

# Rising Regional Inequality in China

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China's rate of economic growth during the last quarter of a century has left many countries craving for a similar experience for their economies, and these countries have been trying to replicate the Chinese 'success' story. While there is much debate about the actual rate of growth China has witnessed ever since it went in for state-controlled and selective opening up of certain sectors of its economy, economists are unanimous in their opinion that the growth has not been insignificant in the sectors and regions that were opened to foreign participation. However, what is worrisome is the fact that this growth has been an extremely skewed one. There is growing imbalance between sectors, and both between and within regions. According to a study by Dali L. Yang and Houkai Wei[1], the average annual growth rates of GNP and industrial gross output value (GOV) in the inland regions of China have been always lower than those achieved in coastal China. Further, the study states that the difference between these growth rates have gradually increased since 1980. Gaps are also arising between the urban and rural populations in China.

**Table 1: Per Capita National Income Gap between Coastal and Inland Regions**

Year	Per Capita National Income (Yuan)		Regional Gap (c) (%)
	Coastal (a)	Inland (b)	$c = 100 \cdot (a-b)/a$
1952	118	85	28.0
1957	169	126	25.4
1965	213	165	22.5
1970	258	187	27.5
1975	325	211	35.1
1978	404	251	37.9
1980	497	310	37.6
1985	897	552	38.5
1988	1429	850	40.5
1990	1650	1016	38.4
1991	1858	1079	41.6
1992	2322	1268	45.4

Source: China Statistical Yearbook, various issues

1992 can be considered as the year in which China decided to speed up its process of economic reforms. Since then the regional gap has increased further. In 1998, the per capita GDP of Shanghai, the richest provincial unit, was twelve times that of Guizhou, the poorest province. In the year 2000 the gap between incomes in coastal and inland regions went up to 57.3 per cent.

Similarly, urban incomes are growing faster than rural incomes. The per capita disposable income of the urban Chinese rose from 5425 Yuan in 1998 to 7703 Yuan in 2002, a rise of almost 42 per cent in five years. Over the same period, rural disposable income per capita rose a meagre 14.5 per cent, from 2162 Yuan to 2476 Yuan. However, both these increases were in nominal terms. If one considers price increases in real terms over this period, per capita urban disposable income rose 13.4 per cent between 1998 and 2002, while rural per

capita disposable income rose a mere 4.8 per cent[2]. A survey conducted by the Institute of Economics of the Chinese Academy of Social Sciences, using data from 1988 and 1995, reveals that rural individuals make up most of those in the lower decile income groups, while in the higher decile groups, urban residents predominate. An important factor behind the faster growth of urban incomes in China in the post-reform period is income from property, which was made possible through commercialization and privatization of the erstwhile public housing system. While the property income of the urban Chinese accounted for a mere 0.49 per cent of total individual income in 1988, by 1995 the share had gone up to 1.3 per cent.

**Table 2: The Distribution of Urban and rural Individuals Across Decile Income Groups, 1988 and 1995 (percentage)**

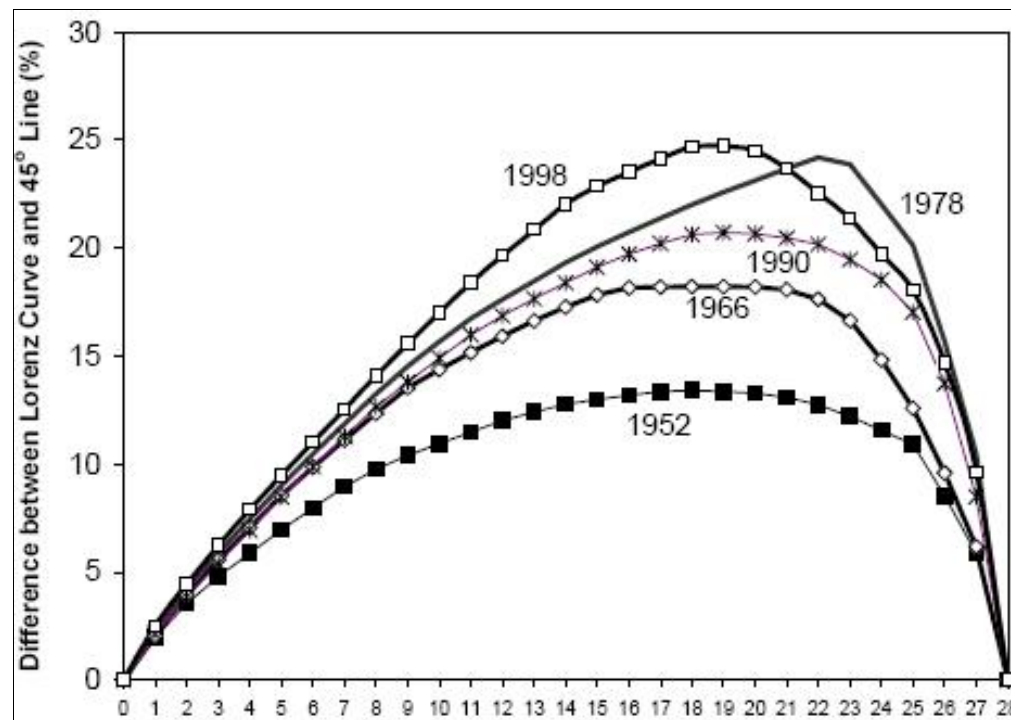
	<b>1988</b>	<b>1988</b>	<b>1995</b>	<b>1995</b>
Decile Group	Rural	Urban	Rural	Urban
Lowest	99.24	0.76	99.36	0.64
Second	97.94	2.06	97.41	1.59
Third	95.37	4.63	94.95	5.05
Fourth	89.30	10.70	90.36	9.64
Fifth	77.53	22.47	76.95	23.05
Sixth	56.71	43.29	55.53	44.47
Seventh	36.37	63.63	34.16	65.84
Eighth	24.87	75.13	23.10	76.90
Ninth	20.47	79.53	18.92	81.08
Highest	19.55	80.54	23.78	76.22

Note: 83179 individuals were covered in the sampling survey of 1988 and 56435 individuals were covered in the survey of 1995.

Source: Renwei, Zhao (2001): 'Increasing Income Inequality in China's Transition' in "China's Retreat from Equality: Income distribution and Economic Transition" edited by Carl Riskin, Zhao Renwei, and Li Shi, M.E. Sharpe, Inc.; New York

The gap between rural and urban incomes narrowed from 1978 all through the 1980s owing to the start of the rural reform period which saw the introduction of the household responsibility system and the simultaneous withering of the commune system. However, as we will observe later, the dismantling of communes increased inequality within rural China, even the urban–rural divide started rising again in the 1990s. This is evident from the Lorenz curve given below:

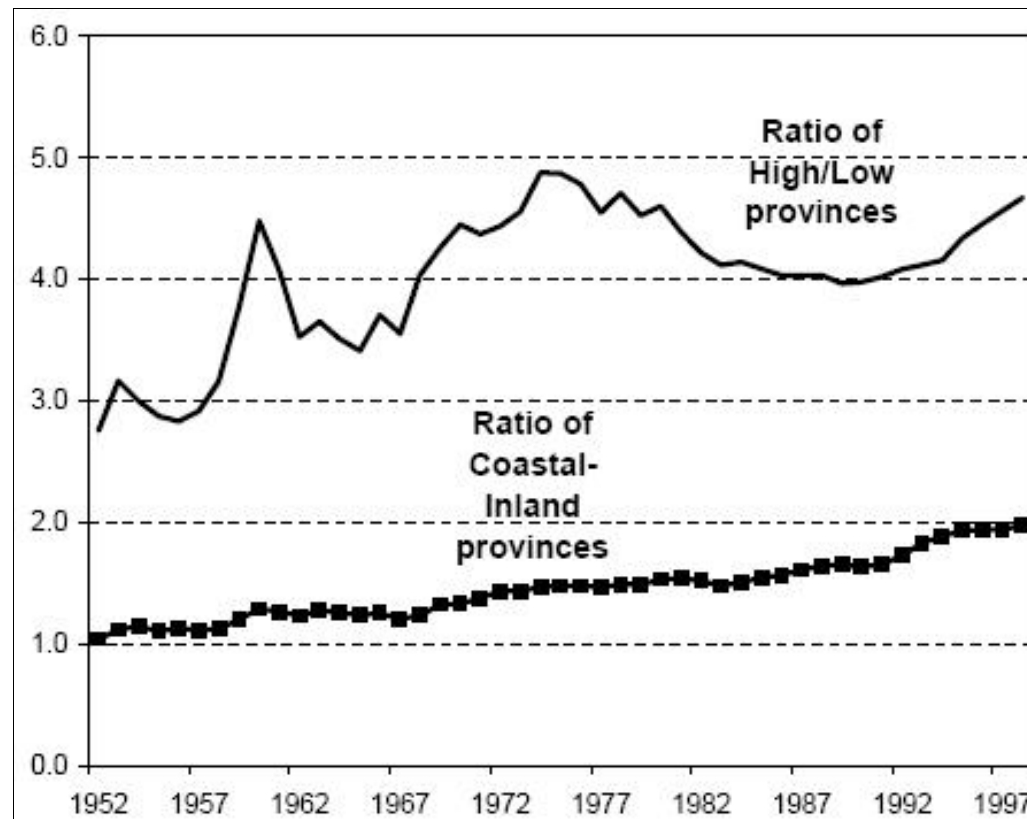
**Figure 1: Difference between the Lorenz curve and the 45° perfect-equality line**



Source: Can Wang (2003): China's GDP: Examining Provincial Disparity; Interim Report,  
International Institute for Applied Systems Analysis, Austria

Figure 2 gives the ratio of per capita GDP of provinces with the highest GDP to provinces having the lowest GDP per capita[3],and also the ratio of per capita GDP of coastal provinces to that of inland provinces. Both ratios witness more or less steady increases over the period under study, with the latter exhibiting a more secular rise. The ratio of per capita GDP of high-income and low-income provinces also exhibits a rising trend, but the ratio had fallen in intermittent years, particularly during the first half of the 1960s and between 1975 and 1990. The differentials of per capita income in rural and urban areas between 1978 and 1995 show an almost similar trend, but according to figures available in an article by Zhao Renwei[4],the urban–rural divide started rising again from the middle of the 1980s.

**Figure 2: The ratio of high/low and coastal/inland provincial GDP per capita**

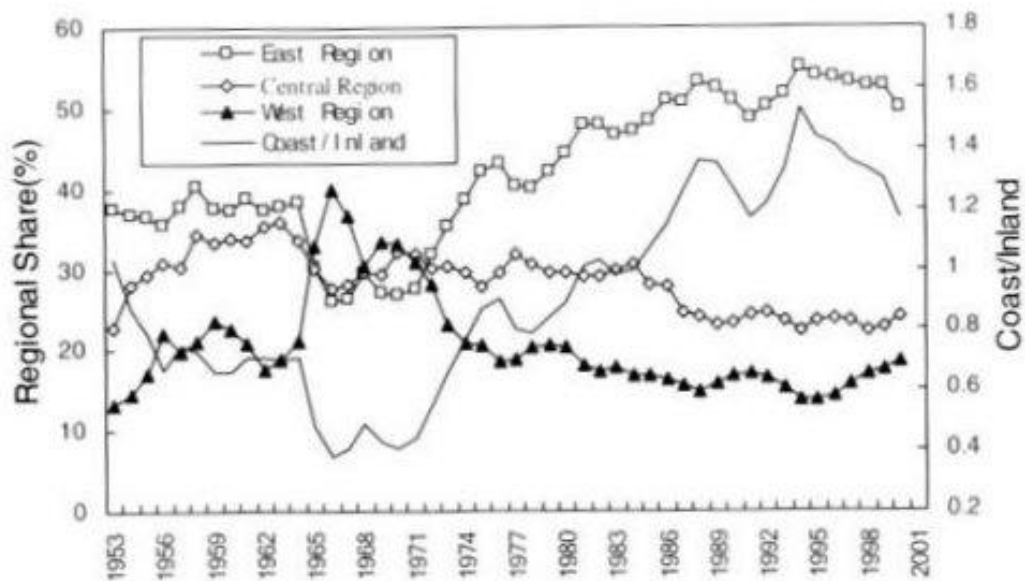


Source: Can Wang (2003): China's GDP: Examining Provincial Disparity; Interim Report, International Institute for Applied Systems Analysis, Austria

The main reason behind the increasing disparities between coastal and inland China, as well as between rural and urban China, is the coastal development policy pursued by the Chinese government. This has led to capital, both foreign and domestic, being invested mostly in the coastal regions of China, with the inland areas being starved of funds. As Figures 3-6[5] below reveal, almost all the investment that has come to China, particularly since the country went in for state-controlled liberalization, has gone to the eastern region. In 2001, 50 per cent of all FDI went to just three locations—Guangdong province, next to Hong Kong, the city of Shanghai, and its neighbour, Jiangsu province. Most of the rest of the money went to other locations up and down the coast. Inland, and indeed in some places along the coast, the flow was just a trickle. In 2001, Guizhou, China's poorest province and home to nearly 40 million people, attracted less than \$30million[6].

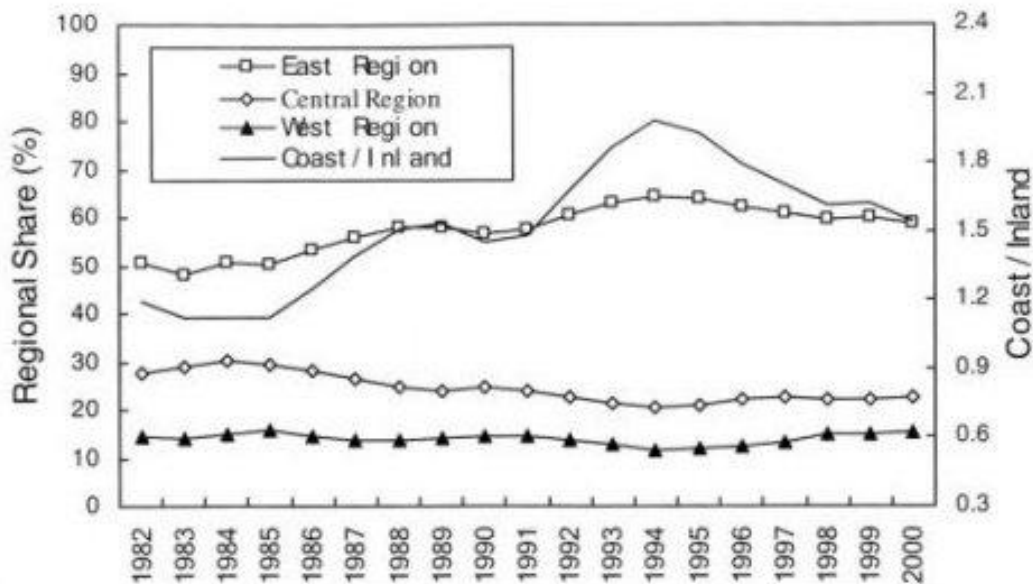
**Figure 3**

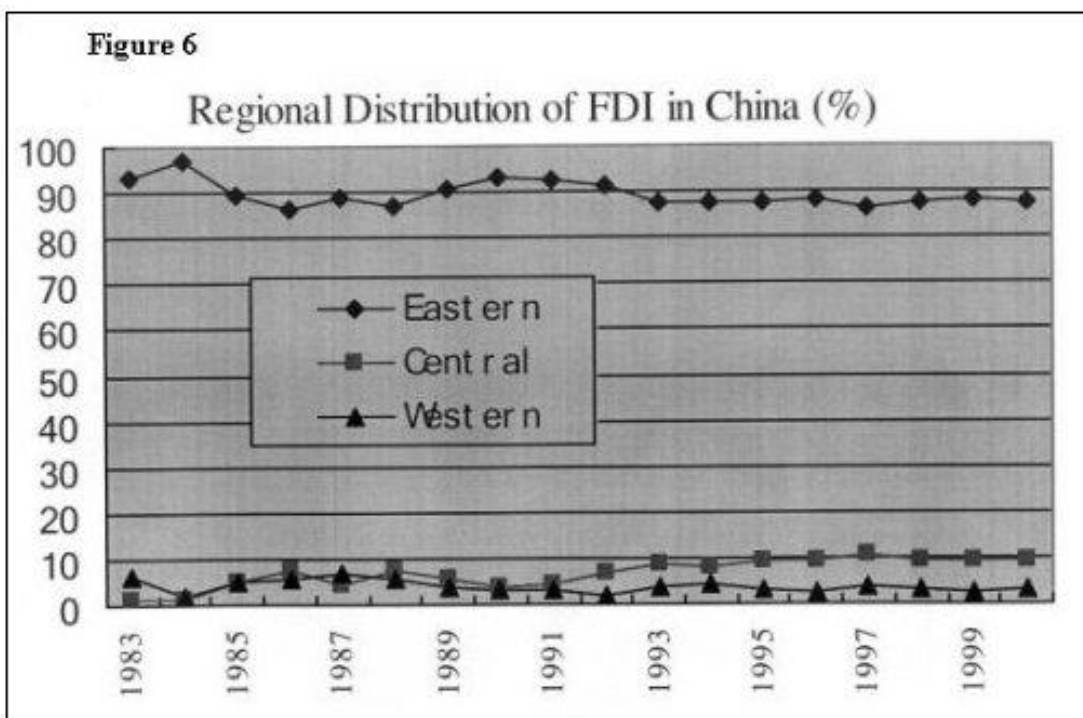
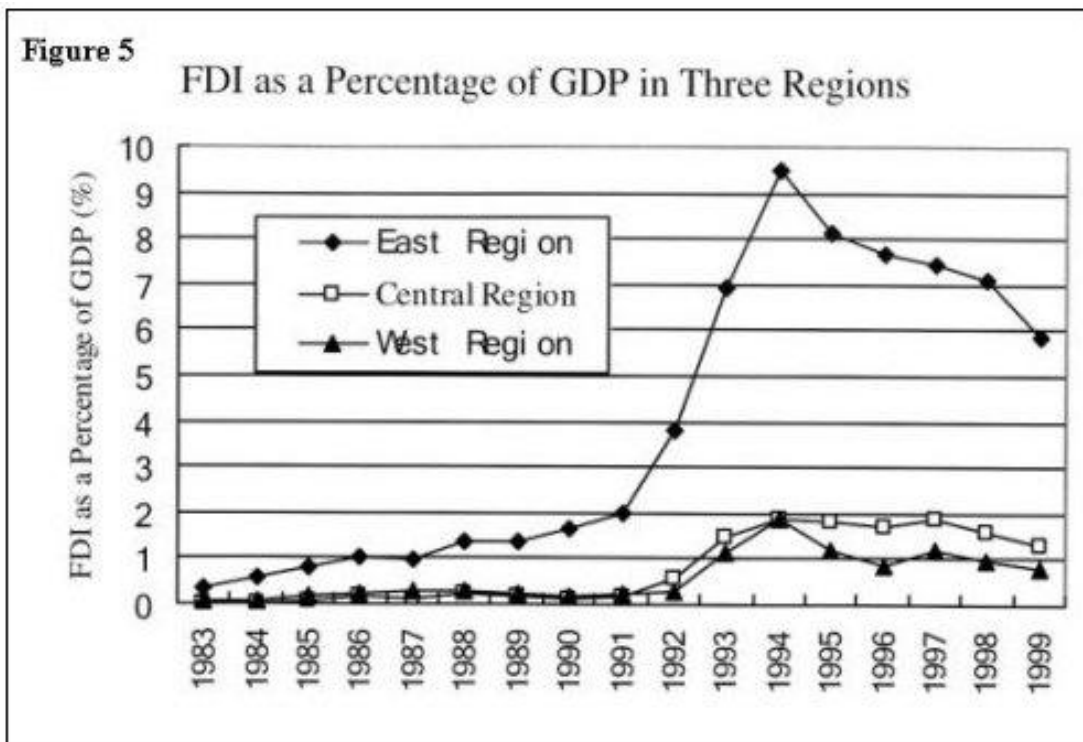
### Investment in Capital Construction Between Three Regions in China



**Figure 4**

### Total Investment in Fixed Assets in Three Regions of China





As a consequence, even the growth of peripheral and satellite industries and services that usually develop in the neighbouring areas of any industrial town or city, have been limited to the rural areas in the coastal region of the country. This is brought out by Table 3, which gives region-wise data for the value of exports achieved by rural enterprises in China. Within a span of eight years, the share of the eastern region went up from 82.8 per cent to 92.6 per cent, while that of the central and western regions fell from 14.6 per cent to 6.5 per cent and 2.6 per cent to a meagre 0.9 per cent, respectively.

**Table 3: Total Value of Export accomplished by Rural Enterprises in China (Amount in billion Yuan; Shares in percentage)**

		<b>National</b>	<b>East</b>	<b>Central</b>	<b>West</b>	<b>Central+West</b>
1985	Amount	3.90	3.23	0.57	0.10	0.67
	Share	100.0	82.8	14.6	2.6	17.1
1990	Amount	48.56	43.09	4.77	0.70	5.47
	Share	100.0	88.7	9.8	1.5	11.3
1991	Amount	66.99	59.78	6.26	0.96	7.22
	Share	100.0	89.2	9.4	1.4	10.8
1993	Amount	235.05	217.56	15.43	2.05	17.48
	Share	100.0	92.6	6.5	0.9	7.4

Source: Dali L. Yang and Houkai Wei (1995): Rural Enterprise Development and Regional Policy in China; Paper delivered at the Annual Meeting of the Association for Asian Studies, April 6-9, 1995; Washington D.C.

The majority of those among the Chinese people who belong to the minorities and the rural poor reside in the inland regions. An excessively wide regional gap could not only undermine social stability but also disrupt political stability and spur secessionist activities. In a bid to address the issue of growing inequalities in the country, the Chinese government seems to have taken steps to bridge the spiralling gap between the coastal and inland regions of China, as well as that between urban and rural areas. The government's assessment was that the widening gap was a result of the decline in the performance of rural enterprises in coastal and inland China, and at the 5th Conference of the 7th National People's Congress held in March 1992, it decided to 'support vigorously' the development of rural enterprises in the central and western regions of China. In that year the People's Bank of China offered an additional 2 billion Yuan worth of bank loan ration and 3 billion Yuan worth of rural credit cooperative loan ration on the basis of original credit planning, with a view to supporting rural enterprises in central and western China. This additional amount was to be provided annually for a period of eight years, from 1993 to 2000. Another annual special loan worth 5 billion Yuan for the years 1994–2000 was pledged by the State Council in September 1993, to support rural enterprises in these regions. The Agricultural Bank of China also set up a 100 million Yuan special discount loan facility from the last quarter of 1992 to cater to rural enterprises in minority-nationality regions in the country. These regions included Guangxi, Ningxia, Xinjiang and Inner Mongolia Autonomous Region, and the provinces of Yunnan, Guizhou and Qinghai. Besides, the Chinese government also announced certain tax exemptions (which included a three-year exemption from income tax for all newly established rural enterprises in certain areas) for rural enterprises in central and western China.

That the efforts of the Chinese government to boost investment in the backward regions has yielded results can be observed from Figures 3 and 4, which reveal that the coast to inland ratios of investment in capital construction and total investment in fixed assets have come down in recent years. Also, local governments of the coastal region have, of late, been encouraging and laying stress on supporting rural enterprises of underdeveloped regions, as rural enterprises in the coastal region are suffering from diseconomies caused by overconcentration and the existence of an inter-regional dual structure. The development of rural enterprises in inland China is further expected to curb the constant migration, both legal and illegal, of labourers from these regions to coastal China in search of a livelihood, thereby easing the pressure on the infrastructure of the coastal region.

However, despite the proclaimed efforts of the Chinese government to spur economic activities, growth and development in inland China, things did not turn out as expected for the central and western regions. Rather than helping the inland regions, the government's policies seem to have helped the developed coastal regions through the supply of cheap labour and raw material from inland China. The policy initiated by the Ministry of Agriculture's Department of Rural Enterprises in China, avowedly to promote mutual economic benefit and common prosperity, in essence has meant that while coastal China will witness the development of high and new technology-based industries and the growth of an export-led economy, the emphasis in inland China will rest on a strategy of resource exploitation. Faced with a rapid rise in wages in coastal China (the wages in eastern China being about 1.5 times higher than in inland regions), the developed coastal areas of China will constantly try to transfer only low-grade labour-intensive production processes to central and western China while trying to replace labour with capital in the medium to long run.

Heavy exploitation of the mineral resources of inland China alongside a booming raw and processed material industry will soon lead to environmental degradation and resource depletion of the region, resulting in long-term calamity. Further, as one must be aware, the terms of trade have historically moved against primary commodities, and there is no reason to believe that for exports of inland China, the trend would be defied.

Projects like the Three Gorges Dam and river interlinking, despite being criticized for disrupting the ecological balance, flooding some of the most fertile lands in the country and causing environmental degradation, are expected to reduce inequalities. In the initial stages such projects are expected to create employment in huge numbers, thereby increasing the income and purchasing power of the people in the provinces in which they are implemented. However, it is in these same regions that such projects displace large sections of the population. Not only do many of them fail to be adequately resettled, even those who are resettled find it difficult to earn a livelihood. Being resettled in a place where the skills of the migrants might not even be in demand, these people, particularly the older ones among them, may find themselves without any purchasing capacity.

Resettlement policies in China have so far benefited the rich among those displaced more than they have helped the poor. With rural property costing less than urban homes, migrants who have been displaced from rural areas get much less compensation in comparison to those displaced from urban homes. As a result, rural migrants are often forced to borrow money from relatives and friends to build new houses—and so start their new lives with a mountain of debt. Rural migrants are also more likely to be forced to move farther away than urban migrants, as well as face daunting economic and social challenges in adapting to an unfamiliar environment [7].

While the experts who were a part of the official feasibility study team for the Three Gorges Dam have claimed that those who were displaced because of this project will all be resettled in the reservoir area, and that 40 per cent of the rural migrants could be redeployed in non-farming jobs, researchers from the Chinese Academy of Sciences have said that the lives of these migrants will not necessarily be better or even the same even if the 'local resettlement' target is met. The researchers tracked a small number of rural migrants in the Wuqiao district of Wanxian city, and found that most of them were significantly less well off than they had previously been. Both newcomers and existing residents had only half as much land as they did before resettlement. The amount of farmland available per person also had declined dramatically after the influx of migrants, and the resettlement site failed to provide new work for individuals squeezed off the land. Almost all the households monitored in the study had suffered increased unemployment and a sharp decline in



income. Since most of the land available for relocation under the Three Gorges project was barren and unsuitable for cultivation, many of those displaced were reluctant to move to such inhospitable conditions.

Even though the official experts had pledged that everybody displaced by the Three Gorges project would be rehabilitated within the reservoir area, the actual has relocation belied their promises. Soil erosion has become a serious problem in the Three Gorges area with the expansion of farmland and construction of hundreds of new settlements. To relieve the pressure on a fragile ecosystem, in 1999, Premier Zhu Rongji announced a policy shift in favour of moving migrants to distant parts of the country. This decision to move 125,000 migrants far from their homes was not part of the original resettlement plan. Many of the migrants found it difficult to cope in their new, unfamiliar physical and social environments, and with conflicts with 'host communities'. Migrants to distant areas found that they could not speak the local dialects and faced tremendous problems in communicating. In March 2002, thousands of rural migrants who had been moved under Zhu Rongji's policy to Badong county in Hubei province, complained about substandard resettlement conditions and asked to be relocated. To maintain social stability, they were moved again. However, such additional relocation has only led to a further rise in the costs of the project.

Most of the soft loans that the Chinese government and banks had pledged for rural enterprises in inland China in the early 1990s have not been forthcoming. With the banking system in China also undergoing reforms, more emphasis is being placed on the profitability of the projects and not on issues like employment generation and reduction of inequality. The People's Bank of China had initially pledged an annual loan of 5 billion Yuan at low rates of interest to support rural enterprises in central and western China, but later the bank decided that it would provide the loan purely on a commercial basis. Even then a major part of the promised funds were not made available, and loans provided by the agricultural banks for rural enterprises in inland China were on the decline. Agricultural banks and credit cooperatives still account for almost three-fourths of the rural enterprise loans in the eastern region of China.

Finally, even the tax benefits initially on offer for those setting up new enterprises in rural areas in the central and western regions of the country were mostly withdrawn under the new tax policies that are being implemented in China. About four-fifths of the taxes paid by rural enterprises go to the central government, and as such, local governments cannot support the development of rural enterprises in those regions through preferential tax policies. Although the new tax regime has exempted all items of export from value-added tax and consumer tax, the western and the central regions hardly benefit from such largesse as less than 10 per cent of the exports of rural enterprises come from enterprises located in these regions.

The Chinese government has recently woken up to the necessity of addressing the concerns of the nation's backward provinces. The Tenth Five-Year Plan (2001–2005) in China has the narrowing of regional inequalities as one of its principal objectives. It pushes for sustainable development—with increased productivity in agriculture and in industrial state-owned enterprises (SOEs). The Plan also intends to create jobs by promoting labour-intensive activities, including services, and developing collective, private and individual businesses. The Plan hopes to create 40 million new urban jobs, and to safeguard the natural resource base. Rural reforms, as outlined in the Plan, aim at accelerating agricultural diversification and raising incomes. The new National Poverty Reduction Plan for 2001–2010 adopts a more comprehensive approach with better targeting of the deprived population in the backward provinces of western China. The Tenth Plan also calls for 'coordinating economic and social development'—by paying greater attention to quality-of-life issues, including investing in

human capital (e.g., anti-poverty measures, better education), protecting natural capital (e.g., by enhanced ecological conservation and environmental protection), and improving social protection (e.g., by strengthening the social security system). In particular, China's Tenth Plan outlines the need for developing the country's economically and socially lagging western and central provinces—by fostering economic development zones through investments in strategic physical infrastructure for transport, water resources management, energy and mining, accelerating other development objectives as cited above, and introducing advanced technologies to upgrade local industries and increase competitiveness.

It is essential that the competitiveness of China's backward regions improves, not only in primary commodities and as providers of raw materials for the country's industrial belt, but also in manufactured and finished products. Regional inequality in China is bound to keep widening as long as thrust of the policy of the Chinese government remains development of inland China as a feeder and provider for the country's coastal region. Investments need to be made in central and western China not only in the resource exploitation and processing industries, to cater to the demand of the export-oriented eastern region, but also in sectors from where ready-to-export-products can be manufactured, ridding the economy of inland China of its dependence on how China's coastal economy performs. Also, the government has to monitor the flow of resources into the backward regions so that agriculture does not get neglected and sufficient investment flows into the agricultural sector. Food security of the people of inland China cannot be compromised in the pursuit of industrial growth.

[1] Dali L. Yang and Houkai Wei (1995): *Rural Enterprise Development and Regional Policy in China*; Paper delivered at the Annual Meeting of the Association for Asian Studies, April 6-9, 1995; Washington D.C.

[2] [http://www.friedlnet.com/images/free\\_chinese\\_statistical\\_communique\\_2002.pdf](http://www.friedlnet.com/images/free_chinese_statistical_communique_2002.pdf)

[3] Ratio of high/low GDP per capita: The ratio of high/low GDP per capita (hereafter denoted as RHL) is defined as the ratio of the top per capita GDP to the lowest per capita GDP among the provinces. In order to avoid some special causes of disparity, such as a too small area and/or sparse population in a certain province, the RHL in this study is expressed by using the ratio of the arithmetic mean value of per capita GDP of the top five provinces to that of the bottom five provinces.

[4] Renwei, Zhao (2001): 'Increasing Income Inequality in China's Transition' in "China's Retreat from Equality: Income distribution and Economic Transition" edited by Carl Riskin, Zhao Renwei, and Li Shi, M.E. Sharpe, Inc.; New York.

[5] Source of Figures 3-6: Houkai, Wei: *China's Regional Disparities and Regional Policies*; Institute of Industrial Economics; Chinese Academy of Social Sciences

[6] <http://www.globalpolicy.org/socecon/ffd/2003/0119chinafdi.htm>

[7] <http://www.threegorgesprobe.org/tgp/index.cfm?DSP=content&ContentID=7008>