the serious lack of arable land, low literacy of rural population, improvement in agriculture technology , poor implementation of birth control policy and the weakness for town and village enterprises (TVEs) to absorb labor force, compared to a large surplus rural labor force. Here we can describe it as “five people plow a piece of land providing a three-people workload”. From 1990 to 2003, the employment rate in town and village population decreased from 73.7% to 65.6%. It is estimated that within 20 years, the unemployment population in rural China would rise from 150 million to 200 million.<sup>⑩</sup>

In the former central planning economy, when the management organization in rural China

<sup>⑩</sup> New Beijing News. 2006. “2010: a future of unemployment for 10 million new laborers”. Nov 08<sup>th</sup>. <http://finance.163.com/06/1109/08/2VFM6DDR00251OB6.html>

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was People's communes and annual output was fixed by governmental agriculture plan tasks, farmers incentives for higher production were generally restricted by the commune's purpose to evade higher task requirements from authorities in the next year if output had exceeded the assigned number. Thus, much land was wasted and left idle, labor force became more abundant. After 1978, although the replacement of the household contract responsibility system in agriculture had endowed farmers freedom to make their own output plan, the undue increase of rural population and rapid shrinkage of arable land in process of rural construction even worsened rural hidden unemployment. Governmental permission of TVEs once helped to solve part of the labor surplus, however, difficulties in finance, technology update, and managerial improvement made TVEs' contribution only temporary and trivial. Large discrepancy between rural and urban wage levels and life styles keeps attracting rural labor. The most effective therapy to rural unemployment still lies in the eradication of barriers between rural and urban labor markets.

#### **4. Policy Suggestions to Unemployment Problem of China**

Threats to a healthy transformation from dualistic economy to a unitary one and the social unrest that could result from current high unemployment rates compel that the government should devote considerable attention to this issue. A prosperous economy is just the prerequisite for the increment of employment, yet the alleviation of unemployment can not simply depend on economic growth, pragmatic employment policies are more necessary and effective. Economic development includes not only economic growth in

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terms of GDP output but also optimization of economic structure and enhancement of economic quality. To successfully cure the unemployment in China, the initiative should be taken by the urban sector first.

(1) Promoting the growth of tertiary industry.

Creating jobs is a fundamental solution to China's unemployment problems. However, once the scale of economy has taken on in mass-production stage of primary and secondary industries, reduction of employment is inevitable. With same amount of investment, tertiary industry is capable to provide much more employment opportunities than primary and secondary sectors and its skill requirement for workers is also lower. Hence, employment potential in tertiary industry should be fully utilized. During the past two decades, the tertiary sector (or service sector), which includes restaurants, retailing, leisure, transport and entertaining industries, is the only sector that has experienced consistent increase in employment. Its employment share increases from 12.2% in 1978 to 27.7% in 2001, with an annual growth rate of employment of 5.9% compared to counterparts of -1.2% and 2.4% in primary and secondary industries.

Yet viewing the experience of other countries, China's service industry can still be described as undeveloped. In US, the output of tertiary sector contributes more than 70% of the total employment, even in developing countries such as Indonesia, the share is also between 35% to 40%. For China's tertiary industry to facilitate employment, efforts can be made in two aspects. One is promotion of urbanization and wholesome of market system because spread out of service sector depends on a mature market economy in urban areas. Another means is diversification of the category of service sectors. Both governmental

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authorities and investors should not confine themselves with the traditional idea of service such as hospitality and retailing, they should be encouraged to explore new territories such as managerial consulting, microfinance, insurance and so on.

(2) Increase financial support and favorable policy for non-state sector, especially small and medium-sized companies in private sector

Non-state sector in China basically includes private companies, joint ventures, foreign-funded companies. It has been playing an active part and become the main source in the re-employment of laid off workers. From 1997 to 2001, SOE jobs decreased by forty three million, and the private sector and non-state sector jobs increased by 16.5 million.<sup>11</sup> In Shanghai, 85% of the employment increment from 2004 to 2005 was attributed to non-state sector. But consider the unsolved unemployment population, the non-state sector is just not growing fast enough to satisfy the employment need. One reason is the unbalanced distribution of state funds among SOEs and business in other property forms.

Worrying about several common drawbacks among private companies such as lack of strong corporate governance system, poor risk-resistance ability, low credit rate and moral constraint, commercial banks are unwilling to provide loans to private sector and roughly three-fourths of bank loans in China has gone to SOEs in order to rescue them from bankruptcy. Actually, the default rate of loans from commercial banks to small and medium companies is as high as 32.11% in 2003, much higher than the average rate among all businesses. Thus, to avoid the vicious cycle of lack of funding and high default possibility in private companies, effective measures should be sought to provide more loans

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11 China Labor E-Bulletin. 2004“An Overview of Unemployment in China 2003” Issue NO.16 .<http://www.china-labour.org.hk/public/contents/article?revision%5fid=18273>

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for the expansion of private sectors. For example, gearing to the characteristics of private companies, commercial banks can make positive changes in their credit rating, transaction procedures and risk management. While the government should make efforts to formulate a complete set of regulations and laws in microfinance and build up social credit system to increase the transparency of financial information. Moreover, an efficient social security system should be fully established both in governmental level and inside private companies, to provide benefits such as medical care, housing subsidy pension and insurance to non-state employees. In this way, the feeling of insecurity for non-state sector employment would decrease

(3) Readjust employment concept and prepare laborers with practical job training and education

This is particularly necessary for majority of laid-off workers and college graduates who can be categorized into frictional or voluntary unemployment. In the first case, because of the relative low literacy and limited skills among laid-off populations, they tend to encounter more failures during their search for re-employment. At the same time, influenced by traditional concept of labor and employment, the “iron-bowl” provided by government, many old-aged laid-off workers have also lost initiatives to search for other forms of employment by themselves. Pride generated by once being employed by the government, fear of competition and great intensity of labor, insecurity of life without various welfare and propensity to permanent jobs drive them to give up any employment opportunities other than jobs from SOEs. They only passively depend on the re-employment centers in their former work units in hope of a distributed job from

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government in the future. In the second case, considering their expensive investment in higher education, lacking career planning instructions and mature perspective of employment, college graduates would rather wait at home than lower their requirements about a decent job positions. Both dilemmas entail a significant transformation in the concept of the meaning of employment the two groups, which calls for cooperation among governments, universities, community care centers and SOEs. Lectures and training on job-hunting skills and diversification of employment should be integrated into the curriculum of universities. Employment centers in SOEs should ensure the implementation of benefit funding as well as lead laid-off workers to search jobs actively. Other training programs inside private companies, foreign-funded companies and joint-ventures should also be established. Both education and job training would shift labor supply from the low-demand, low-skill category to another higher-demand, higher skill category, thus improve employability and productivity.

Meanwhile, efforts should also be made to solve rural unemployment. Generally, means can be classified into three forms: with land in villages, without land in villages and without land outside villages. The first one means expanding agricultural capability to absorb laborers by large investment in production means, diversification of agriculture categories from merely plant production to mixture of livestock breeding, fishery and so on. The second one means promoting the development of town and village enterprises (TVEs) in order to allocate more rural laborers into industrial sectors, this entails dissemination of scientific management knowledge and technological updating in rural areas. The last solution means the migration of rural labor workers into urban areas, whose success

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depends on capital accumulation and creation of new jobs in urban areas.

## **5. Conclusions and Summary**

There are four principle goals for governmental policies in macroeconomics: economic output growth, stability of prices, full employment and balance of international payments equilibrium. Theoretically, all of them should be concerned in the policy-making process of government. But at different stages of economic development, policies should have different emphasis in these four goals. In the soft landing period at early 1990s, China's primary macroeconomic policy was stabilizing prices and controlling inflation. After 1997, the policy focus shifted to the priority of economic growth.. According to the most recent five-year plan work outlines from Labor and Social Security Bureau of China in November 2006, by 2010, the total number of China's labor force would exceed 830 million. In the near future, full employment should be pursued as the most fundamental state policy

As a typical dualistic economy, Chinese economy can be described and predicted by Lewis Model of economic development. Because of its large population and imbalanced distribution of labor in rural and urban areas, the marginal productivity of rural labor is almost zero and the supply of rural labor for industrial growth seems to be unlimited. The transfer of labor force from rural to urban areas is unavoidable historic period for the modernization of China. To eliminate the barriers of labor transfer and build up a united labor markets throughout the country, it is necessary for municipal governments to gradually loosen the strict regulation of labor flow. What is more important is a proper settlement to both urban and rural unemployment problems. Solutions for laid-off , structural, frictional and voluntary unemployment in urban areas lies in industrial capital

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accumulation, proliferation of non-state sectors and the rationalization of employment concept and improvement in labor qualities. As supplementary means, diversification in agriculture production and expansion of TVEs can also contribute to reduce the absolute surplus of rural laborers. Each policy would not have a big impact on the unemployment problem, but with all of them working together, the overall result can be significant.

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