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# The economic causes and consequences of social instability in China ☆

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ABSTRACT

This paper provides a survey of the economic literature relevant to social instability in China and moulds it into an argument. The objective is to offer a fresh view of economic policy and performance through the lens of the threat posed by social instability. This is a concept that economists rarely analyse, and yet it can lurk behind much economic policy-making. China's leadership has often publicly expressed its concern to avoid 'social instability'. It is viewed as a threat both to the political order and to the continued rapid growth of the economy. This threat to growth in turn endangers the maintenance of social stability. The paper examines the likely economic determinants of social instability, using both surveys and other evidence. After discussing the determinants of China's rapid growth, the paper goes on to examine the likely mechanisms by which social instability can affect the growth rate. There is a case for more research on the role of social instability in the economic development process.



## 1. Introduction

It is relatively unusual for development economists to analyse the economic causes and consequences of social instability.[1] Yet it is not unusual for governments of developing countries to worry about social instability, especially if they lack democratic legitimacy. This worry can in turn be important to their economic policy-making. The Chinese government during the period of economic reform provides a good example. Social instability is viewed as a threat both to the political order and to the continued rapid growth of the economy. China's leadership has often publicly expressed its concern to maintain social stability. For instance, according to Shirk (2008: 52), the term 'social (in)stability' had appeared 700–800 times a year over the previous decade in the *People's Daily*, a Chinese Communist Party (CCP) mouthpiece.[2]

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[1] Notable exceptions include Aisen and Veiga (2011), Alesina and Perotti (1996), Alesina, Ozler, Roubini, and Swagel (1996), Campos and Nugent (2002), Collier and Hoeffler (2004), Easterly, Ritzen & Wollcock (2006), Mauro (1995), and Perotti (1996). Most of these are concerned with consequences rather than causes, and with political shocks greater than any experienced by China during its period of economic reform.

[2] There might be some overstatement of the danger insofar as the CCP wants to portray itself as the bulwark against chaos.

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There is evidence that social unrest, as proxied by a proliferation of citizen protests and petitions, has indeed been rising in China. The number of 'mass incidents' (cases of civil unrest, officially recorded) rose from under 9000 in 1993 to 180,000 in 2010.[3] Minzner (2005: 1) quotes a statement of a public security official to the effect that the foundation of social order in China is fragile and that social stability is achieved within an environment of 'unceasing, tough public security measures'.

It is arguable that such concerns have moulded economic policy-making. The reform leadership's economic policy was essentially to accord overriding priority to the achievement and maintenance of rapid economic growth. In this way China became a 'developmental state' (Knight & Ding, 2012). For the first quarter of a century of economic reform, rapid growth was viewed as the one true path to secure political legitimacy and to avoid social instability. However, the remarkable transformation of China's economy and society that rapid growth entailed itself posed new threats. The leadership's subsequent secondary objective of achieving a 'harmonious society' is a response to the need to maintain social stability in the evolving circumstances.

The paper provides a survey of the economic literature relevant to social instability in China and moulds it into an argument. The objective is to take a fresh view of economic policy-making and economic outcomes through the lens of the threat posed by social instability. It is argued that social instability can potentially have serious adverse effects on the economy, and that the threat has been at the heart of economic policy-making. The phenomenon is examined from a narrow economic perspective: no attempt is made at a broader analysis, for instance of its relationship to China's future political order.

The methodological difficulties confronting economic research into social instability are to measure this elusive concept, the effects of its hypothesised economic determinants, and its hypothesised effects on economic outcomes. The more authoritarian the state, the more difficult it is for researchers to obtain the relevant information. We draw extensively on a multipurpose national household survey which asked many socioeconomic questions – but not the ideal ones for the current purpose. We also draw on relevant official sources and international surveys, as well as the academic literature on this issue.

In Sections 2–5 we examine the likely economic sources of social instability, concentrating on income and its change in Section 2, inequality in Section 3, insecurity in Section 4, and institutions and governance in Section 5. The factors underlying China's virtuous circle of rapid growth are explained in Section 6, and the possibility of social instability generating an adverse shock that might break that virtuous circle is examined in Section 7. The concluding Section 8 considers the implications of the analysis for policy and for research.

## 2. The causes of social instability: Income and its change

In order to analyse the causes of social instability in China we examine the determinants of subjective well-being. The reasoning is that unhappy people, dissatisfied with life, are more likely to be socially discontented than happy people, and that the causes of unhappiness suggest pointers to the sources of social discontent.[4] The China Household Income Project (CHIP) national household survey of 2002 provided questions on subjective well-being, and there was a separate module on subjective well-being in the questionnaire for the rural subsample.[5] In this way it is possible to analyse the effects of income and its growth, economic inequality, and economic insecurity on subjective well-being.

The key dependent variable is derived from the question, common to all three subsamples: how happy are you nowadays? Five possible answers were allowed: very happy, happy, so-so, not happy, not at all happy. This can be used as a cardinal variable (with the answers being scored 4, 3, 2, 1 and 0 respectively) or as an ordinal variable. In the former case linear regression, and in the latter case ordered probit analysis, is conducted. Both were estimated but in no case did the choice of method affect the interpretation significantly. We report only the cardinal results as they are simpler to interpret. In the rural subsample, for which a separate question on satisfaction with life was available, the choice of dependent variable made no significant difference to the interpretation: the terms subjective well-being, life satisfaction, and happiness are used interchangeably.

Analyses of the 2002 survey are reported in Knight, Song, and Gunatilaka (2009), Knight and Gunatilaka (2010a,b, 2011, 2012). A striking feature of the results for all three subsamples – comprising rural, urban and migrant households – is their regularities. Many coefficients are statistically significant, generally understandable, similar across samples, and in line with the results from other countries or contexts. The happiness functions are meaningful and informative although there can be disagreement about the conclusions that should be drawn from them.

It is a universal finding in happiness studies around the world that happiness rises with income in the cross-section – in line with theoretical expectations. This is true also of China, and in all three subsamples of the CHIP 2002 data set (for instance, Knight & Gunatilaka, 2011). The effect of instrumenting income is to raise its positive coefficient, possibly because the instrumenting eliminates the effect of an unobserved variable such as aspirations: exogenous aspirations may reduce happiness but, by fostering ambition, may also raise income. Even in the urban sample, for which the income coefficient is highest, the size of the effect is surprisingly small both absolutely and by comparison with the effect that various other determinants, discussed below, have on happiness: a doubling of income raises the happiness score by only 0.22 units (Knight & Gunatilaka, 2011: 9).

Two studies have been made of the role of perceived change in income over the previous five years. Knight et al. (2009: 639) used a question in the rural survey: 'how has your household's living standard changed over the last five years?'. The answers permitted

[3] Perhaps for political reasons, the figure was not officially reported beyond 2008 (when it was 127,000); the figure for 2010 is attributed to Sun Yiping of Tsinghua University.

[4] This assumption is examined further in the concluding Section 8, in the light of the evidence and argument.

[5] Designed by the author with funding obtained from the Oxford-Manchester Global Poverty Research Group supported by the UK ESRC.