The Impact Of China's One-Child Policy On The Elderly Care & Retirement Planning

History and Background

The one-child policy(OCP) in China was introduced by Deng Xiaoping in 1979 to curb China's rapid population growth. In particular, each family could have only one child, as long as both parents were Han Chinese (not applicable to ethnic minorities). In 1988, the government relaxed the OCP to the extent where a family can have its second child if its first child was a female, as the OCP worsened the gender imbalance situation carried in traditional Chinese culture. In 2013 the Chinese government allowed couples to have the second child if both of the couples were the single children; however, not many families applied for the second child upon this relaxation. In 2015, the government completely abandoned the OCP, to counter the severe aging problem in China.

Contributing to The Aging Problem

By making the aging problem worse, the OCP makes China's eldercare and Chinese individual retirement planning challenging issues. During the 36 years of China's OCP, the life expectancy has grown from 67 to 75, and the fertility rate has dropped from 2.8 to 1.7(China Power, 2016). As a result, China's demographic picture is starting to resemble that of Japan, with new births in decline, shrinking working force and an aging population. In particular, from 2016 to 2017, new birth fell from 17.86M to 17.23M; the working force shrank by 5%; the percentage of the elderly population (65 and above) rose from 10.8% to 11.4% (Leng, 2018).

The aging problem is a major challenge to China's eldercare and pension system. Firstly, China has been paying retirees by contributions paid by the working population. However, China did not set up its current pension system until the early 1990s (Ministry of Human Resources and Social Security of PRC, 2008). The gap between the contributions coming in and payments going out gets widening as more people retire and fewer people join in the workforce. This shortfall was estimated to be 429.1B yuan (69.2B USD) in 2016 (Ministry of Finance of PRC, 2016). Wang et al., (2013) also estimated that the shortfall would reach 890B yuan (143.5B USD) in 2020. Chinese Academy of Social Science (2015), one of the government's top think tank, projected that half of China's provincial pension fund is in deficit, as the heavier burden shifting to the new generation to support the elderly, the academy forecasted that there will be an intergenerational economic conflict --- a confrontation between the working young people and retirees.

Secondly, China's economic growth has been closely tied to its population dividend and fiscal stimulus. As China's aging problem gets worse than it used to be, China's economy will get hurt. Particularly, due to the aging problem, China's labor pool dwindles, which would lead to a higher level of wages in the manufacturing sector and ultimately, decreased the profitability of companies in the sector. As a result, the government's tax income would decrease, and this will limit the Chinese government's ability in providing fiscal stimulus and supporting the pension system. Moreover, compared to other countries facing the aging problem, such as Japan, Italy, and Germany, China is in the earlier stage of development(China Power, 2016) where China lacks the social welfare capacity that has assisted developed countries during their demographic transition.

Policy Challenges Due to The OCP

China's government has recognized the problem and the consequence of the OCP. However, as China is a more developed and educated country as a whole, young couples are reluctant to have more children now. Yi Fuxian, a demographer at the University of Wisconsin-Madison, concluded that "Beijing's two-child policy has failed." Zhou Tianyong, a researcher at Central Party School in Beijing, recommends strong measures to address the aging issue, to avoid economic damage stemming from the shrunk labor force, consumer demand and GDP output. However, the consequence of the 36-year long OCP has far more profound impacts on its countermeasures. A typical result of the OCP is the prevalent "4-2-1" family structure in China(4 grandparents; 2 parents neither of whom has siblings and 1 child)(Feng et al., 2012). Under such a structure, a young couple has to provide and support both of the elderly and their children. In research on Chinese demography, Zhang et al. (2006) found that most Chinese people recognize the fact that young couples are not financially capable of supporting the "4-2-1" family. Consequently, young couples are less likely to have one or multiple children, because children can significantly increase a family's financial burden. Another long-term consequence of the OCP is that to pursue better incomes to support their family, young people from rural areas of China migrate to the richer and more developed urban areas. Without the presence and assistance of the young people, the provision of the eldercare in rural areas becomes even more challenging in China. Although rural areas have more elderly residents regarding the percentage due to the pronounced out-migration, many urban eldercare options such as insurance, nursing home, and community committee are largely unavailable in rural areas(Zhang et al., 2006). A long-term goal of the government policy should also focus on reducing the economic gap between urban and rural areas, to mitigate this consequence of the OCP.

Current Retirement Planning/Pension System And The Future

Currently, China's pension system approximately requires individuals to pay 40% of their income to pension funds mandatorily, which is ranked #5 in the world regarding the percentage (Li and Ma, 2013). However, the replacement rate of China's pension system is only 40% (Li and Ma, 2013). Empirically speaking, a replacement rate of 70% is needed to maintain retirees' quality of life if pension payments are the retirees' sole income source after the retirement. One of the reasons that the current pension system provides subpar returns to retirees is due to the poor management of the pension fund. Firstly, the vast majority of China's pension fund is invested in the form of CDs and treasury bonds, on average, the overall return is about 2% annually, which can not even keep up with the inflation rate(Li and Ma, 2013). Secondly, empirical research has shown that even in developed countries, such as U.K. and Italy, corruption problem of pension management can be hard to tackle with when it comes to the defined contribution part of pensions (Williamson et al., 2006). However, China lacks a regulatory agenda in the anti-corruption oversight field. Thirdly, the personnel manages the pension fund are government officers, who were not professionally trained for managing such an enormous amount of money, leading to dubious oversight and subpar return. As a conclusion, Chinese people and government should seek for (partial or full) privatization of the current pension system. In particular, the government should shift from the direct “supplier and provider” to a “regulator and purchaser” of eldercare. On the bright side, Chinese people have already realized the fact that they cannot solely count on their pension plan, and they are saving for their retirement (Zhang et al., 2006). Nonetheless, during the most recent decade, Chinese families have been consistently racking up debts, and reducing their net saving rate from 39% in 2010 to 24% in 2016(World Bank,2018). It largely remains uncertain whether Chinese people can rely on their cash savings for their retirements in the future. As a result, China will be a big market for retirement planning and pension fund management, as both the people and the government will seek for the participation of the private sector in retirement planning services.