Dual Decentralisation and Fragmented Authoritarianism in Governance: Crowding out among Social Programmes in China

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Abstract  
In this paper, we use city-level datasets of social assistance programmes over 280 cities between year 2003 and 2011 to verify the existence of the crowding out between social assistance programmes and unemployment insurance in China. In other words, the expansion of social assistance programmes is associated with a reduction in the enrolment of unemployment insurance. With verifying the existence of the crowding out, this article argues that the crowding out is a result of an ineffective coordination across government departments. In the process of ‘dual decentralization,’ in which the central government has delegated welfare provision responsibility to local governments, the misalignment of incentive and institutions between central and local governments explains the ineffective coordination. Different from many studies in the literature, this paper presents an adverse consequence of China’s bureaucratic incentive system in social policy implementation. Also, while the conceptual framework ‘fragmented authoritarianism’ has highlighted the policy ineffectiveness in the economic policy area, this paper contributes to this literature by illustrating the policy ineffectiveness in the social policy areas

\textbf{Keywords:} China, social assistance, unemployment insurance, crowding out, dual decentralisation, fragmented authoritarianism
The quest for social harmony and expansion of social protection

Since 2003, under the policy of ‘building a harmonious society’, the Chinese government has begun to shift its expenditure emphasis towards social policy, and greater public funding has been appropriated for social assistance programmes. Total government expenditure on employment and social security (including social assistance programmes) rose from 1.9% of GDP in 2003 to 2.5% in 2013.\(^1\) Government expenditure on the major social assistance programme, the Minimum Livelihood Guarantee Scheme (*Dibao*), increased from RMB2.2 billion in 2000 to RMB72 billion in 2014, an average annual growth of 28%.\(^2\)

Interestingly, in the context of expanding social assistance programmes, there are two conundrums regarding social protection for urban workers. First, unemployment insurance cover remains very low compared to other social programmes in China. Although social insurance is compulsory for urban employees, including unemployment insurance and a basic pension scheme, many employees choose not to enrol in the unemployment insurance programme. In 2012 for example, about 60% of urban employees were not enrolled for unemployment insurance. In contrast, the number of urban employees with a basic pension scheme has increased much faster since 2000. In 2014, about 43% of urban employees had unemployment insurance while 65% had a basic pension scheme (Figure 1).

--- Figure 1 approximately here ---

Second, the number of registered urban unemployed is much smaller than the actual number of urban unemployed. The Chinese Academy of Social Sciences

\(^1\) China Statistical Yearbook, various years.
\(^2\) Statistical Communiqué for the development of social services in China, 2014.
estimated the actual urban unemployment rate for 2008 at 9.4%, whereas the registered unemployment rate was about 4.2%. A national level household survey recently estimated China’s average unemployment rate at 10.9% for 2002 to 2009, which is well above the registered unemployment rate (Feng et al., 2015). In other words, many workers do not register to claim unemployment insurance benefits when they are out of work.

This study argues that the crowding out effect between social assistance programmes and unemployment insurance, resulting from a failure of coordination among government departments, can explain the two conundrums. More specifically, the expansion of social assistance programmes is associated with a reduction in the enrolment of unemployment insurance and underreported unemployment rate.

This article adopts two conceptual frameworks to analyse the ‘crowding out’ phenomenon emerging in social programme delivery in mainland China. The first, dual decentralisation, refers to the coexistence of both vertical and horizontal decentralisation in the implementation of social policy and delivery of social welfare programmes in mainland China. Vertical decentralisation involves the delegation of discretion for policy implementation to local government, while horizontal decentralisation refers to a shift in selective responsibilities such as public services provision from the state to the private sector. (Painter and Mok, 2008) The second framework, fragmented authoritarianism, involves the fragmentation of decision-making authority such that interests and information become parochial (Lieberthal and Oksenberg, 1988). Both of these frameworks can enhance our understanding not only of the complexity of coordination between central and local government but also the coordination among different government departments.

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Applying the frameworks of dual decentralisation and fragmented authoritarianism, this article critically examines how lower level government implementation of social policies intended to protect China’s urban workers is affected by conflicts between the central and local economic, social and political needs. While the performance evaluation system for local officials is effective in promoting economic development, it may not be as effective in the social policy area.

We argue that the above two conundrums are unintended consequences of the expansion of social assistance programmes, which causes crowding out between unemployment insurance and social assistance programmes. Using city-level panel data from 2003 to 2011, this study suggests that this crowding out phenomenon is due to ineffective coordination among government departments caused by fragmented authority and information structures. We argue that the misalignment of incentives and institutions between central and local government is the key reason for ineffective coordination among government departments.

This paper contributes to the literature in the following ways. First, unlike the literature that highlights the value of bureaucratic incentives in promoting China’s economic growth (Li and Zhou, 2005; Xu, 2011), this paper presents adverse consequences of these bureaucratic incentives. While there is some research showing adverse consequences of the performance evaluation system on environmental policy (Zhou et al., 2013; Wu et al., 2013), this is the first study to systematically examine adverse consequences of the performance evaluation system related to social welfare delivery in China, with particular reference to the crowding out effect of social programme delivery. Second, this study uses longitudinal city-level data to empirically demonstrate the unintended consequences of the dual decentralisation process. Third, while the literature on fragmented authoritarianism is closely
associated with economic policy, this paper indicates that fragmentary authority and information structures may also render social policy ineffective.

**Social programmes for urban workers**

Social protection for urban workers is an extremely important issue, especially as the urban poverty rate in China has been increasing since the 1980s (Riskin and Gao, 2010). There are two major reasons for the increasing importance of social protection of urban workers.

First, since the late 1980s, following the restructuring of many state-owned enterprises (SOEs), many workers have been laid off and become impoverished, given that many are insufficiently skilled to work in the private sector. Indeed, it is the unemployed who are most likely to fall into poverty (Riskin and Gao, 2010). The estimated number of urban poor in China in 2003 was as high as 72 million (World Bank, 2009). Second, the urban social welfare system was dissolved following the SOE reform. Benefits from in-kind transfers (via work units) in urban China reduced from 21% of total household income in 1998 to 0.7% in 2002 (Gao, 2010). This implies that urban households experienced greater out-of-pocket costs for education, housing and healthcare, and some had difficulty meeting their basic needs after negative external shocks such as serious disease.

In the late 1990s, the central government initiated two clusters of social programmes for urban workers. The first involved social insurance, including unemployment insurance, basic pension and basic health insurance schemes, mainly for employees in the formal urban sector, who were required to register and contribute regularly. One of the most important social insurance schemes, unemployment insurance, saw 152 million enrolments and paid benefits to over two million people in
2012. Although it was initiated to provide basic benefits to workers laid off through the SOE reform, all urban workers have been required to enrol in unemployment insurance schemes managed by local governments since 1999. The duration of benefit payments can last up to 104 weeks. Unlike in many developed countries, China’s unemployment insurance benefits are not earnings related, but are set at a flat rate below the local minimum wage, in principle, according to central government guidelines.

Second, social assistance programmes were initiated in the late 1990s to support vulnerable groups such as retirees, ex-servicemen, informal sector workers, the disabled, etc. The most important of these is the Minimum Livelihood Guarantee Scheme called Dibao, a national means-tested programme initiated in 1999 as a safety net for the urban poor. This programme is managed by the Ministry of Civil Affairs (MCA) and its local subsidiaries, and provided cover for about 22 million people in 2012 (Figure 2).

--- Figure 2 approximately here ---

As with unemployment insurance, the majority of Dibao beneficiaries are urban workers. About 60% of Dibao beneficiaries in 2012 comprised the flexibly employed and both registered and unregistered unemployed (Figure 3).

--- Figure 3 approximately here ---

The Dibao programme is limited to households with local urban registration. The Dibao eligibility line is based on local minimum livelihood costs for the basic needs of food, clothing, housing and children’s compulsory education (PRC Government, 2004). The Dibao line is about 20% of the average disposable income per person in
urban areas. The central government guideline stipulates that Dibao benefits should be below those of unemployment insurance, the minimum wage and pension. Importantly, people claiming unemployment insurance are not eligible for Dibao benefits.

Other complementary in-kind social assistance programmes targeting the poor include medical, educational and housing assistance. For example, medical assistance programmes cover health insurance premiums. Importantly, these in-kind social assistance programmes are managed by different government bureaus; for example, education assistance is managed by the local education bureau, medical assistance by the local bureau of health and housing assistance by the local bureau of housing and urban-rural construction (Lin, 2013).

**Dual decentralisation and fragmented authoritarianism**

The complex dynamics between central and local governments is integral to the understanding of policymaking and implementation. In this context, the concepts of dual decentralisation and fragmented authoritarianism are relevant in explaining the ineffectiveness of policy interpretation during the expansion of China’s social programmes.

When the economic reforms started in the late 1970s, the Chinese government began to release its control over fiscal and administrative policy, devolving more autonomy to subnational authorities. This decentralisation comprised vertical and horizontal aspects (Painter and Mok, 2008), ‘dispersing power vertically within the state’ while also ‘dispersing power away from the state’, both of which weaken the role of central government (Painter and Mok, 2008: 139). It is also worth noting that the economic reform was accompanied by administrative reform in China, as the
central government expanded the decision-making power of lower authorities during the same period. Cai and Treisman (2006) argued that ‘during the 1980s the country became much more administratively decentralized’ (Cai and Treisman, 2006: 508). These ‘intertwined processes’ (Painter and Mok, 2008: 139) were believed to have protected local economies from interference by the central government and motivated local officials to promote economic growth, restructure state-owned enterprises in their territories and conduct local reform experiments (Cai and Treisman, 2006), thereby accounting for China’s ensuing remarkable economic success (Xu, 2011).

In contrast, another group of scholars have stressed the role of strong central control over local authorities through strict regulation as the driving force behind the successful economic reform under the leadership of the Chinese Communist Party. While acknowledging that the subnational governments enjoyed greater discretion, they cite firm control from Beijing as the main reason that China experienced such dramatic growth. Conceiving the Chinese state at one end of a continuum from *laissez faire* to central planning, the directionality of innovation and reform was top down: central government set the policy direction at the highest level, and through rigid control over official approval, the subnational actors competed with each other for promotion within the hierarchical party system by meeting the set criteria (Cai and Treisman, 2006; Landry, 2008).

However, the Chinese state, taking responsibility for overseeing economic and social development during the transitional economic period, continually vacillated between centralisation and decentralisation in addressing China’s vast geographical size and its complex and diverse local interests. It is therefore not surprising to observe ongoing ‘centralised decentralisation’ and ‘decentralised centralisation’ in the design and implementation of policies to secure state legitimacy and control over
economic and social activities deemed ‘strategically important’ (Hsueh, 2011; Mok and Wu, 2013; Lardy, 2014; Li, 2010). Meanwhile, the economic and social reforms not only dispersed power within the state but also introduced market forces to manage economic affairs and govern the social sector through the privatisation and marketisation of housing, health, education, social services and social welfare (Wong and Flynn; 2001, Mok and Ku, 2010; Mok, Ngok and Huang, 2013).

Analysing social welfare provision in China in the light of dual decentralisation, the central government delegated responsibility for welfare provision and social protection to local governments. Therefore, the policy and practice of decentralisation involved dispersing power both vertically within the state and horizontally away from the state. As the command economy essentially merged administrative and economic power under central state control, the transition process involved both dissolving this merger and downsizing the centre. The administrative and economic reforms were intertwined processes with dual decentralisation as the core element. Vertically, economic and administrative decentralisation empowered local governments to manage economic growth, social insurance and social service delivery. As Leung and Xu succinctly stated, the Chinese welfare model is based on ‘the strong role of the state in policy and legislative formulation and reform, provision of resource support, regulating, directing and monitoring policy implementation, and building the innovation and governance capacity of local government’ (2015: 13). Local governments, with their unique and distinctive local conditions, then actively adapted policies and measures for social welfare provision to meet the particular social and economic needs emerging in their different localities. Horizontally, developments such as the withdrawal of the state from the direct provision of public goods and social protection arrangements were in certain settings replaced by new public
management agendas, which were designed to mobilise private capital and local stakeholders in these sectors and use markets and user pay systems to deliver public goods and services (Mok and Ku, 2010; Leung and Xu, 2015).

The complex but conflicting interests in policy design and implementation at different levels of government, succinctly captured by the notion of fragmented authoritarianism (Lieberthal and Oksenberg, 1988), is important in accounting for the ineffectiveness of policymaking in China. According to the literature, policymaking and implementation, particularly with regard to economic policy, was not very effective, as decision-making was fragmented and disjointed across various government departments, each department having a strong incentive to maximise its own interests and marshal information accordingly (Lieberthal 1992). Against this background, coordination across government departments was often very poor.

To improve effectiveness in the context of this fragmentary distribution of authority between central and local governments, a performance evaluation system was designed to motivate local bureaucrats to meet quantitative targets set by the upper level government. By highlighting economic growth in particular as the key criterion for appointing and promoting officials, the evaluation system encouraged local leaders to make more effort to coordinate local bureaus for the promotion of economic growth (Li and Zhou, 2005).

To implement the expanding social programmes, local governments, with their knowledge and understanding of the needs of local residents, were best positioned to allocate resources to meet local social and welfare needs. Nevertheless, unlike the economic policies that promoted GDP growth, the decentralised approach to welfare development led to a misalignment of incentives between central and local government for three reasons.
First, GDP was a quantifiable target, whereas the outcome of welfare policies was harder to quantify and required greater information for central government to evaluate local government performance. Second, under the performance evaluation system, the outcomes of social policies were less significant and measurable than economic outcomes when evaluating officials (Gao, 2015). Local officials therefore lacked the incentive to strive for social policy implementation, and consequently coordination among departments for social policy implementation was less effective. Further, given the tight fiscal conditions in many subnational governments (Guess and Ma, 2015), a larger portion of local fiscal resources was allocated to promote economic growth, leaving a tight budget for social programmes. Thus, local bureaus had incentives to save administrative costs by fulfilling only the minimum requirements of social programmes imposed by higher authorities.

The crowding out effect on social welfare expansion

The dual decentralisation and fragmented authoritarianism led to coordination problems among government departments and different government levels in implementing social policies. This study argues that the crowding out effect between social assistance programmes and unemployment insurance, resulting from a failure of coordination, can explain the two conundrums described in the first section, namely the low enrolment rate in unemployment insurance and the disparity between registered and actual unemployment.

While it is compulsory for formal sector workers to enrol for unemployment insurance, informal sector workers may opt out. From the literature (Ghose 2005), the informal urban sector in China includes registered small-scale private enterprises and individual businesses while the formal urban sector is defined by registered
enterprises including state-owned enterprises, collectively owned enterprises, limited liability companies, shareholding corporations, foreign-owned companies and joint ventures.

The crowding out effect is associated with the self-selection of workers in the urban informal sector. For example, the majority of migrant workers do not enrol for unemployment insurance, and only 14% were enrolled in 2014 (Figure 1). With the benefits from social assistance programmes increasing, workers in the informal urban sector may prefer to claim social assistance benefits and opt out of unemployment insurance. Also, as claiming social assistance does not require being registered as unemployed, there was a lack of incentive to register when out of work. In other words, as social assistance and unemployment insurance were substitute programmes in the informal urban sector, social assistance programmes crowded out unemployment insurance. In contrast, there was no crowding out effect for the basic pension scheme, as there was no substitute pension programme for urban workers. Therefore, the result was relatively low unemployment insurance cover compared to the basic pension scheme, and underreporting of unemployment followed the crowding out effect.

The size of the informal urban sector in China is relatively large. In 2012, the total number of urban employees was about 380 million, over 50% (about 200 million) of whom were in the informal sector, with about 180 million in the formal urban sector. Given the large size of the informal sector, the government was short of capacity to enforce social insurance enrolment, allowing them to opt out in favour of programmes such as Dibao, depending on whether social assistance or unemployment insurance provided the higher benefit. The role of household registration status (i.e.

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4 China Statistical Yearbook, various years.
Hukou) was also significant in this context. Only workers in the informal sector with local Hukou were qualified to claim Dibao. In other words, crowding out between social assistance and unemployment insurance only applied to workers with local Hukou status.

There are two possible causal mechanisms for the crowding out between social assistance/Dibao and unemployment insurance. First, although the direct benefit from Dibao should be lower than that of unemployment insurance, the Dibao benefit increases with household size, so for a large family it may be higher. Once a household has qualified for Dibao, every family member receives a Dibao benefit. The other possible reason for a higher direct benefit of Dibao is that the beneficiaries are exempt from contributions, whereas unemployment insurance requires a contribution of 1% of a person’s pay.

However, the crowding out may not result from a higher direct benefit from Dibao. A second possible cause for crowding out may be the increasing aggregate benefit of Dibao. A household that qualifies for Dibao is eligible to claim additional benefits from complementary social assistance programmes, such as medical, educational and housing assistance, which are managed by different government bureaus (Lin, 2013; Qian, 2014). The aggregate benefit of Dibao therefore includes both the direct benefit and further indirect benefits from other complementary social assistance programmes. When the aggregate benefit of Dibao is higher than that of unemployment insurance, informal sector workers may opt out of unemployment insurance.

If the second mechanism is correct, the crowding out effect stems from ineffective coordination among the government bureaus managing different types of social assistance. The misalignment of incentives and institutions between central and
local government in policy design and implementation is critical to this ineffective coordination for two reasons. First, in the context of dual decentralisation, a local leader lacks incentives to coordinate with other government departments to implement social programmes. In particular, under the performance evaluation system, a local leader is more likely to coordinate the local bureaus to allocate fiscal resources for economic growth. Second, as the fragmented authoritarianism framework suggests, given the absence of both local leader coordination and fiscal support under the performance evaluation system, self-interested individual bureaus have an incentive to target complementary social assistance benefits for households tagged with Dibao to save the administrative cost of screening applicants for qualification.

**Research problem and research focus**

The research question is whether there a crowding out effect exists between social assistance programmes/Dibao and unemployment insurance, and if so, which of the two abovementioned mechanisms, namely direct versus aggregate Dibao benefits, is the more likely cause.

Using two different sets of city-level panel data covering over 280 Chinese cities from 2003 to 2011, this study tested the hypothesis that there is a crowding out effect between social assistance programmes and unemployment insurance. We found that while the Dibao programme itself does not crowd out unemployment insurance, the increasing aggregate benefit from Dibao, including both the direct benefit and the additional benefits from other complementary social assistance programmes, is the major cause of a crowding out effect.
Hypotheses

As the numbers enrolled for unemployment insurance in each city are not available, we used the number of registered unemployed as a proxy. Because only people registered as unemployed can claim unemployment insurance, the number of registered unemployed is closely and positively correlated with the number of people enrolled for unemployment insurance.

Two hypotheses corresponding to the above two mechanisms for the crowding out effect are proposed.

**Hypothesis 1:** *Increased government expenditure on social assistance programmes is associated with a smaller number of registered unemployed in a city.*

Government expenditure on social assistance programmes includes government expenditure on *Dibao* and other complementary social assistance programmes (e.g. medical, housing and educational assistance). Workers in the informal sector opt out of unemployment insurance due to a higher aggregate benefit from *Dibao* (including both the direct benefit and the benefit of other social assistance programmes).

**Hypothesis 2:** *Increased government expenditure on Dibao is associated with a smaller number of registered unemployed in a city.*

H2 suggests that the higher direct benefit of *Dibao* leads workers in the informal sector to opt out of unemployment insurance to claim *Dibao*. Unlike H1 which highlights the aggregate benefit, H2 implies that the direct benefit of *Dibao* is higher than the unemployment insurance benefit.

Data

This article uses city-level data to test the hypothesis that expanding social assistance programmes have a crowding out effect on unemployment insurance. City-level data
can reveal people’s responses to social programmes because city-level governments manage the eligibility and benefits of social programmes, which vary between cities.

Two data sources were used in this study. The first dataset was collected from the China City Statistical Yearbooks (NBS, various years), and includes observations of 282 cities (at prefecture level) covering 26 of 27 provinces (i.e. excluding Tibet) between 2003 and 2006. The data for government spending on social assistance at city level are published in the yearbooks for 2003 and 2006, whereas data for other years have not been released. The second dataset was collected from the MCA website, and contains Dibao data at the prefecture level from 2007 to 2011.

Both datasets cover only 282 of the 332 prefecture cities, as the yearbooks report data for only these cities. A prefecture city usually has both urban (i.e. city district) and rural areas (i.e. county). Because we are interested in urban social assistance programmes, most variables in our dataset are defined for the city district of these prefecture cities only.

**Methodology**

To avoid omitted-variable bias, we used a (city) fixed effect model, and to address the issue of simultaneity we used predetermined values for the independent variable. Nevertheless, we acknowledge that city-level data cannot indicate which individual characteristics are more likely to lead to opting out of unemployment insurance. There are also some concerns about the measurement of unemployment. However, for this paper, the number of registered unemployed is a sufficient indicator of the crowding out effect on unemployment insurance as only those registered as unemployed are eligible to claim.

It may be argued that the number of unemployed may be reduced via other causal
avenues such as the exogenous shock of other government policies or new initiatives that influence urban unemployment. To address this concern, we used local educational expenditure as the regressor in a placebo test. A lack of correlation between the number of unemployed and educational expenditure will confirm the existence of the crowding out effect.

**Basic model**

We estimated the following models:

\[
Unemployed_{i,t} = \beta Social\_assistance\_expenditure_{i,t-1} + \delta X_{i,t} + \mu_i + \omega_t + e_{i,t} \quad (1)
\]

\[
Unemployed_{i,t} = \beta Dibao\_expenditure_{i,t-1} + \delta X_{i,t} + \mu_i + \omega_t + e_{i,t} \quad (2)
\]

The only difference between (1) and (2) is the independent variable, which is social assistance expenditure in (1) and government expenditure on Dibao in (2). The dependent variable \(Unemployed\) is the number of registered unemployed in the city district of city \(i\) during year \(t\). \(\beta\) and \(\delta\) are parameters for the corresponding variable(s) in the model. \(X_{i,t}\) corresponds to covariates including average income, fiscal expenditure per capita, service sector size, local gross product and unemployed in the previous year. The term \(\mu_i\) denotes city dummy variables, \(\omega_t\) corresponds to year dummy variables, and \(e_{i,t}\) defines the error term. The control and independent variables are as follows:

1. **Social**\_**assistance**\_**expenditure** denotes city-level spending on social assistance programmes (in million RMB). Social assistance expenditure includes expenditure on Dibao and other complementary social assistance. We lag **Social**\_**assistance**\_**expenditure** by one year in the regression model.
Enrolees cannot opt out of unemployment insurance due to policy changes in the current year but may change their enrolment status the following year.

(2) Dibao_expenditure denotes city-level spending on Dibao programmes (in million RMB). Similarly, we use lagged Dibao_expenditure in the model.

(3) Population denotes the number of residents in the city district of a city (in millions).

(4) Fiscal expenditure for a prefecture city (in billion RMB) measures local fiscal capacity.

(5) Average income refers to the average annual wage in the city district of a city, based on salaries in the local formal sector.

(6) Gross product denotes the gross regional product in a prefecture city (in billion RMB), as a measure of local economic development and the size of economy.

(7) Service share is the share of the local service sector in the gross regional product. Although not directly linked to social assistance expenditure, the service sector is considered highly labour intensive, thus the larger this sector, the more people are employed. Consequently, the number of registered unemployed should be negatively correlated with the share of the service sector in the local economy.

(8) Informal sector size refers to the number of people working in the informal sector (registered small-scale private enterprises and self-employed) in the city district of a city.

(9) City and year dummies are also included.
Descriptive statistics

The descriptive statistics are shown in Table 1.

--- Table 1 approximately here ---

There are 1102 observations for social assistance expenditure between 2003 and 2006, and 1352 observations for Dibao expenditure between 2007 and 2011. The 2454 observations for registered unemployed and other variables cover the full period between 2003 and 2011.

Results

The result of the Hausman test suggests that the fixed effect models are more consistent than the random variable models, therefore only the fixed effect models are reported in Table 2.

--- Table 2 approximately here ---

Columns (1) and (2) report the results of equation (1) which regressed registered unemployment on government social assistance expenditure. In column (2), aggregate economic variables including registered unemployment, social assistance expenditure, fiscal expenditure, gross product and informal sector size are measured on a per capita basis.

In columns (1) and (2), expenditure on social assistance is negative and statistically significant. In column (1), an additional million RMB spent on social assistance is associated with 22 fewer registered unemployed. The magnitude of the effect of social assistance on registered unemployment is similar in column (2), when
variables are weighted by the number of people. This implies the existence of a crowding out effect between social assistance programmes and unemployment insurance. Hypothesis 1 is therefore supported.

While fiscal expenditure, average income and gross regional product are not statistically significant in columns (1) and (2), lagged unemployment is significant in both. One notable result relates to ‘informal sector size’. If all informal sector workers are enrolled in unemployment insurance, the informal sector size should be positively correlated with the number of registered unemployed, and the coefficient for informal sector size should be positive and significant. However, informal sector size is not significant in columns (1) and (2), consistent with the proposition that some informal workers are not enrolled in unemployment insurance.

Hypothesis 2 states that the crowding out effect is a result of expanding the direct benefit of Dibao. To verify this, we replaced the independent variable ‘social assistance expenditure’ with ‘Dibao expenditure’ (equation (2)). The regression results are reported in columns (3) and (4), with column (4) measuring all aggregate economic variables per capita.

Expenditure on Dibao is not statistically significant in columns (3) and (4), implying that increasing the direct benefit of Dibao is not correlated with the number of registered unemployed. This suggests that the crowding out effect does not result from increasing the direct benefit of Dibao, thus Hypothesis 2 is not supported.

A possible argument against Hypothesis 1 is that the decrease in registered unemployed may be caused by reasons other than the crowding out effect. In particular, increased government social expenditure such as education or health expenditure may affect the welfare and participation of the labour market.

To exclude the possibility that a change in the number of registered unemployed
is caused by reasons other than the crowding out effect, we conducted a placebo test by replacing social assistance expenditure with educational expenditure as the independent variable. Educational expenditure should not directly correlate with registered unemployed after controlling for local fiscal expenditure. This placebo test found that educational expenditure is not a statistically significant determinant of social assistance expenditure. This finding is consistent with the earlier results. Due to space limitations, the results of the robustness tests are not reported in detail.

In short, the above data analysis suggests that the crowding out between social assistance and unemployment insurance is a result of the increased aggregate benefit rather than the direct benefit of Dibao.

**Discussion and conclusions**

This article presented the crowding out effect between social assistance programmes and unemployment insurance. In particular, crowding out occurs when urban informal sector workers voluntarily opt out of unemployment insurance and claim social assistance benefits instead. However, the welfare implications of this are unclear. Given that people opt out of unemployment insurance voluntarily, the crowding out may be welfare enhancing. Nevertheless, this crowding out may cause welfare losses in two ways. First, welfare will be lower for households with an income just above the Dibao line, who thus do not qualify for Dibao. In this case, the crowding out between social programmes leads to inefficient allocation. Second, the crowding out encourages the persistence of the informal sector, as households in this sector claiming social assistance are better off than households remaining in the formal sector, who must enrol in the unemployment insurance programme.

The crowding out among social programmes stems from ineffective coordination...
among government departments. However, there may be two very different institutional reasons for this lack of coordination. First, the policy design of ministries at the central level neglects the crowding out effect by failing to coordinate the central ministries, and local governments mechanically follow the directions of central ministries. Second, if central ministries are responsible only for drafting and distributing general guidelines while local governments have large discretion over implementation, crowding out may result from the misalignment of incentives and institutions in policy design and implementation between central and local government in the context of decentralised welfare delivery.

The paper argues that the second possibility is more likely under China’s dual decentralisation. While the central government has initiated many social programmes, recent studies report that local governments have large discretion over the implementation of these programmes, including setting benefit levels, eligibility conditions and more (e.g., Li, 2011). Where crowding out occurs among social programmes, misalignment of the incentives and institutions between central and local government is the more likely reason, given the wide discretion of local governments.

Unlike the literature highlighting the promotion of economic growth through bureaucratic incentives (Li and Zhou, 2005; Xu, 2011), this paper identifies the adverse consequences of bureaucratic incentives in social policy implementation in China. While the performance evaluation system is very useful in incentivising local officials to promote economic growth, it may also have unintended consequences for social programme implementation. In particular, under a performance evaluation system that stresses economic growth, local government leaders lack incentives to coordinate government departments and allocate fiscal resources to welfare delivery.
This paper also proposes an important issue in social policy implementation under dual decentralisation. Although the central state continues to expand social welfare provision, the emerging fragmentation in local welfare programmes creates strong negative incentives to subnational governments. On the one hand, the central state continues to use local officials to expand welfare provision and navigate the direction of local experimentation. On the other hand, these officials generally lack the financial incentive to provide good welfare for domestic, economic and political reasons, as illustrated by the crowding out effect. Further, in a more general policy context, as regional social programmes are largely financed through local budgets, they tend to become exclusive in nature, preventing outsiders from sharing the resources (Mok, 2015). For example, people without local Hukou are not qualified to claim Dibao. Regional experimentation with social programmes is likely to generate self-reinforcing institutional inertia that is difficult for central government to overturn later through attempts at standardisation (Shi, 2005; Peng, 2011). As a consequence, local agents redefine local policy goals and implement ‘new’ policies with enhanced local capacity (Mok and Wu, 2013).

The findings of this paper are also consistent with the concept of fragmented authoritarianism. Welfare losses through crowding out render policy implementation ineffective. However, each bureau at the local level operates rationally in terms of its departmental interests. While local MCA bureaus carefully design the Dibao benefit level to be lower than that of unemployment insurance, other bureaus have incentives to provide in-kind assistance to households eligible for Dibao to save the administrative costs of screening applicants to target the appropriate recipients.

Conceiving the Chinese political economy as developmental, we should note that China’s fragmented bureaucratic structure and factionalised key agencies/units remain
very active in shaping social and economic developments, particularly where a cadre of state officials (whether at central or sub-national level) is charged with improving developmental outcomes, providing them a degree of decision-making autonomy in the context of a relatively weak civil society (Leftwich, 2000). However, this paper shows that while the performance evaluation system is effective in promoting economic growth in the context of the fragmented and decentralized bureaucratic system, there are adverse consequences of the performance evaluation system as revealed in the area of social policy implementation. In conclusion, the crowding out among social programmes discussed in this paper clearly demonstrates the dynamism and complexity of policy implementation in China which involves a wide range of actors with diverse economic and political interests at both the central and subnational level.
References


Zhou X et al. 2013. A behavioral model of ‘muddling through’ in the Chinese
Table 1: Descriptive statistics

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<tr>
<td>Unemployment (thousands)</td>
<td>2454</td>
<td>12.39</td>
<td>14.64</td>
<td>0.261</td>
<td>147.97</td>
</tr>
<tr>
<td>Social assistance expenditure (million RMB)</td>
<td>1102</td>
<td>79.09</td>
<td>102.44</td>
<td>4.29</td>
<td>922.10</td>
</tr>
<tr>
<td>Dibao expenditure (million RMB)</td>
<td>1352</td>
<td>105.4</td>
<td>77.98</td>
<td>3.21</td>
<td>575.47</td>
</tr>
<tr>
<td>Fiscal expenditure (billion RMB)</td>
<td>2454</td>
<td>5.09</td>
<td>8.33</td>
<td>0.13</td>
<td>124.96</td>
</tr>
<tr>
<td>Average income (thousand RMB)</td>
<td>2454</td>
<td>22.96</td>
<td>8.12</td>
<td>5.16</td>
<td>70.72</td>
</tr>
<tr>
<td>Gross regional product (billion RMB)</td>
<td>2454</td>
<td>46.04</td>
<td>77.70</td>
<td>1.21</td>
<td>991.58</td>
</tr>
<tr>
<td>Population (millions)</td>
<td>2454</td>
<td>1.15</td>
<td>0.97</td>
<td>0.14</td>
<td>8.84</td>
</tr>
<tr>
<td>Share of service sector (%)</td>
<td>2454</td>
<td>41.00</td>
<td>10.63</td>
<td>8.58</td>
<td>78.66</td>
</tr>
<tr>
<td>Informal sector size (thousands)</td>
<td>2454</td>
<td>177.18</td>
<td>309.17</td>
<td>1.12</td>
<td>4307.122</td>
</tr>
<tr>
<td></td>
<td>(1) Unemployment per 1000 people</td>
<td>(2) Unemployment per 1000 people</td>
<td>(3) Unemployment per 1000 people</td>
<td>(4) Unemployment per 1000 people</td>
<td></td>
</tr>
<tr>
<td>--------------------------------</td>
<td>----------------------------------</td>
<td>----------------------------------</td>
<td>----------------------------------</td>
<td>----------------------------------</td>
<td></td>
</tr>
<tr>
<td>Social assistance expenditure (lagged)</td>
<td>-0.0222** (0.00922)</td>
<td>-0.0193* (0.0100)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dibao expenditure (lagged)</td>
<td></td>
<td>-0.001 (0.00506)</td>
<td>0.000637 (0.00284)</td>
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</tr>
<tr>
<td>Fiscal expenditure</td>
<td>-0.488 (0.372)</td>
<td>-0.248 (0.658)</td>
<td>-0.188** (0.0832)</td>
<td>0.102 (0.0973)</td>
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</tr>
<tr>
<td>Population</td>
<td>1.267 (1.156)</td>
<td>0.584 (0.564)</td>
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<td></td>
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<tr>
<td>Average income</td>
<td>-0.009 (0.146)</td>
<td>-0.0234 (0.174)</td>
<td>0.0274 (0.0454)</td>
<td>-0.0224 (0.0505)</td>
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</tr>
<tr>
<td>Unemployment (lagged)</td>
<td>0.149*** (0.0331)</td>
<td>0.134*** (0.0325)</td>
<td>0.331*** (0.0314)</td>
<td>0.297*** (0.0290)</td>
<td></td>
</tr>
<tr>
<td>Informal sector size</td>
<td>0.00664 (0.00419)</td>
<td>-0.00237 (0.00671)</td>
<td>-0.0002 (0.00161)</td>
<td>0.00186 (0.00253)</td>
<td></td>
</tr>
<tr>
<td>Service share</td>
<td>0.0263 (0.0644)</td>
<td>0.0399 (0.0764)</td>
<td>0.0171 (0.0392)</td>
<td>0.0260 (0.0434)</td>
<td></td>
</tr>
<tr>
<td>Gross product</td>
<td>0.0349 (0.0346)</td>
<td>0.0737 (0.0583)</td>
<td>0.0258** (0.0122)</td>
<td>0.0160 (0.0187)</td>
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</tr>
<tr>
<td>Constant</td>
<td>10.25*** (3.559)</td>
<td>10.10*** (3.952)</td>
<td>6.042*** (2.122)</td>
<td>5.736*** (2.214)</td>
<td></td>
</tr>
</tbody>
</table>

City fixed effect: Yes
Year dummy: Yes

N: 1102
R²: 0.5307

Standard errors in parentheses. * p<.1, ** p<0.05, *** p<0.01. In columns (2) and (4), the aggregate economic variables unemployment, social assistance expenditure, fiscal expenditure, gross product and informal sector size are weighted by local residential population.