The Economic Basis for Social Unrest in China
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Social unrest in China

Much of our recent attention has focused on anti-Japan riots in China, yet a competing story in recent years is the extraordinarily scale of social unrest linked not to patriotism and foreign policy but to economic tensions and perceived economic loss. Some analysts even allow that the anti-Japanese riots themselves were permitted to continue so that China’s citizenry could “blow off some steam” over government’s poor economic performance (McLaughlin 2005).

The most recent available statistics, from police records for 2003, indicate 58,000 protests that year involving 3 million protesters in all (Table 1 and Tanner 2005). The average size of protests and demonstrations grew from 8 persons in 1993 to 52 in 2003 (Liaowang magazine, cited in Tanner 2005). Reports of large-scale incidents in 2004 continue to appear (see below). Some are directly linked to economic issues, while others are sparked by a non-economic incident but are reported as reflecting depressed economic conditions affecting the demonstrators.

This memo presents an analytical framework for considering the economic roots of these disturbances, without pretending to have conducted independent research into the scale and nature of the demonstrations themselves.

The memo’s general hypotheses and conclusions are that economic tensions underlying large-scale disturbances involve a dual-layered process. First, disturbances derive most of their basic energy directly from dissatisfaction over the impact of economic reforms and market-based modernization. Second, widespread enterprise and government corruption and malfeasance supplement and greatly amplify this basic dissatisfaction.

Reforms and modernization unleash conflicting claims over limited resources, and it is not clear that any form of government at either the central or local level, including those based on multi-party competitive elections, could eliminate the resulting dissatisfaction. (Arrow 1951) It does seem clear, however, that more effective national and local governance could greatly mitigate the formation of unrealistic expectations and the exacerbation of dissatisfaction due to corruption and corporate lawlessness.

Table 1

<table>
<thead>
<tr>
<th>Year</th>
<th>Incidents of Social Unrest in China</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>8,700</td>
</tr>
<tr>
<td>1994</td>
<td>10,000</td>
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<tr>
<td>1995</td>
<td>11,500</td>
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<td>1996</td>
<td>12,500</td>
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<td>1997</td>
<td>15,000</td>
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<td>1998</td>
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</tr>
<tr>
<td>2002</td>
<td>50,400</td>
</tr>
<tr>
<td>2003</td>
<td>58,000</td>
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Growth and the economics of social unrest

The simplest economic explanation of social unrest—that faltering growth causes unrest—fails to explain the trends mentioned above. The number of incidents did indeed accelerate during the difficult years of 1997-99, when domestic economic policy errors affecting the rural areas sent China’s overall economic growth rate into a serious slump. But as China’s economy boomed in the 2001-to-2003 period, the number and scale of incidents continued to rise sharply (Table 1 and Tanner 2005).

An alternative and more plausible explanation is microeconomic rather than macroeconomic—that dislocations and dissatisfactions accelerate with structural reform and modernization and that in China, reform and modernization are proceeding rapidly during both the boom and the slump phases of its macroeconomic cycle. This was especially evident during the most recent cycle, but it held in the past as well, with tragic consequences.

In the latter 1990s, GDP growth slumped to as low as 4.5% (Keidel 2001). Losses and the build-up of unsold inventory became so obvious to policy makers and workers alike that officials could feasibly initiate state-owned enterprise (SOE) reforms involving layoffs of one-third of all SOE and collective workers, or 50 million workers, by end-2004—with 30 million jobs lost in the span of just three years from 1997-99 (NBS 2005). Meanwhile, during this same period, the initial rural policy errors caused household consumption in rural areas to decline in absolute terms, while employment in township and village enterprises (TVEs) also declined. These difficult rural conditions increased both the share and number of households below the rural poverty line and pushed increasing numbers of rural workers to migrate to towns and cities in search of jobs.

Since 2000, while growth has boomed, SOE and collective layoffs have continued, with more than 20 million additional lost SOE and collective jobs by the end of 2004 (NBS 2005). Meanwhile, reform and restructuring have taken additional forms that generate new dislocations without alleviating earlier ones. The boom has been centered in regions and sectors both far removed from the laid-off workers in various rust-belt provinces and far removed from farmers in low-income grain-belt regions. At the same time, the boom has brought accelerated infrastructure, industry and real estate investments, which have stepped up displacement of rural and urban residents from their homes and land. Finally, loss of in-kind health and education benefits for urban workers and separation from village-based support for rural workers have only worsened the impact of layoffs and loss of homes and land. In these ways the economy has become rapidly more monetized without providing adequate monetized income for large segments of the labor force.

In short, personal disruptions from reforms and modernizing investment have been severe and on-going, in times of both slump and boom. A slight shift in interpretation might say that the initiation of accelerated SOE reforms in the latter 1990s put in motion a wrenching process of reforms in the whole household registration (hukou) system on which SOE and collective employment and welfare depended—a reform process that continues and if anything gains momentum today, through good times and bad.
Many forms of social unrest with an economic basis

If the underlying economic hardships experienced by large numbers of individuals reflect the overall impact of reform and modernization, the specifics of these hardships and resulting unrest take many forms. This memo will merely touch on several as representative of the widespread nature of the phenomenon. While overall statistics reported above come from official sources, a cataloguing of individual incidents is apparently difficult, and we are left with a collection of anecdotal descriptions of various incidents. Research resource limitations for this memo could not allow a more comprehensive list. It nevertheless gives some flavor of the unrest common in China recently.

**Low and unpaid wages.** Workers frequently demonstrate to protest low wages and work conditions, in addition to expensive company store, dormitory and other expense charges. For example, in April 2004 more than a thousand workers went on strike in two factories in southern China demanding higher pay and one day off a week, resulting in the arrest and sentencing of the strike leaders to up to 3½ years in prison. (BBC 2004, Chan 2004)

**Layoffs and unpaid back wages.** Workers frequently take the law into their own hands to protest layoffs and unpaid wages. For example, in November 2004, workers at one factory in southern China took their bosses hostage over unpaid back wages, and also in November workers in another factory in the same town fought with security guards to protest layoffs. (Chan 2004)

**Loss of worker benefits.** Loss of health and pension benefits has disenfranchised large numbers of urban *hukou* workers. For example, in March 2002, 80,000 retired workers protested in two towns in China’s northeast over unpaid pensions. (Zhao & Wen 2002)

**Union representation.** Labor unions are illegal in China, but official labor organizations do little to protect workers from employer malfeasance with local government collusion. Efforts to form independent labor organizations lead to confrontations with police and often violent clashes. For example, in 2004 in Shaanxi Province 7,000 textile workers reportedly struck for seven weeks when they were forbidden to form their own union. (Marquand 2004)

**Environmental degradation.** Economic development leading to deforestation and grassland overgrazing are converting vast stretches into desert and forcing rural migrants into cities where they are not welcome. For example, in 2001 in China’s northeast, migrants from desertified areas working as pedicab drivers blocked the entrance to a government compound to protest local government efforts to use high fees to force them out of town. (Economy 2003)

**Access to water.** Water shortages in the north of China lead to social unrest over access to what limited supplies are available. For example, in 2000 in eastern Shandong Province a thousand villagers fought with police for two days over access to water for irrigation. (Economy 2003)

**Tolls and fees.** Many protests object to fees and exorbitant tolls levied by local officials—in part to pay for public services and in part to supplement their official incomes. For
example, in November 2004 a woman’s anger at bridge tolls apparently led 30,000 persons to riot, confronting hundreds of police and paramilitary units, leaving one person dead. (Chan 2004)

**Land condemned for public use.** Citizens faced with relocation to make way for roads, airports, dams and other sanctioned public investments have little effective legal recourse to ensure just compensation, leading them to demonstrate publicly. For example, in October 2004 in Sichuan Province, 90,000 peasants reportedly fought with police over losing their homes for little compensation to make way for a hydroelectric dam. Only martial law restored order. (Marquand 2004, Mooney 2004) Demonstrations against both the relocation and environmental damage from dams are reportedly growing in size, frequency and sophistication as activists organize across provinces and with the support of central government environmental agencies. (Economy 2004)

**Ethnic tensions.** Ethnic tensions apparently often exacerbate the economic stress brought on by economic dislocation. For example, fighting broke out in 2004 in the southern city of Guangzhou between Moslem Uighur migrants and local riot police after security guards stopped Muslims from selling fried mutton in a shopping district. (Mooney 2004) In Henan Province in October 2004 an ethnic battle between Han Chinese and Muslim Hui minorities using farm implements left many dead, including 15 policemen, by one account. But the link to economic tension was not so straightforward, since the widespread fighting was sparked by a traffic incident in which a Hui refused to pay compensation to a Han. The inferior economic opportunities available to the migrant Hui households is one explanation given by a local Hui interviewed by the media. (Marquand 2004, Pocha 2004)

**Economic analysis of Chinese social unrest—productivity, remuneration and tastes**

In economic terms, a great deal of observed social tension over the past 25 years in China can be better understood by considering what reforms and global opening have done to patterns of productivity, remuneration and lifestyle expectations. Rapid changes have rewarded many beyond their dreams while at the same time disenfranchising many others who had established standards of living to which they had become accustomed and committed.

Shifts in productivity, pay and expectations reflect changes in at least three critical dimensions—relative prices, location and aptitude requirements. Increased monetization of the reforming economy provides a sub-theme for all of these dimensions. Changes in these dimensions are unavoidable aspects of reform and modernization, and for many people they inevitably generate large and worsening mismatches between expected and actual rewards. These unavoidable mismatches make the job of neutralizing economic dissatisfaction impossible. But a clearer understanding of how they work may help mitigate tensions.

**Relative price shifts since 1978**

Relative price shifts since the start of reforms in 1978 are one of the most powerful levers in China’s emerging market economy responsible for economic dislocations.
example is in rural-urban terms of trade—prices paid for rural products versus prices for urban products—and what their shift has done to SOE finances and urban standards of living.

Beginning in the early 1980s, prices of rural products began to rise relative to prices of goods made in the city. At the same time, rural productivity in the early 1980s jumped dramatically with the breakup of communes and revival of household farming on individually managed plots. Matters came to a head very quickly in 1984-85, when production of rural goods, especially grain output, grew so rapidly with reformed higher prices so remunerative, that cities and local governments ran out of cash with which to buy them. This early and most famous incidence of “hard-to-buy, hard-to-sell” (nanmai nanmai) ushered in more than a decade of urban inflationary booms alternated with credit-tightening job-cutting slumps.

The immediate result of these price shifts favoring rural areas was the realization that urban productivity was not high enough, when combined with the higher relative rural prices, to pay for the standard of living once guaranteed to all registered urban households. Not only were food prices higher, but construction materials and other rural products also became more expensive. The longer-term result of the shift in relative prices was that urban households needed larger and larger direct cash subsidies through official urban distribution centers, and when these became too great a government budget burden, retail price reforms coupled with matching urban wage increases shifted the financial burden onto employers, especially SOEs and urban collectives. As SOE financial burdens in support of the accustomed urban hukou standard of living grew, so did SOE losses. The climax to this shift in relative prices began to unfold in the late 1990s as SOEs and urban collectives rapidly began to reduce their cost burdens by laying off workers.

Exacerbating the direct impact of relative price shifts on urban household purchasing power was its impact on urban incentives to work harder to compensate for less advantageous terms of trade. Rather than understanding these changes to be a natural part of the reform shift from central planning to a market-based economy, urban workers saw them as unjustified deterioration in their accustomed standards of living. Hence, instead of providing incentives to work harder and adapt to new realities, these price shifts brought about a series of three major social unrest incidents in the middle-to-latter 1980s, all with deep economic foundations.

While the most famous of such unrest incidents was in Tiananmen Square in May-June 1989, smaller-scale demonstrations also reflected similar economic frustrations—first in the summer of 1985 and second in the winter of 1986-87. In all three cases, the economic roots of the unrest were camouflaged by claims of a higher purpose—anti-Japanese activism in 1985 and pro-democracy activism in 1986-87 and at Tiananmen in 1989. Despite the publicity given to the pro-democracy rhetoric of the latter two movements, closer examination reveals the shallow nature of their democracy components and the powerful economic underpinnings for the anger and frustration released by students and workers alike. (Keidel 1992)

1 “Hard to buy” because while farmers had cash, the stores were sold out of manufactured products from the cities, and “hard to sell”, because while farmers had good harvests and guaranteed purchase prices, government procurement offices closed down because of shortages of funds.
In sum, China’s economy today is still reeling from the impact of relative price shifts begun in the early 1980s, shifts made only worse by the slower productivity response of urban workers in their traditional occupations compared to the productivity increases of those urban and rural workers who have adapted to the new more demanding work environment of a competitive market economy.

**Regional productivity shifts**

Nowhere is necessary adaptation to new and natural productivity patterns more difficult than in the dimension of regional location. This is the second great economic dimension of underlying shifts responsible for social unrest. Most of the new opportunities presented by market and globalizing reforms are in coastal and other centers of transport and communication. Most of China’s labor force, however, is in interior cities and farm belts. The need to move locations to enjoy modern productivity gains is one of the greatest sources of economic inequality and dissatisfaction.

Interior concentrations of manufacturing labor reflect circumstances and policy decisions in the nearly 30-year Maoist period, as well as patterns of rural population concentration thousands of years old. First, cut off from the rest of the world by the Korean War, China relied completely on the USSR for technology in its first five-year plan (1953-57). Hence, a large industrial concentration accumulated in Manchurian cities, far from the coast, at the end of the trans-Siberian railway. This area is today the northeast (*dongbei*) rust belt.

Second, when fear of global nuclear war and fighting in Vietnam made coastal installations appear vulnerable, the Cultural Revolution’s “Third Front” industrialization strategy shifted major industrial concentrations deep into interior provinces where they would be able to support a war of resistance against foreign occupation. These industrial concentrations, from Guizhou to Lanzhou to Xian, are today China’s interior rust belts.

Third, the plentiful farmlands of China’s central alluvial regions, especially where combined with good rainfall in the Yangtze River basin and all to its south, mean that these regions, because of high per-hectare farm productivity, have for thousands of years supported large populations far from today’s centers of modern employment opportunities. These large and heavily populated interior farm regions today contain China’s impoverished grain belt areas.

In all three dimensions of inappropriately located population concentrations, no degree of policy success could avoid the market-oriented shift in relative productivity and value added advantages away from these regions toward the coast and other major natural crossroad locations. The only viable long-term solution to these regional gaps in productivity and income is large-scale migration from low-productivity to high-productivity locations—from interior to coast and from farmland to cities.

The relevance of location factors for economically based social unrest is two-fold. First, workers and households living in low-productivity locations do not interpret their plight as being due to natural and understandable shifts made necessary by reform and modernization. Instead, they attribute their difficulties to injustice and government incompetence. They do not
immediately see out-migration as a natural solution. Second, incentives for migration in many cases end up spurring young and enthusiastic workers to compete in cities with traditional established urban workers. In many cases, the combination of urban hostility toward migrants, migrant competition for good city jobs, and poor migrant working conditions is a potentially explosive combination responsible for economic-based social unrest.

**Market requirements for work aptitude – education, initiative and elbow grease**

Finally, the third major dimension of shifts in productivity and remuneration is that of aptitude for productive employment. Aptitude encompasses education, skills, entrepreneurial smarts and energy, and the willingness to work hard in possibly unattractive working conditions. Between the 1980s and 1990s, for example, as a result of market reforms, educational attainment became increasingly correlated with household income. While into the 1980s a person’s weaker educational attainment might not be much of an income handicap, ten years later it was. Similarly, in contrast to the pre-reform work attitude relying on the enterprise or “work unit” for guaranteed lifestyles, the new reform-era qualities of hustle, ingenuity, and risk-taking became highly prized attributes enjoying levels of remuneration as good as if not better than that of the typical SOE worker. No amount of policy ingenuity could neutralize the anger and frustration of those who find themselves without the more productive aptitudes.

A second aptitude gap is between rural and urban workers. Rural workers coming to the city, because of a generally less privileged upbringing, have a much greater aptitude for undertaking dirty and physically tiring work. This gap reflects the difficulties of shifting one’s lifetime expectations of a certain established package of job quality and living standard. While in many cases this is convenient for ensuring that necessary urban services and other tasks can be provided economically, it also characterizes urban worker attitudes about accepting less prestigious employment after being laid off from an SOE. (Chen 2004) Tensions generated by productivity and remuneration shifts in this dimension are an unavoidable part of market reforms and modernization.

A third aptitude gap emerges because of the shifting structure of the economy, away from farming and manufacturing into services. Workers, especially older workers, with a traditional aptitude for farming or assembly line work, find it difficult to learn the new skills needed to work in the service sector, much less in the newly expanding higher-tech dimensions of China’s manufacturing expansion. To the laid-off worker, it just seems that there are no suitable jobs remaining. And yet this rapid structural transformation of China’s economy by sectors is the very essence of market reform and modernization. Related disaffections are impossible to avoid.

Other examples of shifts in productivity and remuneration brought on by market reforms and modernization would emphasize the same point. Whether caused by price shifts, location differences or newly revealed aptitude mismatches, economic disaffection is unavoidable and will predictably lead to higher incidence of social unrest as the pace and scale of reforms increase.
Corruption and malfeasance amplify unavoidable instances of economic dissatisfaction

While reforms and modernization make popular dissatisfaction and social unrest unavoidable, corruption and malfeasance by employers and government worsen the impact of these trends to such a degree that what may have been bearable in the transition to markets and global opening becomes insufferable, triggering open hostility and violence. Hence, while it would be a mistake to attribute social unrest completely to corruption and malfeasance, corruption and malfeasance clearly generate much of the distrust and anger that converts underlying economic disaffection into open social unrest.

While this is not a memo intended to catalogue and analyze corruption in China, it is useful to mention a handful of corruption dimensions that act to worsen the impact of reforms on citizen circumstances and hence the economic basis for social unrest. This list is intended to be suggestive, not exhaustive. ²

**Fees and tolls.** The abuse of local authority to levy fees and tolls has, until recently, been a major bane of both rural and small-town life, and it remains to be seen whether fee-to-tax reforms begun nationwide in 2003 will significantly improve the situation. Before the fee-to-tax reforms, official restrictions limiting rural fees to 5 percent of local per-capita household net income were routinely ignored and additionally spawned exaggeration of local income levels by local officials. Tolls on roads and bridges, introduced to service financing for needed infrastructure projects, in many locations became inflated as general revenue sources and continued long after the infrastructure costs were recovered. While fees and tolls represent additional unavoidable consequences of modernization and the monetization of local life, their abuse as vehicles to enhance personal incomes for local officialdom underlies resentment and anger that come to the surface when a random event triggers social unrest.

**Real estate project “fundraising” (“jizi”).** Given the weak local tax base and central restrictions on local government borrowing, illegal but locally sanctioned fund-raising schemes have become commonplace over the two and a half decades since reforms began in earnest. Conducted in neighborhoods and urban workplaces, jizi involve local government’s often open approval for collections by developers and business leaders of funds from ordinary citizens in return for paper promising rates of return higher, at times unrealistically higher, than in local bank and credit cooperative accounts. In many parts of the country jizi have served the useful and even essential function of channeling local funds into popular and much-needed projects. But when jizi organizers fail to repay their creditors, especially where funds have been misappropriated, social unrest erupts. For example, jizi in Chongqing in the middle and latter 1990s lost lifetime savings for large numbers of ordinary citizens and sparked civil unrest.

**Land confiscation and asset stripping.** An essential part of modernization in any country is condemnation of land for public use or commercial assembly of land for an investment site through separate and often secret purchases of individual land parcels at market prices. Similarly, in virtually all countries in transition from planned and government-invested

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² The treatment of corruption here reflects in part views aired and discussed at an October 5, 2004 seminar at the Carnegie Endowment for International Peace in Washington, D.C., “From Socialism to Spoils: Corruption in Contemporary China” featuring Professor Yan Sun of CUNY at the time of publication of (Sun 2004).
systems, privatization of government-owned facilities is a desirable and generally necessary final step in enhancing corporate governance and productivity. Determining appropriate remuneration is a challenge in most countries, as is treatment of “holdouts”, and competitive bidding for government assets is a standard procedure. In many parts of both urban and rural China, however, collusion between local government officials and the construction and commercial companies seeking land results in little if any compensation for land taken, homes destroyed and livelihoods displaced. Similarly, rigged and uncompetitive sales of government property result in the widespread incidence of “sweetheart deals”, in many cases followed by layoffs or facility closings. Formal channels for complaints and petitions are swamped and inadequate. Social unrest frequently substitutes for lack of official recourse.

**Enterprise workplace abuse.** In the transition from cradle-to-grave benefits unrelated to productivity, the necessity of shifting to a productive job and then doing the work can be discomforting. Profit incentives and reasonable remuneration for labor productivity are at the heart of market reforms. But in China, collusion between local officials and business managers frequently results in failure to enforce laws and regulations governing workplace procedures, remuneration and safety. In some cases local officials themselves are abusers of workplace procedures for government employees, especially for rural teachers. Local officials frequently tolerate late payment of wages and salaries, and in many cases outright failure to pay. Similarly, exhausting work schedules and dangerous work conditions, especially in mines and on factory floors, are tolerated by local officials as a cost of economic success for their jurisdiction and hence their careers. Receipt of side payments is frequently reported, and efforts to redress grievances through official channels can end in arrest. Workers and households affected by such abuse find recourse in demonstrations and violent unrest.

**Sale of official positions.** In addition to promoting their own careers through collusion with local businesses, personal financial needs of local officials also play a prominent role in motivating corruption. Supplemental cash income needs are increased, however, because of the apparently widespread practice of selling official positions to the highest bidder (Sun 2004). Paying for one’s position requires recouping compensating amounts through leverage gained in the position, and hence sale of official positions serves to exacerbate the incidence of corrupt activity in all its forms.

**Inadequate government oversight mechanisms.** While most of what is known about local corruption comes through its investigation, prosecution and publicizing by official Chinese law-enforcement and auditing agencies, the structure of Chinese national and regional governance appears inadequate for the task of significantly reducing the impact of corruption in ways that worsen social unrest resulting from economic dislocations. Higher levels of government in China generally manage local affairs of interest to them through the relevant local official. There is no parallel, separately funded, presence at the local level. Higher levels of government resort to *ad hoc* investigations and procedures that give them temporary independent authority at the local level. This informational and operational distance from local affairs on the part of higher authorities serves to increase the disenfranchisement of local citizens from the rights and privileges guaranteed to them by law and proclamation. Without a more effective higher-authority presence to curb abuses of local civil authority, normal dislocations from reforms and modernization can transform them into social unrest.
Policy options

This memo is a presentation of the economic foundations for social unrest in contemporary China. A comprehensive set of suggestions for mitigating both economic stimuli and social unrest is beyond its current scope. Nevertheless, the foregoing analysis warrants several brief conclusions.

To the degree that social unrest rooted in economic causes reflects a combination of unavoidable reform dislocations and their exacerbation by local corruption, policy steps to reduce the level of social disruption needs to address both components.

The unavoidable social side effects of market reform and globally based modernization can be mitigated through appropriate choices for the design and implementation of those very reforms and modernizing procedures. Growth and job creation are essential, as is the better preparation of the labor force for its necessary improvements in productivity and remuneration through improved education, job training, regional mobility, and benefit portability. On-going reforms and investments in China’s educational system, social safety nets, transport and communications infrastructure and hukou (residence registration) barriers are all addressing this need.

Importantly, significant degrees of income inequality, by location, educational status, entrepreneurial initiative, and willingness to work, are also essential. Workers and their families need incentives to shift to new occupations, locations and work conditions voluntarily, and this can only succeed in an environment with appropriate patterns of significant inequality. In this regard, special attention should go to efforts to diversify farm and non-farm income opportunities for the rural workforce. Official emphasis on grain production, the least profitable farming activity, for reasons of custom or national security, deserves urgent review in light of persistent and crippling rural poverty and the increased official acknowledgment that China’s national security is already exposed to international commerce through fertilizer, energy and technology imports.

Separately, corruption deserves urgent treatment by enhancing both avenues for legitimate local activism, local oversight bodies, and independent local monitoring by higher levels of government. Other on-going reforms promise to help in this endeavor. The tax-to-fee reforms include a wide range of “companion reforms” (“peitao gaige”) which reduce the authority of local officials and modernize payment for such public services as teaching. Pending legislation, long delayed, establishing an administrative procedures law will, if passed, strengthen formal requirements on local officials in the conduct of their everyday business.

Full treatment of these and other policy-related topics broaches the whole range of issues related to China’s sustainable economic expansion and its promotion of institutions supporting civil society safeguards. Recognition that social unrest caused by economic factors is a normal dimension of reform and modernization, which is distorted and worsened as a reaction to corruption and malfeasance, provides a first-cut consideration of these problems.
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