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Unemployment duration and earnings of re-employed workers in urban China

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Abstract

The recent draconian program of labor retrenchment in China caused widespread unemployment. Many of the retrenched workers remained unemployed for a long time. How did the duration of their unemployment affect their re-employment earnings? The possible relationships between unemployment duration and subsequent wages are modelled heuristically, four explanations for a negative relationship being found. This hypothesis is investigated by means of a survey of workers in 13 Chinese cities, conducted in 2000. Re-employment earnings are found to decline as unemployment continues, an effect that is both statistically significant and quantitatively important. China's displaced workers face a tough labor market.

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1. Introduction

The restructuring of Chinese state enterprises resulted in over 37 million workers being laid-off over the period 1995–1999. Fewer than half of them had been re-employed, either formally or informally. How do the re-employed workers fare in the labor market? Does their duration of unemployment affect their wages? These questions will be investigated in this paper. To answer them, we analyse the data from a household survey in urban China conducted in 2000.

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Table 1
Restructuring the urban labor market, 1994–2000

	1994	2000	Change 1994–2000
Urban employment (million)	184.1	231.5	47.4
Employment in urban units (million)	152.6	116.1	–36.5
Of which: State-owned	112.1	81.0	–31.1
Urban collectives	32.9	15.0	–17.9
Other ownership	7.6	20.1	12.5
Other urban employment (million)	33.9	115.4	81.5
Registered unemployment (million)	4.8	6.0	1.2
Xia gang employment (million)	1.6	9.1	7.5

Source: National Bureau of Statistics of China, 1995 and 2001 editions.

The process of economic transition has had a significant impact on the urban labor market. The new enterprises — mainly privately-owned and self-employed — could not grow quickly enough to absorb the laid-off workers. Unemployment, in both official and *xia gang* — off sentry duty—form, has risen sharply and in 1999 represented 9.6% of the urban labor force. The urban labor market is segmented between those who have never lost their jobs and those who have. The former are relatively protected against competition, whereas the latter face a tough and restricted labor market. In this buyers' market they may have to take whatever jobs are available, rather than jobs which match their productive characteristics such as ability and skill. Using the same data set, Appleton, Knight, Song, and Xia (2002) found evidence of segmentation between these two groups of workers, with the re-employed at a distinct disadvantage. It was this finding that induced us to pursue further the nature of the labor market facing retrenched workers. In particular, we wish to examine the effects of their unemployment duration on the earnings of workers when they re-enter employment.

There is considerable evidence from various countries that re-employment earnings decline after worker displacement, i.e. involuntary mobility. For instance, Crouch (2001) for Germany, and Fallick (1996) and Kletzer (1998) for the United States reported cuts in the range 6–16%. A fall in earnings is more likely to occur after an involuntary separation, but it is possible even after a voluntary quit. Gregory and Jukes (2001) examined the effect of both the incidence and duration of unemployment on the earnings of British men, 1984–94. Unemployment itself, whether voluntary or involuntary, carried an earnings penalty of 10% within the first year, falling to less than 4% after two years. Unemployment duration added a further penalty — of one per cent after a month, 5% after 6 months and 11% after 12 months. Moreover, the depressive effect of duration, unlike incidence, continued: this scar was permanent. Nickell, Jones, and Quintini (2002) obtained even stronger results for British men in the 1990s. Earnings were lower after being unemployed, voluntarily or involuntarily, by 11% immediately and 13% permanently. There was an additional earnings loss if the unemployment exceeded six months: 18% immediately and 10% permanently. Pichelmann and Riedel (1993) found that in Austria a 10% increase in unemployment duration is associated with a 0.8% fall in re-employment earnings. There is thus international evidence that re-employment wages tend to fall as the duration of unemployment lengthens. Is that true also for China?

In Section 3 we sketch out hypotheses about the effect of unemployment duration on wages. Section 4 describes the data and provides some descriptive statistics. Section 5 briefly summarises the findings of others concerning the effect of retrenchment itself on wages, using the same data set. Our methodology is explained in Section 6. Estimates of the relationship between unemployment duration and wages are presented in Section 7. Section 8 concludes.

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