Urban-Rural Disparity in Post-reform China

Prepared for China Rural Development Center

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Phenomenon (1)

Average Living Expenditure in Rural and Urban China: 1978-99
(Unit: RMB)

Phenomenon (2)

Urban-Rural Consumption Ratio (1978-1999)

Outline

- Theoretical Framework
- Pre-reform Urban-Rural Institutional Arrangement
- Urban-Rural Disparity in the Post-reform Period
- Policy Implications
Theoretical Framework: Two-sector Economic Development

- Lewis Model (1954)
  - Unlimited supply of labor from rural area
  - Labors are unskilled and of equal quality
  - Free migration and labor market
  - “Marginal productivity law” principle

- Harris and Todaro Model (1970)
  - Unemployment in urban sector

- Knight Model (1999)
  - “Average productivity law” principle in rural China
Theoretical Framework: the Urban Bias Model

Lewis Model

Harris-Todaro Model

Rural supply

Urban demand

W_u

W_c

Urban Unemployment

Rural labor force

Urban employment

Total Labor force
Theoretical Framework: Equilibrium Outcomes in the Model

- Improvement in terms of rural-urban trade
- Inter-sectoral transfer of labor
- Eventual improvement of inter-sectoral equality in labor income
Pre-reform Urban-Rural Disparity: “Urban Bias” Policy (1)

- Inter-sectoral trade
  - Scissors Price: Distorted price structure in favor of the urban sector

- Inter-sectoral capital transfer
  - Exploiting the agriculture sector to accelerate industrialization

- Urban labor market
  - Above-equilibrium urban wage
  - Surplus jobs in the state sector
    - Overstaffing and underemployment
Pre-reform Urban-Rural Disparity: “Urban Bias” Policy (2)

- Rural labor market
  - Equal land sharing policy in rural sector
  - Rural labor income is based on average productivity
    - Violation of marginal principle
  - Sharing disguised unemployment as underemployment among the rural labor force

- Inter-sectoral labor transfer
  - Strict restrictions on rural-urban migration
    - Household registration system (hukou)
Post-reform Convergence (1978-1985): Golden Age for Rural China

- Land contract system reform in rural area ignited the shocking increase in rural productivity

- Price reform in favor of the agriculture goods
  - Sharp increase in the procurement price

- Rural industrialization
  - Start-up of township and village enterprises
Three Sectors' Share of GDP in China (1978-1998)
Post-reform Widening Disparity (after 1985):

- Restrictions on rural-urban migration
- No integrated national labor market
  - Discrimination on rural migrants in urban areas
- Private sector development in urban area
  - Compete with TVEs for capital, market, etc.
Post-reform Widening Disparity (after 1985):

- Supply of rural surplus labor is below the market equilibrium level
  - Rural labor supply (to urban) is based on average productivity, rather than marginal productivity
  - Peasants are not entitled with land alienation rights

- The urban wage is set above market equilibrium level

- Education disparity
  - Urban and rural labors are of different quality
Rural-Urban Disparity in Education: Years of Schooling

### Rural-Urban Disparity in Education: Educational Attainment

<table>
<thead>
<tr>
<th>Level of Education</th>
<th>Urban (%)</th>
<th>Rural (%)</th>
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</thead>
<tbody>
<tr>
<td>Below Primary</td>
<td>5.9%</td>
<td>28.8%</td>
</tr>
<tr>
<td>Primary</td>
<td>13.5%</td>
<td>32.5%</td>
</tr>
<tr>
<td>Lower-secondary</td>
<td>36.5%</td>
<td>29.8%</td>
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<tr>
<td>Upper-secondary</td>
<td>22.5%</td>
<td>7.5%</td>
</tr>
<tr>
<td>Technical institute</td>
<td>16.0%</td>
<td>0.9%</td>
</tr>
<tr>
<td>College or above</td>
<td>11.7%</td>
<td>0.5%</td>
</tr>
</tbody>
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Rural-Urban Disparity in Education: Dualistic Financing System

- Decentralized education funding system
- Dualistic system on education financing
Policy Implications:

- Further relax household registration system
- Centralize the education funding system to provide rural residents equal education opportunity
- Entitle rural residents the interim land alienation right
- Remove discrimination on providing education, health, social security, and housing to rural migrants
- Remove the current expatriation policy in large cities
Selected References


