

Labor force

No need to panic

by Judith Banister

China's population is aging. After more than three decades of forceful family-planning policies, including the one-child policy, the share of children and young adults in China's population is shrinking. At the same time, the population growth rate has slowed and people are living to much older ages. Conventional wisdom holds that this dramatic demographic shift bodes ill for China's economy: a growing labor shortage will damage competitiveness, while the graying hordes of unproductive retirees will overburden a depleted workforce. But that prognosis is too grim. In reality, China has myriad options for managing its shifting age structure—not least by raising workers' participation rates and making productive use of surplus labor.

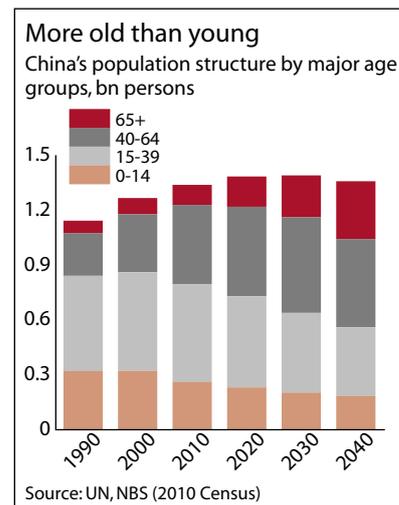
In recent decades, China experienced a “demographic window of opportunity,” as the number of people of working age grew rapidly both in size and as a share of the total population. China's censuses showed that the absolute number of people aged 15-64 grew from 620m in 1982 to 999m in 2010, while their share of the population jumped from 62% to 75%. This trend was caused first by declining mortality, which unleashed rapid population growth; and then by declining and low fertility, which reduced the share of children in the population and, concomitantly, raised the share of adults.

Today China has over 1 bn adults aged between 15 and 64, a mass of brain and muscle constituting one-seventh of the entire global population. This fact should be recalled when manufacturers moan about labor shortages. Yet it is also true that China's demographic dividend is now coming to an end. The population aged 15-64 will peak by 2015 and then decline as a share of the population. It is vital, however, not to exaggerate the impact of this demographic turning point: the size of the potential labor force will only decline very gradually. The United Nations projects that China will still have 960m adults aged 15-64 in 2030. This means there should be no absolute shortage of potential workers for the coming two decades and beyond.

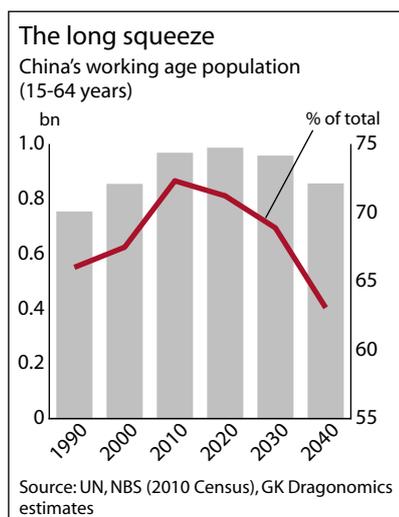
Chairman, we shrunk the kids

China's population is set to undergo two major structural shifts. Almost uniquely among developing countries, China's population has an unusually small percentage of children. After four decades of mandatory family-planning policies and more than three decades of the one-child policy, the number of children under age 15 is shrinking rapidly. In 2000, China was home to an estimated 323m children. By 2040, this will fall to a projected 185m. Meanwhile, the absolute size of the elderly population,

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China faces no absolute shortage of potential workers for at least the next 20 years



defined as those aged 65 and over, is set to explode from 110m in 2010 to nearly 320m by 2040. As the population ages, the age structure of the workforce will also change. Today more people are aged 15-39 than aged 40-64. After 2020, however, more workers will fall into the older half of the labor force age range.

Yet China will not be crippled by its shrinking young adult workforce any more than developed countries have been crippled by their own aging populations. Many other countries, not all of them rich, have already experienced a similar demographic transition. The list of supposed ailments include low mortality and fertility levels, shrinking numbers of children and young adults, population and labor force aging, and very slow (or even declining) population growth. Some countries have dealt with these changes better than others—yet China is hardly unique in confronting these demographic trends.

Moreover, it is too easy to ignore the many benefits that demographic changes have brought and will continue to bring. The impressive decline in mortality means that average life expectancy in China is now about 75 years. Children and working age adults live longer and healthier lives than ever before. And the myriad availability of birth-control techniques coupled with low fertility expectations mean that women benefit from broad occupational options when joining the workforce—a fundamental shift with enormously positive economic and social implications. Lower birth rates, which would have occurred regardless of China's coercive family-planning policies, also mean there are more resources available to educate children. The young adults entering China's workforce are much more productive than earlier generations of workers.

Demographics: not the be all and end all

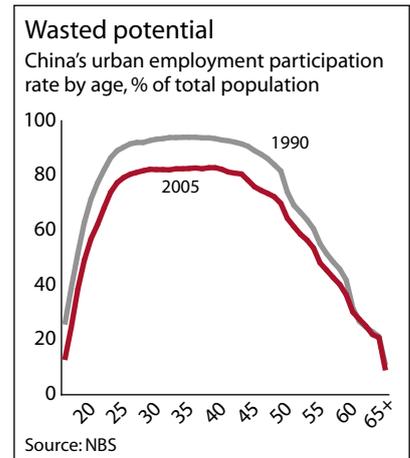
Indeed, other countries may have what some analysts see as much more favorable demographics—India is the obvious example—but China has done a much better job of ensuring that its workers have basic skills. Only 4% of the adult population is illiterate, and most adults have at least attended school up to the age of 15. High-school and college participation rates are rising: of China's employed workers, an impressive 10% have attained some level of post-secondary education. By 2010, about 25% of 18-22 year-olds—over 22m students—were enrolled in colleges and universities. Rising educational attainment will help to raise productivity further, and therefore boost economic growth even as the size of the workforce shrinks.

This is an important point, because most of the driving forces of China's remarkable economic ascent over the past 30 years were not demographic. Other factors such as liberalizing economic reforms, growing trade and the adoption of technology were just as important. In future decades, even as the population structure becomes less favorable to economic growth, China can continue to utilize its many competitive advantages to support its economy. Demographics are an important element in the economic mix—but they are not necessarily the defining factor.

Demographics are an important element in China's economic mix—but not the defining one

That said, a tighter labor market will hit industrial competitiveness, especially in low-margin manufacturing. In the 1980s and for most of the 1990s, labor costs were held down by the glut of workers moving out of subsistence agriculture into higher-paying non-agricultural work. Many employers seemed to believe there was an endless supply of eager workers willing to work long hours for low pay and few benefits. That situation changed over the past decade as a new generation of better-educated workers began to demand fairer treatment and higher wages. But it was underpinned by the shifting age structure of the workforce, as the share of young workers began to decline as a percentage of the total.

Industrial employers in the Pearl River Delta first began to report labor shortages in 2003. Since then, such reported shortages have spread across a broad swath of coastal provinces, forcing employers to raise wages and improve working conditions to find workers. In 2003-10, real wages in urban economic units more than doubled, even as their number of employees rose from 110m to 131m. Many manufacturers have traditionally employed only young, unmarried and preferably passive workers. Yet, after more than 20 years of low fertility, these workers are now much tougher to find. If employers continue to demand workers in a narrow age range with very specific characteristics, then they will continue to complain of a shortage. But that does not mean that there is an absolute shortage of workers.



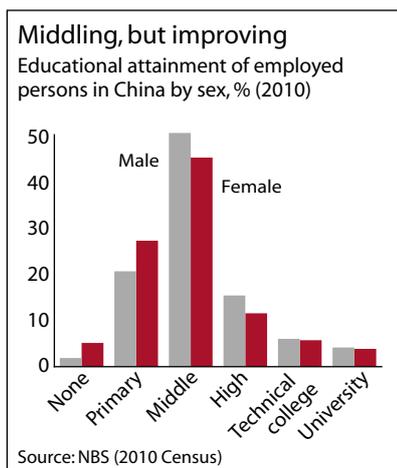
C'est la vie

When France raised its legal retirement age from 60 to 62 in 2010, millions of people took to the streets. As the most vociferous protestors burned cars, smashed storefronts and blocked deliveries to gas stations, France's northern neighbors raised a quizzical collective eyebrow. After all, both the UK and Germany had already decided to raise their retirement ages from 65 to 67, following the lead of Norway and Denmark. In a country with an average life expectancy in excess of 80, allowing citizens to enjoy more than 20 years of retirement appeared a recipe for national bankruptcy. To outside commentators, the French people's determination to retain their country's generous social model looked like an act of madness.

Yet France is not alone in maintaining an uneconomically low retirement age. China's urban citizens enjoy some of the lowest retirement ages worldwide. Men can retire and receive a pension at 60, while most women retire at just 50. Most urban workers are required to retire when they reach the official retirement age, even if they would rather continue to work. Even by French standards, China's statutory retirement laws are generous: life expectancy in many large cities approaches or has surpassed 80. China could easily raise participation in the labor force by raising legal retirement ages that were set in the 1950s when life expectancies were much shorter than they are today.

How would raising the legal retirement ages work? A law could be passed and publicized now for implementation in the future. This strategy, modeled on similar policies around the world, would refrain from jolting the plans of those approaching imminent retirement. It would also avoid worsening any current shortages of jobs in China's cities. Such a new law would only apply to those retiring in five or 10 years' time, and could be designed to raise legal retirement ages for women faster than for men. In time, the legal retirement ages for men and women would converge.

Higher retirement ages are vital to ease financial pressure on the pension funding systems. They would keep huge numbers of workers contributing into the systems for longer, and reduce the number of pension payout years across the board. Later retirement could also ameliorate feared urban labor shortages as the shrinking cohorts of new workers born under the one-child policy enter urban labor markets. China's top labor officials have been floating the possibility of raising legal retirement ages since early 2011, but so far no action has been taken. Until recently, the priority was to free up jobs for young workers. But as the labor market tightens, it will make far more economic sense to squeeze more productivity out of older workers.



China's demographic transition over the coming decades should not derail economic growth

More jobs wanted

In fact, China has a vast army of surplus and underemployed workers that it could potentially bring into the labor force. Huge productivity gains can be made from employing its enormous current and future workforce more efficiently than it has done in the past. Millions of farmers spend much of the year with little productive work to do, whiling away the time before the next planting season or harvest. With slightly more mechanization of agriculture, more workers could be freed from labor-intensive field work for non-agricultural jobs. China could also reform its household registration (*hukou*) system, which keeps many people on the farm, to encourage more labor migration to towns and cities.

Surplus labor is not only restricted to rural China. Millions of urbanites are employed in unproductive jobs, especially in the state-owned sector. Many low-level bureaucrats seem to spend their working days slurping tea, reading the newspaper, and taking leisurely afternoon naps in their offices. Reforms to boost further the role of the private sector alone would push up productivity levels nationwide. That is not to mention the many millions of urban dwellers who have no job. Overall urban employment participation rates fell by about 10 percentage points between 1990 and 2005. If jobs were available—admittedly a big if—there is no reason why participation rates should not rise.

China has a good base from which to build. At the end of 2010, 57% of the total population were in some form of employment. Female employment rates are much higher in China than in many countries, including developed countries such as Japan. The prime reason is the legacy of Communist ideology, which encouraged both work outside the home and male-female equality. China's high employment participation rate means that it should weather the aging of its population better than economies in which women are expected to stay at home and look after the children. At the same time, China's strong tradition of family support for the elderly could help hold down the costs of care for the aged as their numbers multiply.

Not all doom and gloom

China's demographic transition will present enormous economic and social challenges over the coming decades, but there is no reason why it should derail economic growth. Many other countries are already going through a similar process—albeit not at China's accelerated pace—and China will be able to learn from their solutions. Admittedly, China will have to face many of these challenges at a lower level of development than most other aging societies. But that also means that some of the associated costs will be lower, and that it will be easier to raise productivity levels to help pay for them. Above all, China still has enormous potential to raise participation rates among the working-age population. It is too early to talk about a demographic disaster lurking over the horizon.