



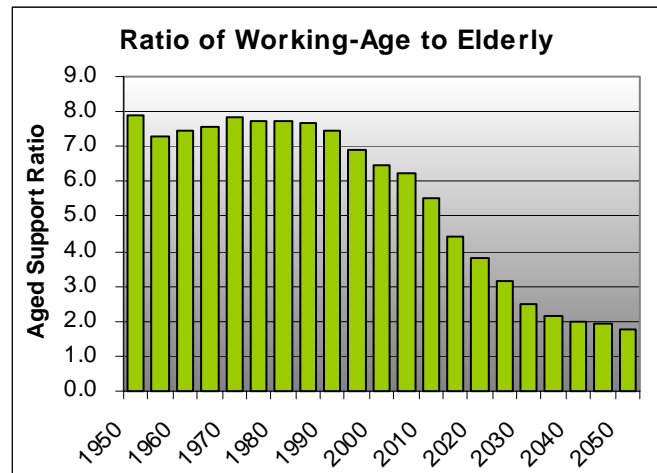
## Paying for the Aging Revolution in China

Will China grow rich before it grows old? That is the question on many minds these days considering the demographic transformation about to unfold in the Middle Kingdom. Over the next 35 years, while China strives to preserve strong growth levels, further link its economy with the global economy, and maintain social and political order, Beijing must also contend with an aging and diminishing work force. By 2040, when China's median age will rise to 44 years, the ratio of elderly to youth will be a remarkable two to one. There will be 10 percent fewer working-age adults than there are today, rising to 18 percent fewer by 2050. China's continued economic growth, not to mention political and social stability, could hinge on the government's ability to prepare for this demographic transformation. Is China ready for this imminent "age wave?"

### The population problem...

Today China's youth segments are still robust; workers are still numerous; and the absolute numbers of people are still growing. In fact, the most significant dilemma, currently, is to find enough jobs for the 10-15 million new people added to the workforce each year. In the next few decades all of these trends will reverse. The total population will peak and begin to decline, beginning around 2030. The number of working-age adults will fall, causing the worker-retiree ratio to plummet. By 2050, the number of Chinese aged 60 to 79 will triple, while those over the age of 80 will grow more than eightfold, reaching nearly 100 million. The immediate challenge for Beijing, then, is to maintain the economic growth fueling rising standards of living while preparing for a growing dependent elderly population. It will have to accomplish this goal without overburdening taxpayers or overwhelming families.

For some time, experts have been warning about the impending crisis for Europe and Japan in the face of graying populations. However, these are well-developed, affluent societies and economies. As Richard Jackson, director of the CSIS Global Aging Initiative, noted at a CSIS Global Strategy Institute Forum, "China is about to undergo a stunning demographic transformation. This transformation, one that took the United States and Europe 150 years to experience, will occur in China in just one generation."



The number of working-age adults (aged 15-59) available to support each Chinese elder (aged 60 & over) is declining rapidly. (Source: United Nations Population Projections, Constant Fertility Scenario, 2003.)

### The cause...

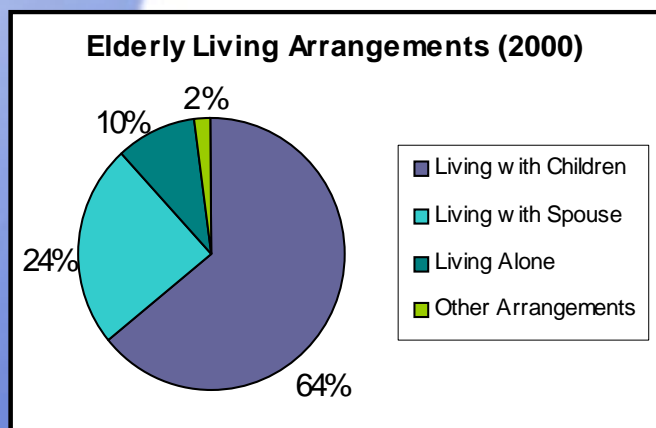
The two forces behind this aging revolution are similar to those in Europe -- the Chinese are having fewer babies, on the one hand, and living longer, on the other. The overall fertility rate has fallen from 5.8 babies per woman in 1970 to 1.8 today. In Beijing and Shanghai, the fertility rate is as low as 1.0 -- the lowest in any population or society ever recorded. Although the one-child policy is an obvious explanation for this falling fertility, rising affluence across China is also driving down birth rates. Furthermore, improved sanitation, healthcare, and nutrition associated with rising affluence have brought about a dramatic increase in life expectancy nearing many developed countries.

### Caring for the elderly...

In the absence of any functioning wide-based pension system, demographic trends spell real trouble for the Chinese government and economy. A recent report by the CSIS Global Aging Initiative puts it this way, "The aging of its population will test China's ability to provide for the old without imposing a heavy burden on the young."<sup>1</sup>

<sup>1</sup> Jackson, Richard and Neil Howe. *The Graying of the Middle Kingdom*. CSIS and The Prudential Foundation, 2004, pp. 6.

Traditionally, the younger generations of large Chinese families have accepted the responsibility of caring for the elderly. In 2003, 64% of elderly Chinese, aged 65 or over, lived with their children. How will the next generation of workers adjust to the pressures of single-handedly caring for their own children as well as two parents and four grandparents? Demographers call it the "4-2-1 problem."



Most Chinese elders still live in extended families with their children. (Source: Jackson and Howe, 2004.)

Of course, this assumes that children will accept the responsibilities of caring for their aging parents. As young rural workers leave en masse for the cities where per capita income is three times higher than in the countryside, traditional family structures and values are eroding. Furthermore, the legacy of the one child policy will leave its mark on the pampered single-child "little emperors" unable to find wives. Illegal, sex-based abortions and infanticide have resulted in a disproportionate male to female ratio in China. This shortage of eligible bachelorettes will translate into a shortage of daughter-in-laws, the traditional caregivers for the elderly.

### Preparing for the age wave...

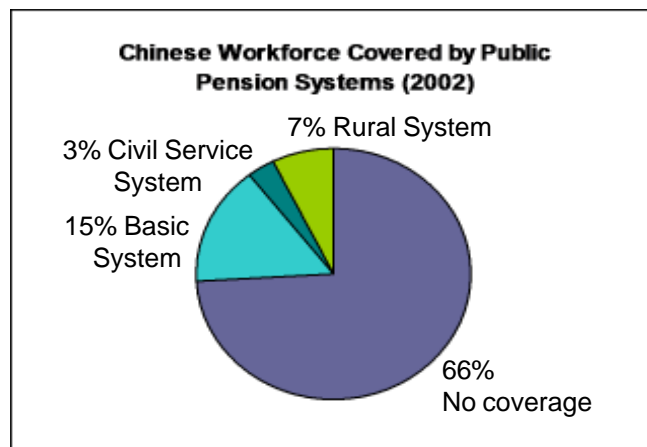
In light of such pressures, the logical solution is for the elderly to fund their own retirement through some sort of pension system. However, as a recent issue of the *Economist* states, "The [Chinese] pension system is a mess, and the government only has a few years to sort it out before a fast ageing population turns the problem into a full-blown crisis."<sup>2</sup> The dimensions of this current "mess" are straight-forward. The past pay-as-you-go system only

covered a fraction of the workforce and initial attempts at reform have fallen short of their goals.

The original pension system, established through the old state-owned enterprises (SOEs), was a pay-as-you-go system whereby current workers are taxed to fund the retirements of previous workers. The legacy continues in today's system in which the majority of workers covered are employees of state- and collectively owned enterprises or civil servants. In 2002, two-thirds of the Chinese workforce were not included in any kind of pension system. Most of those that went uncovered were farmers, migrant workers, and rural small-time manufacturing workers. Even within the cities, however, only 55% of workers are covered by public pension systems. As of 2002, only six percent of workers in the private sector were covered.

In 1997 the State Council initiated reforms for the national pension system and for the first time extended basic coverage to private-sector workers. The old pension system, based purely on a pay-as-you-go cycle, was replaced by a two-tiered system involving both scaled-back pay-as-you-go benefits as well as personal retirement accounts. The contribution rate remains at 24 percent, but 11 percent is credited to a personal account.

Due to the continuing burden of funding the old system, contribution rates to U.S. Social Security. This prohibitive



The majority of Chinese people are still uncovered by any pension system. (Source: Jackson and Howe, 2004.)

<sup>2</sup>"Time Bomb," *The Economist*, May 22-28, 2004, pp. 37.

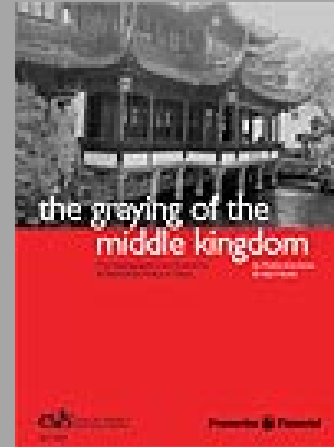
cost together with widespread mismanagement has contributed to resistance from private firms. Moreover, contributions to both tiers of the pension system are deposited in the same government bank accounts, allowing local governments to “borrow” personal account contributions to balance the bottom line of the social pools. Essentially, workers joining the new system today are being asked to pay off the liabilities of the old system while having no assurances that it will still be functional when they reach retirement.

As the CSIS report, *Aging in the Middle Kingdom*, summarizes, “The pension system is burdened by excessive contribution rates. It promises workers funded savings but gives them empty accounts. Meanwhile, despite the heavy cost burden, it leaves three-quarters of the workforce without any coverage at all.”<sup>3</sup>

#### Looking forward...

Many questions remain regarding China's ability to create a system that will care for the growing number of elderly without overburdening tomorrow's youth. It remains abundantly clear that successfully navigating the aging revolution will be as critical as any issue in China's economic, political, and social development.

<sup>3</sup> Jackson, Richard and Neil Howe. *The Graying of the Middle Kingdom*. CSIS and The Prudential Foundation, 2004, pp. 23.



CSIS Report  
*The Graying of the Middle Kingdom*  
available online at:

<http://csis.org/gai/index.htm>

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