



China's new rural pension scheme: can it be improved?

China's new
rural pension
scheme

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Abstract

Purpose – This paper aims to describe China's need for old-age pension coverage in its rural areas, to highlight the strengths and weaknesses of the new rural pension system currently being implemented, and to suggest some needed reforms.

Design/methodology/approach – This paper's analysis is based largely on evidence from Chinese government documents, newspaper reports, and research reports including those discussing related programs in rural areas of other developing countries. This evidence is supplemented with a small number of interviews with government officials, Chinese academics, and farmers living in rural China.

Findings – China has recently started a major effort to bring old-age pension coverage to rural China. While it is too early to know how successful this effort will be, there are some structural issues that should be addressed. The paper's major conclusion is that the current funded accounts component needs to be supplemented with a modest social pension scheme.

Originality/value – To date next to nothing has been published for an academic audience about this major new and first ever countrywide old-age pension program for rural China. If successful, this program has the potential to stimulate efforts in many other developing nations around the world to provide pension coverage in rural areas. The paper analyzes the program, uncovers some serious limitations, and proposes changes to deal with those limitations.

Keywords Rural areas, China, Social policy, Elderly people, Pensions

Paper type Research paper

1. Introduction

China's population is aging rapidly. In 2007, approximately 11 percent of China's population was age 60 or over making up 21 percent of the world's elderly population (United Nations, 2007). In 2002, a report from the Asian Development Bank (Leisering *et al.*, 2002) described the People's Republic of China (hereafter China) as a country with a distinct rural and urban divide that is established both politically and legally.

The huge gap in living standards, educational systems, public infrastructure, health services, and old-age security has made China, in effect, "two different nations". In the early 1950s, the government laid the foundation of China's social security – a comprehensive public social security system which coupled with the state-owned enterprises provided urban workers with generous benefits while the rural population had to rely on land and family as the source of old-age security (Shi, 2006). Currently, out of the population of 150 million elderly (over age 60) in China, about 100 million live in rural areas (China News, 2009). Until recently, rural old-age social security has received little attention from the government.

In the past three decades, China's GDP has increased ten-fold, growing at an average annual rate of 9.9 percent and per capita income has grown at an average annual rate of over 8 percent (*China Daily*, 2008). This growth has greatly reduced the extent of extreme poverty and many Chinese people have gained from China's rapid transformation towards an industrialized society. However, the gains from this prosperity have been unevenly distributed. China's "rural nation" of the peasantry



gained initially from the reforms of the late 1970s and 1980s, but since then the gap between the rural and urban population, with respect to economic and social development, has increased substantially (Dummer and Cook, 2007; Pei, 2007). China's relative lack of social security coverage for rural elders exacerbates the already severe rural-urban economic disparity and slows the rate of rural poverty reduction. The continuing economic disparity between rural and urban areas has led Chinese policy makers to recognize the need for a social security system for rural residents.

In 2009 China began to implement a new rural social pension program (China News, 2009) that will be the focus of our analysis. It is the most ambitious rural pension system in China's history and could, if successful, serve as a model for rural populations throughout the developing world. We discuss both the pros and cons of the pension plan. We also propose some modifications in this new scheme based on evidence drawn from rural pension policies currently in place in other developing nations, modifications which may substantially increase the efficacy of the current rural pension reform effort in China.

Our analysis draws on evidence from many sources including government documents, Chinese newspapers, reports on related programs in other developing countries, informal interviews with several government officials, Chinese pension policy experts, and farmers in rural northeastern China.

2. Why China needs a rural pension scheme

2.1 Erosion of traditional sources of old-age security

For thousands of years, land resources and one's family have provided social security for the elderly in rural China. This traditional security system has been carried over by the Chinese government since the founding of the People's Republic of China. Chinese traditional values emphasize the obligation of adult children (particularly sons) to support their parents in old age. During Mao's time, under rural people's communes, land and other means of production were collectively owned. Rural laborers used to work together, communally producing and distributing goods. When someone was no longer able to work, he or she would withdraw from productive activities and be taken care of by family members – a social contract stretching back thousands of years. Through collective support, childless and disabled old persons were guaranteed food, clothing, housing, medical care, and burial expenses by the collectives – Five Guarantees – the well-known social assistance program in China (Wang, 2006; Li, 2007). However, the dramatic social and economic changes in recent years have weakened the traditional system. The economic reforms associated with the introduction of the household responsibility contract system in 1978 dismantled the institutional basis for the collective-based social security system in rural areas, including the Five Guarantees program (Li, 2007).

The decline in fertility rates starting in the late 1970s due to the one-child policy and the subsequent graying of the Chinese age structure is further undercutting the traditional rural system of old-age security. Yet another important factor has been the rapid rate of economic development and the many structural and cultural changes associated with that development.

Due to these changes and related changes in family structures, such as those linked to the migration of many young adults to urban areas, the ability of the family to support its older members is being undercut (Zhang and Tang, 2008). Due to the industrialization and urbanization process, the number of rural migrant workers has increased substantially, from around 2 million in 1983 to 132 million in 2006 (OECD, 2009). The out migration of primarily young workers has accelerated the graying of the age structure in rural China.

Today 56 percent of China's total population, but 70 percent of its elderly live in rural areas. Although remittances from these migrants do help alleviate rural poverty, for many old parents this support does not keep them out of poverty. Due to the massive scale of rural to urban migration in China, insufficient family support for the rural elderly has made the government's lack of pension support in most rural areas particularly problematic.

China's continued urbanization has also accelerated the decline in cultivated land available for agriculture in rural areas. With population increases and urbanization, in many regions farmland can no longer be the major income source or an adequate safety net for farmers due to the small size of family plots and unstable ownership of farmland. In short, the dramatic social and economic changes over the past few decades including the falling family size, massive rural-urban migration, fast shrinking of cultivated land, and diminishing "filial piety" have eroded the traditional old-age support system in rural China (Zhang and Tang, 2008).

The public media and the government for the first time state that land and families can no longer provide sufficient old-age social security in rural China (China News, 2009). This makes the introduction of a rural old-age pension system with general coverage a priority for China's modernization.

2.2 Poverty reduction and bridging the urban-rural gap

China has successfully lifted over 200 million people out of poverty during the last 30 years (Weng and Wang, 2008). However, since the 1990s, poverty reduction has slowed down as both the regional income gaps and rural-urban economic disparity are widening (Wang, 2006). The co-existence of a relatively developed urban social security system and a relative lack of rural social security protection is a major obstacle to harmonious social development in China. The establishment of an old-age social security system throughout rural China will be crucial to bridging the urban-rural divide and promoting balanced social development. Studies of social pensions in low- and middle-income countries show that the introduction of pension benefits reduces the poverty of both older people and others in their households (Williamson *et al.*, 2009).

2.3 China's basic program for rural social security insurance

Influenced by the worldwide spread of neo-liberal ideology in connection with social security policy reforms during the 1990s, the Chinese Ministry of Civil Affairs promulgated the Basic Program for Rural Social Security Insurance at the county level in some well-off rural areas (Li, 2007). According to the regulation, rural residents should start to contribute to the social insurance schemes at the age 20 and would receive pension at the age 60. There is no state subsidies involved. As a result, many rural pension insurance schemes have collapsed or exist in name only (Li, 2007). An official said "the system virtually failed, as it required payment solely from farmers, who eventually gave up because of a lack of money." In 2007, 5.3 million rural elderly people were qualified for the Five Guarantees program and received benefits. Together with 3.9 million pensioners from the old rural insurance scheme, about 9.2 million rural elderly people receive regular pensions nationwide. However, given a population of 100 million elders living in rural areas, the pension coverage for rural elders is under 10 percent (Ministry of Labour and Social Security of China, 2007; National Bureau of Statistics of China, 2007).

2.4 Sustainable economic development and social stability

A report by the Asian Development Bank points out that pensions have a wider significance beyond contributing to a living for the elderly. Social security can help unite

the country and contribute to the social cohesion (Leisering *et al.*, 2002). This report also summarizes the lessons from developed countries concerning the relationship between social policy on the one hand and economic and agricultural policy on the other. Governments pursue social security not only for social justice, but also for economic reasons as pension programs can stimulate development in rural areas. In recent years the Chinese government and media have emphasized the importance of “building a harmonious society” and developing rural economy (Fan, 2006). Marked inequality between the rural and urban economy and the resulting polarization of interests between these two sectors tend to undercut social harmony and political stability. The existence of at least a modest rural social security system can help to integrate the country and to bridge the division between the “two nations” – urban and rural. Such a scheme can also contribute to sustainable economic and social development (Leisering *et al.*, 2002).

3. China’s new rural social pension scheme and its significance

Based on a number of pilot studies in select rural areas, in 2009 China introduced a nationwide, experimental rural social pension plan. Government officials have indicated that they expect the scheme to cover 10 percent of rural regions by the end of 2009, about 50 percent by 2012, and 100 percent by 2020 (China News, 2009). A major feature of this scheme is that, for the first time in China’s long history, the government will make direct contributions to a rural pension scheme. This government involvement will have major implications not only for millions of old people living in rural areas, but also for economic and social development in rural China more generally.

This new pension will have two components, a basic pension component financed by local and central government and a personal account component based on contributions from enrolled individuals. In relatively poor regions the central government will pay approximately 80 percent of the cost of the basic pension component and the local government will bear the rest. The contribution from local government will be higher for more affluent regions and as high as 90 percent in some of the most affluent areas (China News, 2009).

As part of this new rural pension scheme the central government will contribute 55 Yuan per month (about US\$8) to the basic pension component – a figure that is very close to the poverty line in rural China. Depending on the level of economic development, which varies from region to region, local governments are encouraged to make additional contributions. The 55 Yuan a month per retiree is the minimum benefit. With 100 million rural residents aged 60 and above, the cost for the central government will be roughly 2 percent of annual government expenditures. It is a voluntary program and all rural residents aged 16 and above are being given strong incentives to participate. To qualify a resident must be at least 60 (for males) or 55 (for females) and have contributed for at least 15 years. The minimum annual contribution participating workers are required to make generally ranges between 4 and 8 percent of the county’s average personal income during the previous year (China News, 2009). The actual rate varies from region to region and from county to county, depending on the level of economic development. The new scheme also requires residents living in some more developed areas to make contributions of over 8 percent to their personal accounts. For example, rural residents living in the suburbs of Beijing are required to contribute 10 percent of the average personal income for the region during the previous year (Beijing Labor and Social Security Net, 2008).

Residents who contribute for more than 15 years will receive higher pension benefits. For those who are currently 60 years old, the required years of payment will

be shortened. Those who are already 65 years old can receive the benefit from the basic pension (US\$8 a month being the minimum) without having contributed anything to the program subject to the condition that all of their family members aged 16 and above participate in the pension plan (China News, 2009). This plan also encourages local governments of relatively developed areas to make additional contributions. For example, residents living in the suburb of Beijing will receive a basic pension benefit of 280 Yuan (equivalent to US\$41) a month per person in addition to a payment from his or her personal account (Beijing Labor and Social Security Net, 2008).

The four principles of the new pension scheme are (China News, 2009):

- (1) a guaranteed basic benefit,
- (2) wide coverage,
- (3) flexibility from region to region, and
- (4) sustainability.

The first principle of a guaranteed basic benefit emphasizes that the starting benefit level is low and the main funding source is provided by the central and local governments. This is the key to the program. The government commitment and the low benefits are expected to result in wide coverage. Taking into account the disparities from region to region, the new scheme allows local governments to adopt a flexible level of personal contribution and commitment. The Chinese media have already reported some positive effects attributed to the new pension scheme for the rural elderly in areas covered by the 2008 experimental version of the program. A research study carried out in 2008 by HelpAge International in partnership with Renmin University in Beijing reported that older people in rural areas who have become recipients of this new program have an improved sense of personal security and self-esteem since receiving the pension (Zhang and Tang, 2008). Focus group discussions with recipients of the new pension showed that it:

- helps to pay for necessities such as food, medicine, clothing, and water and electricity;
- increases economic stability and decreases dependency on others for financial support; and
- brings greater respect from other family members and reduces family tensions, because older people are able to contribute to household expenses.

Several farmers we interviewed expressed their hope for the new rural pension scheme, one saying, "I've been worrying about what I should do when I can't grow crops anymore. If I can have a guaranteed income every month I see hope of my life." Another said, "I was always jealous of urban elderly people who receive a pension after retirement. The day has now come that I can have a stable income every month." Other researcher's also report similar comments. For example, one farmer interviewed by Zhang and Tang said, "I was embarrassed to ask the children for money before. Now I feel much better because I have a regular income and buy anything I want." Another said, "We are very excited to get a regular income like urban residents. It was unimaginable before . . ." (Zhang and Tang, 2008, p. 17).

Due primarily to the one-child policy started in the 1970s, recent census data show that in rural China the gender ratio is way out of balance (BBC, 2007). Most analysts attribute this to the prevalence of son preference which is particularly strong among

farmers. This gender preference is linked to the traditional Chinese belief that it is the responsibility of a son to support his elderly parents. The introduction and eventual institutionalization of a rural pension scheme may, over time, reduce the strength of this gender preference and lead to a more balanced gender ratio.

If by 2020 the program does cover all rural areas in China, it will be a major accomplishment. No doubt, it would serve as a very influential model to other developing nations around the world, particularly those that currently lack pension coverage for their rural populations.

4. Possible problems with China's new rural pension scheme

4.1 Coverage level

The coverage of the new rural pension scheme will vary from region to region mainly depending on the level of economic development. For example, Beijing started an experimental variant of the new pension scheme in January 2008. By the end of 2008, it was reported that 1,065,000 (over 80 percent) of rural residents living in the suburb of Beijing city were participating in the new rural pension scheme (Yuan, 2008). This participation level is partly due to the relatively high living standards in Beijing's suburbs and partly due to the higher than usual financial contribution from the central and local government (280 Yuan a month per retiree). But most of rural China is much poorer than Beijing's suburbs. A Chinese researcher we interviewed said, "A big concern in applying the new pension scheme is lack of adequate revenue of many local governments." In addition, it is a voluntary program requiring contributions for rural residents of between 4 and 8 percent of the previous year's average income in the local area. Can rural workers afford to pay this much to participate in the program? China has about 80 million people living under the poverty line. A professor in the field of social security, whom we interviewed, said, "Many farmers in poor areas have no desire to participate and they do not expect to have the money needed to keep paying required premium for 15 years."

In rural China there are three times as many elderly poor as in urban areas (China News, 2009). We interviewed a county official who said, "So far many of the local villagers have not signed up for the program. It sounds like a great plan, but it takes time for farmers to accept it. The other reason is that many villagers can't afford it." Due to the substantial regional differences in economic development level and income, many poor families in poor regions will not be able to afford to pay the necessary contributions. This will keep the pension scheme from reaching the poorest of the poor. The success of the new scheme will, to a great extent, depend on widespread coverage and a high participation rate. These, in turn, will depend on the trust of rural residents in the government and the level of the government's financial contribution to the scheme.

4.2 Implementation and administration of the new pension scheme

In urban areas the implementation of social security is relatively straight forward because the payment of the pension premium by employees and employers is legally guaranteed. The rural pension scheme, in contrast, is built on voluntary participation. Only when the farmers trust the government and believe that their contributions will bring back more benefits will they decide to participate. It is thus crucially important for the government to meet its promises with respect to benefits while managing the accounts with sufficient transparency for pensioners to maintain confidence in the plan.

Effective financial management is also crucial to the success of any pension system. Chinese government officials (*Yangcheng Evening Paper*, 2009) emphasize that pension funding for the new rural scheme must be set aside solely for the purpose of paying

benefits and that the individual accounts must not be notional. Managing the pension fund for such a huge rural population will inevitably be a challenging task. The administrative cost and the risk of mismanagement will be quite high and hard to control. Considering the evidence that untold sums of urban pension funds have been spent on unrelated purposes (Frazier, 2004) and frequent misuse of funds contributed to prior small-scale rural pension schemes in the past and the widespread corruption at various levels of government in China more generally (Pei, 2007), it is reasonable to assume that there is a high risk that many of these rural county pension funds will be mismanaged.

According to published reports, county government will be responsible for setting up the personal accounts, managing the local pension fund, and distributing the benefits for retirees within the county (China News, 2009). As in all developing countries, compared with urban governments and administrative offices, the efficiency and effectiveness of the lower level government bureaucracies in rural areas of China are weak. For this reason successful implementation of the new rural pension scheme is not going to be easy.

4.3 Low benefit level

China's new rural pension scheme is providing very low pension benefits to most recipients. Most will receive about 55 yuan (US\$8) a month from the basic component of the scheme, but the average monthly spending among old people in these rural areas is close to 200 yuan (US\$29) (Zhang and Tang, 2008). Although 55 yuan does help pay for some essential items, it is not enough to live on. Given its current level of economic development, a case can be made that China could afford to provide a higher minimum benefit to its rural old people.

4.4 Definition of beneficiaries

As mentioned above, the new pension scheme requires that workers contribute for at least 15 years to become eligible to receive the pension upon reaching retirement age (60 for men, 55 for women). However, those who are currently 65 or over are not required to make any contributions to become eligible for these pensions if their family members agree to participate in the pension scheme and pay their pension premiums (China News, 2009). That said, after reviewing the published regulations, we were unable to find a precise definition of "family members." In recent times the traditional family structure of three generations living in one house is becoming less common. The vague definition of the term "family member" invites corruption on the part of the local officials in charge of the program.

5. Does it make sense to add a second pillar to the new rural pension scheme?

China's ambitious rural pension scheme represents a positive step towards much improved old-age security for the rural elderly in the years ahead, even though the benefit level is currently quite low. Based on our analysis of the limitations of the new rural pension plan and our analysis of related policies in other countries, we propose that an additional universal non-contributory pillar be added to the new pension scheme for rural China. A combination of the pension scheme currently being implemented and our proposed universal non-contributory pillar would more effectively reduce old-age poverty in rural areas and do a better job of reducing the level of income inequality between rural and urban areas. Including a universal non-contributory pillar would also help promote social and political stability.

5.1 *Universal non-contributory social pensions in other countries*

Most low-income developing countries share the common characteristic of a largely rural economy based mainly on family agricultural production. In many of these countries, pension programs are financed predominantly on the basis of contributions from covered workers, most of whom are located in urban areas (McKinnon and Sigg, 2003). As a result, pension programs tend to cover at most a very small segment of the rural population. In developing countries, an estimated 342 million older people lack adequate income security. This number is projected to increase to 1.2 billion by 2050 unless coverage expands far beyond its current scope (United Nations, 2007). Most of the excluded elders are lifelong agricultural workers living in poor villages.

An increasing number of developing countries are adopting social pension schemes. There are two categories of old-age social pensions:

- (1) universal pensions, those paid to everyone over a specified age; and
- (2) means-tested pensions, those paid only to people above a specified age and with incomes under a specified level, often far below the official poverty line.

Many countries, such as India and Bangladesh, have introduced means-tested pensions for poor old people, but very often these programs fail to reach a large portion of those who in theory meet the eligibility criteria. In India only 45 percent of these pensions end up going to the poorest 20 percent of the old people and 55 percent end up going to those who are better-off (Willmore and Kidd, 2008). Local officials often distribute pensions as favors and many poor people must pay bribes or go through very long and difficult bureaucratic processes to get their pensions. Even in Chile, which has relatively strong regulatory infrastructure, the means-tested pension has not been very effective in reaching the poor, with only 60 percent of these pensions reaching those in the poorest quintile (Arenas de Mesa and Mesa-Lago, 2006). In short, many countries find it hard to assure that means testing limits the pension benefits to the poorest of the poor. Many who are poor are missed and many who are not among the poorest end up with social pension benefits.

On the other hand in many countries, universal pensions have been very successful in helping to alleviate poverty in old age. New Zealand, using its universal social pension, has been very successful in eliminating poverty in old age (Willmore and Kidd, 2008). Similar success can be found in developing countries too. In Mauritius, the poverty rate among households with an older person would be 30 percent were it not for the nation's universal social pension that reduces the poverty level to 6 percent (Willmore and Kidd, 2008).

Universal pensions provided by the government can increase productivity, particularly when some or all of the pension is used to improve the productivity of the family as a whole. In Zambia, the pension beneficiaries have invested 29 percent of the modest pensions they received in activities such as agriculture and animal rearing. As a result, seven times as many households own goats. In South Africa, pensions have increased access to credit and capital equipment (Lund, 2002). In Lesotho, about 18 percent of cash from the pension is spent on activities that create jobs (Croome and Nyanguru, 2007).

Pension systems can foster regime legitimacy and social solidarity. Means-tested pensions are much less likely to contribute to social cohesion as the distribution can be more easily manipulated to favor one group over another; in addition, it creates a disincentive to work and to save. In contrast, universal pensions tend to foster social cohesion which in turn contributes to a positive investment environment as well as

encouraging people to work. An International Monetary Fund paper (Subramanian and Roy, 2001) points out that 40 years ago Mauritius had a mono-crop economy, high poverty rates, and a great deal of racial tension, but today, it has a very low poverty rate. The authors report that the new pension scheme has played an important role in strengthening the social contract between government and citizens.

The biggest advantage of a universal non-contributory pension is that it ensures all elderly people will be covered. It does not require personal contributions or family member participation in the program. Because it is universal and age is the only requirement, the program will be more cost-effective to manage and will have a substantially lower administration cost. Another advantage is that it carries more incentive to save and invest than a comparable means-tested alternative. Therefore, in the long run, it will make greater contributions to economic growth and social cohesion. Universal pensions can play an important role as the foundation pillar of a pension system upon which other pension pillars can be built, whether they are mandatory or voluntary schemes (Willmore and Kidd, 2008).

5.2 The fiscal cost of a universal pension

Can China afford a universal non-contributory scheme for rural elders? Two key parameters need to be taken into account when determining the cost of a universal pension scheme:

- (1) age of eligibility (the age at which people become entitled to the pension) – the higher the age, the lower the overall cost of the scheme; and
- (2) size of benefit (the cash amount provided to beneficiaries) – the lower the benefit, the lower the overall cost of the scheme.

It would take us beyond the scope of this study to attempt to present a detailed analysis of the pension schemes in all of the nations that currently have social pension schemes in place. But we will briefly consider Nepal as an example. Nepal started its universal pension scheme in 1995. At that time, the qualifying age was set at 75 years old and the pension benefit was 10 percent of per capita GDP. The pension was 150 rupees (US\$2.12) per month in 1999 (Gorman, 2004). Recently, Nepal has reduced the age of eligibility from 75 to 70 and to 60 in one part of the country. Nepal has also increased the size of the benefit to 25 percent of GDP per capita. In addition, pensions will also be paid to all widows over the age of 60 (Willmore and Kidd, 2008). The World Bank reports that, in 2008, GDP per capita with purchasing power parity for China was US\$5,962, and for Nepal it was US\$1,112. If Nepal can offer a modest universal pension to its older citizens, it is reasonable to argue that China should do so as well.

We believe this additional universal non-contributory pillar would add a much needed supplement to the rural pension scheme currently being implemented. It would substantially improve the quality of life for millions of Chinese rural residents. The long-term benefits of a universal social pension would go far beyond old people themselves.

6. Conclusion

The provision of old-age security for the rural elderly in developing nations is a problem worldwide. It is an issue not only for the protection of this segment of the population, but also for sustainable social and economic development. China, as the most populous country in the world and with 56 percent of its population being rural, has the potential of exerting a major influence on rural pension policy in many other

developing countries. China's rural pension system has undergone major changes during the last six decades. Under Chairman Mao there was some collective-based eldercare in rural areas, such as the Five Guarantee scheme. With the economic reform and the transition from command economy to a largely market economy starting in the late 1970s, there has been a corresponding shift in the political ideology and associated values that most strongly inform social security policy. During the Mao era socialist ideology and values associated with that ideology were dominant. With the shift in the direction of a market economy, there was a shift toward social security policies based on neo-liberal ideology. During this neo-liberal period, the collective-based eldercare system was undercut with the collapse of the People's Communes. The Basic Program for Rural Social Security Insurance was influenced by this new ideology. The state did not provide pension subsidies for this program; rural pensions, to the extent that they existed at all, were entirely financed by farmers themselves. The approach ended in failure. The leading role of the family and household in providing eldercare has persisted. The initial success of the new rural pension scheme currently being implemented is mainly due to the introduction of government subsidies. One of the government officials we interviewed said, "The new scheme differs from the previous pension approach because it is not entirely based on funding from farmers themselves." The transition from pension policy based primarily on neo-liberal ideology to one based, at least in part, on a more social democratic ideology seems to be one reason for the grassroots support for the new rural pension system. However, in response to what we consider shortcomings of this pension scheme, we have proposed an additional pillar – a universal non-contributory social pension pillar. This universal social pension pillar would require more government commitment to providing basic protection for elderly farmers, but as in Nepal it could be phased in starting with a very modest benefit and a relatively high age of eligibility.

We note that the new Chinese rural pension scheme already includes a quasi-universal social pension for those over age 65. The basic pension component of that scheme does not require any contributions for this age group so long as their adult children (if they have any) participate in the program. Our proposal would assure that there would be coverage for the poorest of the elderly rural residents whose children are often so poor that they cannot afford to participate in the program, a precondition for their elderly parents being eligible for benefits in connection with the current scheme.

A few years ago, when the authors visited some government officials in China and discussed the potential utility of a universal non-contributory pension scheme for rural China most officials expressed reservations including the following arguments:

- China has never had a pension or any government financed social protection system that has covered a large fraction of those living in rural areas;
- China has a rural population of over 800 million. This huge rural population makes the case of China qualitatively different from the other countries that have introduced government-subsidized pensions in rural areas; and
- China has major regional disparities with respect to income and level of economic development making such schemes unfeasible.

Is it too early to establish a rural pension system in China? Probably not. Many European countries introduced pensions for farmers at similar or even lower levels of economic development than existing in present-day China (Leisering *et al.*, 2002). We believe that a combination of the new pension scheme currently being implemented

and our proposed universal social pension pillar would be effective in both reducing old-age poverty in rural areas and reducing the level of income inequality between rural and urban areas.

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