



China's Three-Child Policy: Passive Permission vs. Active Incentive

The ramifications of China's One-Child Policy from 1980 are still creating socioeconomic and political challenges today. These factors are driving China's new three-child policy in 2021, but the Chinese Communist Party will need to do more to incentivize citizens to have more children.

China's new three-child policy is an acknowledgment by the governing Communist Party that the shrinking population jeopardizes the country's economic future because it reduces the skilled labor force. On May 31, 2021, China's Communist Party Politburo, the nation's top decision-making body led by President Xi Jinping, officially announced that it would allow all married Chinese couples to have up to three children. The policy was formally passed into law by the National People's Congress, the national legislature of China, on August 20, 2021. However, it remains to be seen if the new policy will yield better results. The end of China's one-child policy and beginning of its two-child policy in 2015 has failed to raise the country's declining birthrates and prevent a looming demographic crisis that could turn out to be the Achilles heel of China's incredible economic transformation over the last 40 years, according to a *New York Times* article. "China's economic expansion has created a society where many young couples now struggle with economic pressures — including rising education and housing costs

— making it difficult to have even one child, let alone two," the article stated.

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The Chinese Communist Party first imposed a one-child policy in 1980 to mitigate the growth of the world's most populous nation, which was nearing 1 billion people, after failed party policies of the Cultural Revolution and Great Leap Forward led to 88% of China's population under poverty by 1981, as measured by the World Bank's Poverty and Equity Database. While the one-child policy did bolster economic development and social mobility (consolidating the combined wealth of two previous generations into the investment of one child), with the poverty rate reduced

to under 1% percent by 2016 World Bank data, the policy created a whole new set of challenges for the Politburo: Births in China have fallen for four consecutive years, including in 2020, when the 12 million babies born marked the lowest number since the Mao era in 1961. Births have also been below projections by China's National Health and Family Planning Commission.

According to the United Nations Population Division, China's total fertility rate — an estimate of the number of children born over a woman's lifetime — now stands at 1.3. This is officially considered "lowest-low fertility" and is well below the replacement rate of 2.1 — defined as replacement level fertility for each generation to exactly replace itself — raising the possibility of a shrinking population over time. Chinese women born during the years following the one-child policy are now reaching or have already passed their peak fertility age. As a result, there are not enough Chinese women to sustain the country's population level, despite new efforts by the government to encourage families to have three children.

"The Chinese government may be missing the point."

The decline in the birthrate, along with an increase in life expectancy, also means there will soon be too few in the labor force to support an enormous and aging population, according to a report issued in January 2020 by the Chinese Academy of Social Sciences. The academy estimated the contraction would begin in 2027, though experts believe it could be sooner or has already begun.

The declining population could create an even greater burden on Chinese society. With fewer workers in the future, the government could struggle to pay for a population that is growing older as well as living longer. A decline in the working-age population could also slow consumer spending and therefore have an impact on the economy in China and beyond.

Missing the Point

The Chinese government may be missing the point. While implementing a three-child policy is a step in the right direction to reversing a precipitous slowdown in birthrates

among Chinese women over the last three decades, one policy will do little to change the attitudes of women who refuse to have more than one child, if any. Dr. Yun Zhou, a social demographer and family sociologist specializing in Chinese family units, writes in *The Washington Post* that college-educated urban Chinese women have cited "high housing costs and long work hours" as key constraints against having more than one child. This is even among women who viewed having one child as the "natural next step after marriage." After a 40-year legacy of severe penalties for having more than one child, there is no guarantee that governmental support will translate into fertility behavior. The Chinese government needs to provide robust socioeconomic incentives that specifically relieve the financial demands of housing and day care — key costs that negatively influence the outlook on raising families in China. However, even if Beijing subsidizes housing and day care, the private-sector ramifications for women may be significant.

James Liang, economics professor at Peking University, has said that China will need to spend about 5% of its GDP, compared with "practically 0% now," in "cash, tax breaks, housing subsidies, and day care incentives" to increase the Chinese fertility rate to 1.6 children per women. Liang also proposes the government step in to build day care centers and kindergartens to allay fears of a high cost burden among prospective Chinese families. Even with a prospective government investment of \$736 billion, or 5% of China's GDP, 1.6 children per woman is well below the 2.1 replacement rate — a rate not seen since 1992, according to the World Bank.

The Chinese government has indicated that far more than a three-child allowance is in the works. In a readout from a 2021 Politburo meeting, President Xi stated that China would "lower educational costs, step up tax and housing support, and guarantee the legal interests of working women," but his committee gave no proposals on a course of action at the national level. However, there has already been action at the local government level to encourage an increase in fertility among women.

According to the *South China Morning Post*, in late July 2020, the city of Panzhihua in Sichuan committed to giving local women an extra month off and \$80 monthly stipends for second and third children until the age of

three. While an important move, government action at a higher level is necessary to address the broader systemic issues of housing and child care accessibility, particularly in larger cities.

Because the CCP has yet to lay out a plan for subsidizing child care and housing, the size and scope of the impacts of government involvement are difficult to understand. But it is not hard to see why the economic impacts will be very significant.

Data from the World Bank shows that while average annual wages for full-time employees in Shanghai have amounted to approximately ¥90,000 as of 2017, the average price for a new, centrally located residential property in Shanghai in 2020 was ¥118,510 per square meter. Properties outside of the center ring are still ¥26,740 per square meter. Ma Chunhua, a sociology professor at the Chinese Academy of Social Sciences, has discovered that low-income families (defined as having household income of less than ¥50,000) spend on average 70% of their earnings on their children, including child care. Understandably, the Chinese government must consider how much of its national income it wants to earmark and what the minimum amount is to increase the birthrate to replacement levels.

It is not hard to see that real estate and child care are big industries in China, and there has been concern of China crowding out large, private players in these industries. Nevertheless, the economic ramifications of government non-intervention to bring down child care and housing costs to boost the working population are even more drastic. According to scholar X Yu, by 2050 it is expected that there will be over 100 million Chinese retirees needing ¥800 billion in pensions — 20 times the 1993 amount. The Chinese government must decide whether it wants to commit to the upfront cost of subsidizing its future population growth or deal with the cost of a retired population that will account for more than 10% of national income.

Tackling the Economics of Education

In addition to lowering the cost of housing and child care, raising China's fertility rate will require addressing the thorny issue of the cost of education. Although most

children attend free public schools during the day, the vast majority of parents choose to send their children to private "cram schools" after their regular school day ends. Private schooling options exist but are strictly regulated by local governments and do not enroll many students. According to a 2021 survey conducted by the China Education Paper, 92% of parents enrolled their children in additional classes outside of school and roughly half spent \$1,500 a year or more on expenses. With each additional child, these costs grow. The entire K-12 education system in China is geared towards preparing students for the single future-defining exam that students take in their final year of high school, known as the gaokao. The exam controls entrance to university, and graduates from the top schools are all but guaranteed well-paying and secure careers. Without a reliable pension system to fall back on, parents are forced to rely on their children to support them in elderly years and view education as the key to ensuring their children are successful. Anxieties about the future fuel an educational arms race among parents, with exam preparation courses beginning as early as kindergarten. A hypercompetitive culture and educational system geared towards a single test puts parents under severe pressure to provide as many educational resources to their children as possible, both for the sake of their child as well as their own future financial stability. The competition is fiercest in big cities such as Beijing and Shanghai, where average incomes are higher and options for tutoring and exam preparation courses abound. In response to this incredible demand, the for-profit private education industry in China has grown to be worth over \$150 billion.

In July, the Chinese government announced measures aimed at curbing the industry as part of an effort to lower the cost (and stress) of having children. The move bans for-profit companies from teaching core subjects, bans foreign investment in the industry, and forces all existing educational companies to register as nonprofits. The announcement caused shares of educational companies in China to fall as much as 60%.

Anxieties around education are closely linked to rising housing prices in some areas as well. In 2019, for example, houses in the top school districts in Beijing cost nearly three times as much per square foot as the city-wide average price, prompting the government to take steps

to combat the soaring prices. In January 2019, Beijing implemented price controls on houses in certain districts. Many cities have also implemented rules that force schools to allocate seats to students outside of their school districts, so that owning a home near a school no longer ensures admission to that school. In Shanghai, some of the top schools allocate 50% of their seats to students outside their district.

Although these are significant steps in the right direction, they do not solve the underlying structural issues with the educational system that cause the frenzied pursuit of educational resources to begin with. With so much of a child's future riding on a single exam, it is only natural for parents to pour resources into ensuring their children's success. The demand for additional educational resources did not shrink after restrictions were placed on the for-profit education industry, and private tutoring may rise as an outlet for pent-up demand, further entrenching the advantages of wealthy families. Ironically, if China succeeds in raising the fertility rate, it could increase the competition for seats at the top universities and further exacerbate the problem of rising educational costs. Unless

there are more structural changes, the pressure — both emotional and financial — associated with raising a child will not be reduced and will therefore remain an obstacle for families considering having more children.

China's low fertility rate and aging population pose significant challenges for the future of China's economy — and the popularity of the ruling CCP. While the CCP has clearly identified the issue and begun to take measures to address it, the actions taken so far are not sufficient. Rory Green, senior China economist at macroeconomic forecasting firm TS Lombard, told CNBC that the new policy alone is "completely inadequate to reverse the demographic decline" without further structural changes. Adequate measures will have to impact other key areas of China's society and economy, primarily housing, child care, and education. Managing this growing issue will be among the CCP's biggest challenges in ensuring the continued success and growth of China, and their own popularity.

This article was written by Christian Anthony, Kevin Ke, and Matthew Griffith, members of the Lauder Class of 2023.



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