



Institute for Contemporary  
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## Hukou Reforms at the Third Plenum: A Catalyst for Urbanization in China?



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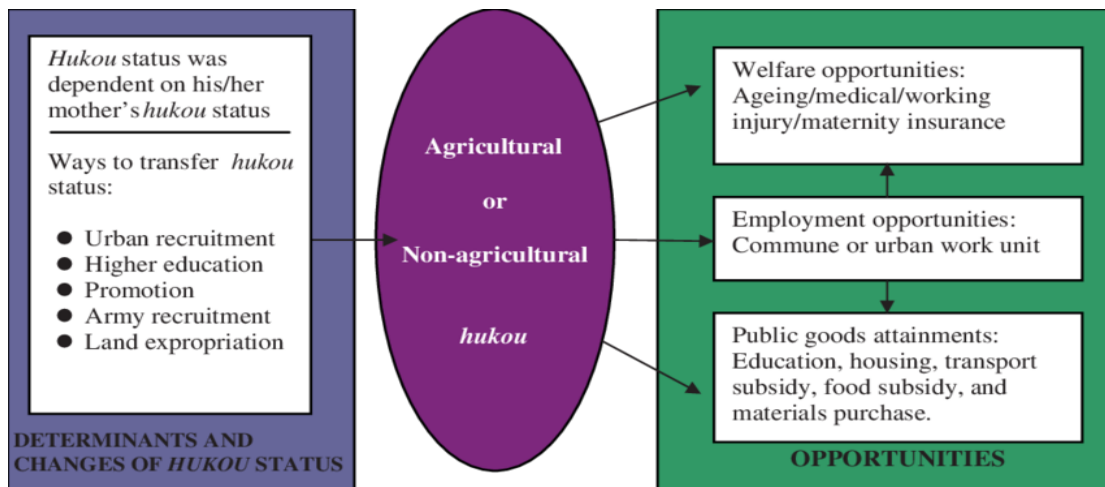
## 1.0 Introduction

After an unprecedented nine-month delay, the third plenary session of the 20th Communist Party of China (CPC) Central Committee was held in Beijing from July

15 to 18, 2024. The 22,000-word resolution document released post-session outlined several reforms, including modifications to the *Hukou* or Household Registration System. As China's economy transitions from industrialization to post-industrialization, more people are migrating from rural areas to cities. Consequently, the existing hukou management system struggles to handle the influx, particularly in major cities. Post-reforms, the Hukou system has been viewed as a challenge to China's economic development. Economists argue that maintaining the current form of the Hukou system hinders the development of a Chinese-style or Socialist market economy.

## 2.0 What is Hukou?

The household registration system, popularly known by its Mandarin name *Hukou*, system originated in ancient China to implement forms of population registration to manage resources, conscription, and taxation. The system as we know it today began to take shape during the Ming Dynasty (1368-1644). The Ming government introduced a more formalized household registration system to facilitate tax collection, military conscription, and social control. During the Qing dynasty (1644-1911) the Hukou system acted as Basis for social hierarchy and privileges. Population control and tax collection, and restricted migration within the empire. The modern *Hukou* system, which reached maturity in 1958, points out access to local social services like education, healthcare, and employment (see **Figure 1**). As we can see in the diagram there are both rural and urban *Hukous*. Initially *Hukou* served as an effective tool to curb mass internal migration during a time when China's economy was primarily agricultural and underdeveloped.



**Figure 1. Hukou**

### *The Upsides and Downsides*

Interestingly there are both upsides and downsides of the Hukou system in China

#### *The Upsides:*

1. Manages population distribution effectively
2. Allocates resources efficiently based on location
3. Encourages rural development in some cases.
4. Provides a basic social safety net
5. Offers valuable data for demographic studies.
6. Played its role in maintaining social order in China and prevented slums like other Chinese neighboring countries.

There are also those who see the Hukou system as preventing the Chinese-style modernization based on urbanization. It has often been described as the Chinese *Varna System*. These downsides are listed as below.

#### *The Downsides:*

- 1. Limited Labor Mobility.**
- 2. Inequality in Public Services**

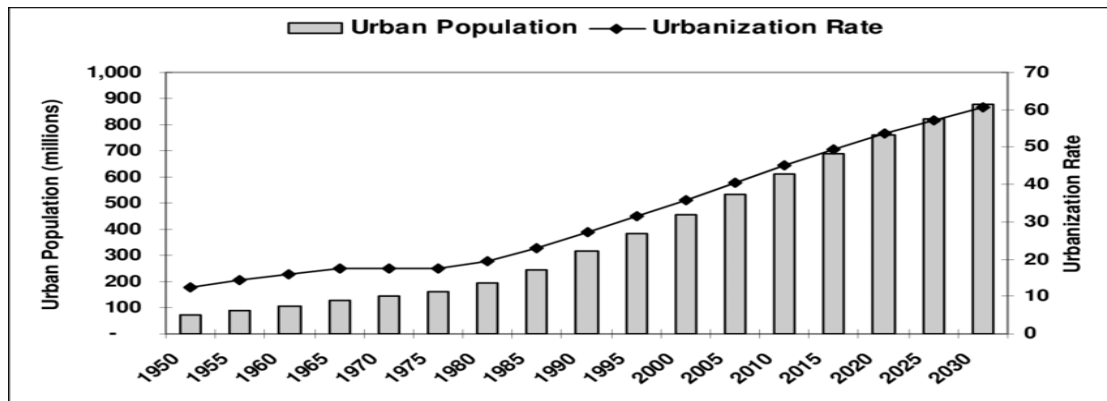


3. **Urban-Rural Income Gap.**
4. **Barriers to Entrepreneurship.**
5. **Educational Disparities:**
6. **Housing Market Distortions.**

### **3.0 Hukou Reforms outlined at the Third Plenum**

The Central Committee of the Communist Party of China has endorsed a plan to advance reforms and foster Chinese-style modernization. This decision, reviewed during the Third Plenary Session of the 20th Central Committee, aims to enhance the provision of basic public services based on permanent residence registration. It seeks to ensure that migrant children and eligible agricultural transfer populations receive the same social insurance, housing security, and compulsory education as registered residents. The goal is to accelerate the integration of agricultural transfer populations into urban citizenship.

The “Five-year Action Plan for Deeply Implementing the People-centered New Urbanization Strategy,” released by the State Council (or the Chinese Cabinet) on August 5th, outlines reforms for the household registration system over the next five years. According to Zheng Bai, the deputy head of the National Development and Reform Commission China's urbanization rate of permanent residents stood at 66.16 percent by the end of 2023, a marked rise from 53.1 percent by the end of 2012 (see **Figure 2.**). He added that a total of 165 million rural people became urban residents through the country's household registration system in the past decade. The plan aims to increase the urbanization rate of permanent residents to nearly 70 percent. It proposes removing settlement restrictions in cities with less than 3 million people, relaxing permanent residence restrictions in urban areas, improving conditions for settling in cities with 3 to 5 million people, and enhancing the point-based settlement policy for cities with more than 5 million people.



source: Statista

**Figure 2. Urbanization in China (1950-2030)**

The five-year plan is also notable for its focus on financial incentives, particularly linking fiscal transfers to urbanization rates. This approach motivates local governments to incorporate rural migrants by aligning their financial goals with national priorities, thereby tackling the historical funding shortages that have hindered previous reform efforts.

As per Shang Jiahua, an official of the Ministry of Human Resources and Social Security China still has nearly 300 million rural migrant workers in China and the Chinese government has adopted multiple measures recently to enhance their employment in cities and will continue with these efforts.

Outlining the specific measures to reform the hukou system the document of the Third Plenum said, “We will implement the systems for allowing people to obtain household registration and access basic public services in their place of permanent residence. We will push to see that eligible people who have moved to cities from rural areas enjoy the same rights as registered local residents with regard to social insurance, housing support, and access to compulsory education for their children living with them.” Some other important measures mentioned in the document include,

- Accelerate the process of granting permanent urban residency.



- Protect the lawful land rights and interests of former rural residents with permanent urban residency.
- Safeguard, as per law, their rights to:
  - Contract rural land
  - Use their rural residential land
  - Share in proceeds from rural collective undertakings
- Investigate ways to enable voluntary, paid transfers of these rights.

After listing these reforms it is very appropriate that we decode these reforms in terms of their impact on the Chinese economy

## **4.0 Decoding the Reforms**

For decoding these reforms let us first understand the economic reasoning of the Party-state behind these reforms.

### ***The Dual Challenges of the Chinese Economy and the latest Wave of Hukou Reforms***

Currently, China's economy faces the dual challenge of a slowing property market and changing demographics. China's economy, which previously thrived on rapid industrial growth and a booming real estate market, is now facing challenges due to an oversupply of unsold homes and decreasing demand. These problems are worsened by demographic shifts, including an aging population and a declining workforce, which threaten the viability of traditional economic growth strategies.

Economists widely agree that for China to rejuvenate its economy, it needs to shift from an investment-driven model to one that focuses on domestic consumption and the growth of the service sector. China's 14th Five Year Plan seeks to develop a complete domestic demand system. Here, domestic consumption is leveraged to drive the economy and purchase choices drive up innovation on personal and family items. Reforming the hukou system is considered crucial in this transition, as it could enhance labor mobility and increase consumer spending by fully integrating rural migrants into urban economies.



Another important element of the plan is its approach to rejuvenate the slow property market by encouraging rural migrants to buy homes. This twofold strategy aims to increase demand in the housing sector and provide migrants with a meaningful investment in urban living. In addition to tackling housing issues, the plan also broadens public services, offers more vocational training for migrants, and improves educational opportunities for their children.

It is also pointed out that increased urbanization, which goes hand in hand with the easing of Hukou restrictions, allows all urbanites to access social services and welfare which in turn aids this new consumer-driven economy as household capital is freed up. Furthermore, with increased consumer purchasing power, living standards are raised.

### ***The Hukou Reforms at the Third Plenum: A Breakdown***

It is important to note these reforms are to be implemented over a course of 5 years. This will prevent a mad rush to already large cities which could overburden their social services. There are some economists who argue that it will encourage even urbanization across China, creating new economic centers, preserve local culture and prevent "Londonization", where all resources get sucked into one metropolis. It also allows the central government to focus resources on smaller cities.

The issue up to now has been that urban migrants, lacking access to essential services, have tended to save for retirement and emergencies rather than spend. A 2020 study by Wen-Tai Hsu and Lin Ma from Singapore Management University suggests that this behavior would shift with a more liberal urbanization policy that ensures social services for everyone. The economists are also connecting the *Hukou* reforms with building a highly efficient socialist workforce. They argue that with the increased use of AI and robotics in the manufacturing process, the initial unskilled rural labor that drove China's opening up to the world will become increasingly redundant.



It is also argued that the primary aim of hukou reform is to enable the unrestricted movement of individuals and ensure that everyone can access basic public services regardless of their hukou status. Hukou should merely serve as a permanent residence registration system, with the associated rights and benefits gradually being minimized.

However, the Hukou reform plan has not gone unchallenged. It has its own share of challenges.

## **5.0 Challenges in effecting the proposed Reforms in Hukou**

Hukou is a very deeply entrenched social and economic system. Hence implementing these reforms even in the gradual manner faces significant hurdles. They are listed as follows,

1. Local governments, reliant on the system for population control and resource management, may resist change. Fears of overwhelming urban infrastructure with an influx of migrants could further hinder reform efforts.
2. Urban residents may perceive migrants as competition for jobs and resources, potentially leading to social unrest.
3. Financial incentives are key to successful hukou reform. Tying fiscal transfers to urbanization rates can motivate local governments. However, strict oversight is essential to prevent misuse of funds and ensure proper infrastructure development for new residents. This requires improved transparency and accountability in local governance.
4. The plan seeks to address property market oversupply by encouraging migrant home purchases. However, this policy-driven demand could worsen market distortions. Additionally, local governments may resist the plan due to financial constraints, as accommodating new residents requires substantial investments.
5. The reform faces social challenges. Historical inequalities and deep-rooted biases against migrants can fuel social tension. Incidents like the 2017 Beijing





fire underscore this issue. Mega-cities like Beijing and Shanghai are particularly resistant due to concerns over congestion and social stability.

6. China's declining birth rate and aging population pose demographic challenges. While urbanization can expand the labor pool, it's crucial to avoid exacerbating social inequalities.
7. Rural hukou, offering land rights and security, hinders urban hukou adoption. Deep-rooted land system issues further complicate the reform process.
8. A significant barrier to reform is the dual nature of rural hukou, which grants land rights and serves as a back-up option for many migrants. In a slowing economy, the security of having rural land to fall back on makes many migrants reluctant to fully commit to urban living by obtaining urban hukou. This reluctance reflects broader issues with the land system, which is itself in dire need of reform, a process that will likely take many years.

## 6.0 Conclusion

**The Chinese household registration system reforms unveiled at the Third Plenum are primarily intended to address** the dual challenges of a slowing property market and changing demographics. China's economy, once buoyed by rapid industrial expansion and a thriving real estate market, is now grappling with issues like an oversupply of unsold homes and declining demand. These challenges are compounded by demographic changes, such as an aging population and a shrinking workforce, which undermine traditional economic growth strategies. Economists broadly agree that to revitalize its economy, China must transition from an investment-driven model to one centered on domestic consumption and the expansion of the service sector. However, despite outlining the *Hukou* reforms at the Third Plenum one can observe a Deng-like precaution in these reforms. Deng Xiaoping did not immediately implement his reforms; instead, he adhered to a Chinese proverb that says, "crossing the river by feeling the stones" (*Mózhe shítou guò hé*). Similarly, new reform measures are following a two-step strategy. They aim at reducing *Hukou* restrictions for smaller cities first and then eventually scrapping restrictions for China's large urban centers.