

# The Emperor Has No Clothes: Inequality of Wealth in Modern China

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The success of China's economic reforms have been widely dissected by both economists and politicians alike, who having spent the decade watching the Chinese Communist Party's (CCP) move to a market-oriented society, are now trying to figure out what went right. Right now, as a result of intense concentration on its exports and manufacturing, China is currently the world's largest developing economy, ranking sixth in world trade and exhibiting levels of trade comparable to that of the United Kingdom and Japan. Each factory that opens, whether from foreign investment or through privatization, means the creation of that many more jobs, as well as gains to an already vaunted GDP, which grows at an average rate of 7 to 8 percent annually. Yet, has this prosperous flood benefited the Chinese citizenry equally-or in the case of some, wrought any change in their standard of living at all? One thing is certain: notions of egalitarian rhetoric and brotherhood have been lost to free market "shock therapy" in a bid to retain legitimacy in a world inching toward more representative and capitalistic forms of governance. With the situation in China resembling that across East Asia--specialization in low-end manufacturing and like-wise low-end wages that are still better than the prior equivalent--poverty and inequality across the mainland have become significant to the debate over trade liberalization. Are organizations like the World Trade Organization, a body representative of the world's wealthier nations, actually promoting free trade in the charitable interest of the world's population, or is the end result something much more worldly? The comparative advantages of cheap labor is likely the most realistic escape for the Chinese worker, yet reforms that continue to encourage disproportionate growth could face strong opposition in the future if they are continually seen as coming at too great a cost to the poor. This is something Hu Jintao, the successor to former prime minister Jiang Zemin, will have to remember as he faces the daunting prospect of bringing China to speed with the rest of the world.

## **A Convalescing Superpower**

Though China's growth in the last quarter century is enviable by any measure, it's still considered catch-up to the rest of the modern world. Communal agricultural policies been abrogated, resulting in the migration of rural labor to special economic zones on the coast and in the south, where privatization has been encouraged by an historic reform agenda. Spurring foreign direct investment and Chinese entrepreneurs, the changes have rescued approximately 160 million people from absolute poverty and singularly boosted per capita net incomes (Kurnaltzick, 2002:42), increasing over 1000 percent from 1978 to

1995. Yet, it is increasingly clear that because the economy has grown so enormously—an annual average of seven percent GDP growth in the last decade—indicates that this type of behavior is unsustainable in the long run. This gradual but perceptible decline in robust growth predicts something else as well; the Chinese are running through the simplest changes available to them.

China's transitional period underlies an alarming rise in inequality as well. It's this growing discord in the allocation of wealth gained from modernization that belies the benefits of a rising incomes throughout the citizenry. Among urban households, where the majority of the new wealth is located, the richest 20 percent garnish 42 percent of total urban incomes, whereas the poorest receive only 6.5 percent (Economist, 2001:5). Such uneven holdings distort prosperity indicators like the average net income and indicate that perhaps the spoils of the new economy have not been dispersed as fairly as was once believed.

The poverty in the urban sectors is apparent to anyone who visits. On the roads, luxury cars share the road with dilapidated motorcycles carrying sometimes entire families; it is impossible to go for long through the city without encountering neighborhood slums in various states of decay. Alongside the nouveau riche, there has been an expansion in the ranks of the urban poor: an estimated 12-20 million now (Qian and Wong, 2000:114). With the finalization of China's membership in the WTO, the situation of those residing under the poverty line looks to be further exacerbated by policies designed to reduce rampant protectionism, which has played a role in maintaining the vulnerable agriculture and state-owned sectors.

It is true that something needed to be done to correct the years of decay incurred from under Communist rule, and that moreover free markets can win over many of its detractors by simply pointing to the historical record. Does the modernization of markets preached by westerners really benefit everyone, as some economists presume? Econometrics responds with a qualified "yes," but manipulate variables and the results turn inconclusive (Economist, 2002:3). The reasons for disparity in China need to be understood and delineated if one wants to land rationally on either side of the globalization debate. If displacement from increased exposure is, in economic terms, ephemeral, may we not expect an eventual decline in world poverty as well as convergence between the world's rich and poor. On the other hand, if the outcome is merely the assuagement of absolute poverty, and to the reward of a relatively few individuals, could we not witness a rise in disastrous social upheaval, as is occurring now among those in China marginalized by the new economy.

### **China's Widening Income Inequality**

When inequalities in income are compared one of the devices used is the Gini coefficient, which measures income distribution along a scale from zero to one: zero representing perfect equality and one symbolizing a society in which one person receives all the wealth. In 1999, China's Gini coefficient was officially stated as .39, a number dangerously close to what then Prime Minister Zhu Rongji considered the

“internationally recognized danger level.”<sup>1</sup> Moreover, many believe this estimate to be an understatement of a more grievous situation. One scholar, He Qinglian, author of “China’s Pitfall,” believes that a more accurate picture would place the number closer to .6, citing the failure in the official assessments to account for substantial illegal and undeclared incomes, which naturally accrue to the more affluent. If He is correct, then China’s income distribution is one of the most disproportionate in the world (Economist, 2001:5).

The analysis captures striking discrepancies among rural and urban populations as well; here inequality appears to have risen in step with the more extreme second stages of Deng’s incremental reforms. Gustafuson and Li report that Gini coefficients of household incomes for urban areas in 11 provinces increased from .228 in 1988 to .276 in 1995.<sup>2</sup> From similar data, Khan and Riskin find an increase from .233 to .332 over the same period (Meng, 2002:5). Rural equality fared no better—rising to .34 in 1999, as the increasing favoritism towards the cities for such things as health care, housing, and education further skewed the quality of life between urban and rural regions.

Disparity of this type has not always been a problem for the Chinese. In fact, before the advent of radical factor market reform, inequality remained at fairly moderate levels, though admittedly, ordinary life was harsh and opportunities for advancement were remote. Income ratios comparing the top 10% of urban households to the poorest 10 percent increased only gradually from 259 percent to 295 percent across a ten-year period, from 1981 to 1991 (Meng, 2002:5). Prior to the second stages of reform, modifications were tailored mostly to the product markets; labor markets, wage structure and state employment were left largely untouched and displacement and the loss of jobs were incidental. Then as mobility restrictions were gradually eased, the supply of labor in urban areas skyrocketed, as rural Chinese attempted to capture the marginally better lifestyle offered by cities and their burgeoning private industry. Even as private business and manufacturing saw their demands grow, the unceasing migratory flow of workers exuded immense downward pressure on wages and created the current stagnation of today. Data from Xin Meng’s paper on income inequality states that income ratios of the top and bottom rungs of society began to separate conspicuously in the past decade, from 378 percent in 1995 to 459 percent in 1999, as the numbers of unsupportable unskilled and under-unemployed urban Chinese continued to expand, arriving at time when wages have so far exhibited little **vibrancy**. Furthermore, compensation for unskilled labor has not markedly risen in the past ten years.

There is more than one reason for inequality is rising in China, among the Chinese as a whole as well as inter-provincially and between urban and rural regions. In the cities, the employees of monopolistic industries such as banking, telecommunications,

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<sup>1</sup> A measure above .4 is viewed by many in the Chinese government as a warning against future instability arising from aggregate dissatisfaction with the allocation of resources.

<sup>2</sup> Gini coefficient can also be measured on a scale from zero to one hundred. This is the actual method used by Gustafuson and Li (1997), Khan and Riskin (2000).

and petroleum enjoy higher wages, and through the benefit of state-control, secure long-term employment and job security. An aggressive fiscal stimulus designed to ameliorate ailing domestic demand has increased average wages for skilled workers in such industries as health care, education and the governmental bureaucracies. In stark contrast, however, are the traditional manufacturing industries, where wages stagnate, and the agricultural sector, which can only provide workers with a relatively low return due to their marginal productivity. With the removal of agricultural export subsidies looming, Chinese farmers look to face more falling incomes in the future.

Recent times have witnessed a growing demand for the lavishly compensated, urban technocrats of a private sector strengthened by the erasure of barriers to foreign and private investment. Many privately-owned businesses have been resoundingly successful and their sung praises have comprised a good deal of what has been dubbed, "the Chinese miracle." In 1993, there were some 510,000 private enterprises employing 3.2 million workers, most of whom received higher wages than their counterparts under state employment. Foreign owned enterprises (FOE) routinely offered choice compensation as well, sometimes by as much as 1.6 times on average (Qian and Wong, 2000:115). But as Stephen F. Diamond writes in his review of the Chinese markets, "the new so-called private sector has no where near the resources to take on the huge industrial needs of Chinese society." He elaborates by saying that the revenues of the largest private entity in China equal only half the turnover of the lowest-ranked company on the Fortune 1000 list. Chinese workers employed by private industry represent only a small fraction of the nation's 1.3 billion people and are the exception rather than the rule.

One major tale of the economic progress in rural China was the ascension of the town and village enterprise (TVE); though, in recent times these small privately owned enterprises have lost a lot of their previous luster. TVE's were successful in creating a locus of low-paying manufacturing jobs available to rural Chinese, but simultaneously gave birth to a wealthy-managerial class whose incomes further increased the disparity in China's provincial regions. Furthermore, the provinces grew at vastly different rates to each other throughout the eighties and nineties, with the majority of the progress focused in the southeastern coastal regions. Analysis shows that the incongruity is primarily the result of uneven dispersal and success of the TVE's by province rather than any discrepancy in agricultural bounty. Ratios of per capita incomes for the richest and poorest provinces were 4.5 in total incomes, but only 2 in agricultural incomes. Ratios of TVE's incomes, on the other hand, were more egregious: 13.4 (Shuijie and Liwei Zhu, 1998:5-7). Expectedly, there is much bitterness and enmity over these inter-regional inequalities, particularly amongst the western and central regions towards the better off south.

### **Urban Unemployment in China**

As reforms continue to crystallize with China's membership in the WTO, widespread unemployment that the organization's policies have caused before could have a dangerous destabilizing effect on the society. Already, millions of state employees have lost their jobs from structural adjustments implemented to boost productivity in the

hopelessly inefficient state sector. Redundancy in state employees, leftovers from full employment initiatives of the Maoist era, is now a burden on efficiency and profits of such monolithic state-owned industries as petroleum and automobile manufacturing. When PetroChina Company went public in 2000, it required the layoffs of hundreds of thousands of employees in order to achieve credibility on foreign capital markets; subsequently, protests occurred in the Daqing oilfields of northwest China as hundreds of laid-off workers protested against the meager severance packages they received at the hands of PetroChina (Diamond, 2002:95). Protests like these, and others as far away as Beijing itself, punctuate fears to the current regime of the waves that could result from the abandonment of those low unemployment-friendly practices of the past known by the Chinese as the “iron rice bowl.”

Transition to a market economy has played havoc on state-owned businesses in another way. Previously an economy of shortages, China’s state-owned enterprises were guaranteed markets for their products. Now, in direct competition with the private sector, state-owned businesses must compete alongside more efficient private firms by producing at lower costs and with more attention to quality. The type of production that was feasible and necessary to sustain full employment in the past is now leaving many firms with no other option but to initiate widespread layoffs of their employees, many of whom before considered encroachments on their job security a remote possibility.

Workers retrenched from the state contributed only subtly to increases in official unemployment figures: 2.9 percent in 1995 to 3.1 percent in 1999; yet, these erroneous numbers fail to include the majority of workers eliminated. Other estimates of unemployment propose that close to 15 million state employees lost their jobs in 2000 and as many as 27 million in 2001. Data from 1995 and 1997 show that the urban unemployment rate defined to include employees purged from the state sector rose from 8 percent during this period upward to 17 percent (Meng, 2002:6). By 1997, retrenched employees constituted 10 percent of the total labor forces of state run enterprises. That same year, talks began at the 15<sup>th</sup> Communist Party Congress concerning the privatization of tens of thousands of medium-sized state businesses with the acknowledgement that only a portion of them would survive outside of collective control (Economist, 2000:2). Indeed, some economists believe that 30 to 40 percent of the SOE’s workforce faces elimination in the coming years if state firms are to obtain economic viability (Qian and Wong, 2000:116).

At the beginning of the reorganization, agriculture was privatized, and while some farmers benefited many others turned transient, though this had little effect on long-term unemployment because of the rise of the town and village enterprise (TVE), which specialized in light manufacturing and an abundance of human capital. However, TVE growth was severely stunted by the entrance of foreign owned enterprises utilizing a more technology driven and capital-intensive approach to manufacturing. These foreign firms accomplished two things; they drove less efficient TVEs out of business and reduced the need for a large supply of unskilled labor. Foreign backed firms efficiently produced goods of superior quality and thusly employment in the labor-intensive TVE’s began to decline, forcing many rural residents, desperate for work, to emigrate to the

cities (Levin, 2001:40).

Some 100 million farmers have made the move, arriving to the cities mostly in the time between the planting and harvesting seasons. The reaction of the government has been inimical to their presence. The tactics used so far to restrict the flow of migrant workers into the urban labor supply include frequent fare increases on incoming trains to weight restrictions on transportation originating from rural areas. Migrant Chinese are systematically discriminated against, banned from employment, or forcefully ejected from the city itself. They are denied public services by urban dwellers resentful of their presence who blame them for such social ills as the worsening crime rate and economic cyclicality.

WTO policies will exacerbate the situation by easing tariffs and eliminating subsidies, as per se the liberalization of trade, allowing foreign agricultural suppliers to enter the domestic market, simultaneously driving down food prices and crowding out many Chinese farmers. Conservative estimates predict 10 million farmers will find themselves unemployed as the result of WTO accession, resulting in more migratory patterns towards the wealthier cities. In addition, another 6 million jobs will have to be created to accommodate natural increases to the urban population. Along with the numerous jobs lost to the trimming of state-owned enterprises, this means that nearly 20 million jobs will need to be created each year for the next few years if unemployment is to be remain checked (Economist, 2000:3).

The boost to exports will be one of the greatest prizes that China will take away from their WTO membership; it's in developing the economy along the lines of which the CCP's fate is intertwined, namely delivering a rate of growth so prodigious as to discourage criticism. Yet, with GDP per capita in a gradual decline since 1993 (SEPI, 2002:1-9), there are grave uncertainties over the current capacity of Chinese industry to absorb the brunt of the displaced workers. If the industrial core does not expand as rapidly as the agricultural and state sectors constrict then the poverty and social malaise of unemployment will turn into a blight on China's near future.

### **Unrest and Division**

In August of 1999, farmers from the Jiangxi province attacked government offices and homes of the wealthy in a rebellion numbering some twenty thousand people. The protests were subdued only at the arrival of the People's Armed Police who were called in to help to fight the uprising (Levin, 2001:40). It is believed if the clamor for reprisal was to ever become rabid enough to affect social change on the Chinese mainland, the first balloon to go up would most likely come out of the impoverished agrarian regions.

In February 2000, twenty thousand workers rioted in Liaoning Province after the closing of the Yangjiazhangzi mine. In Liaoyang, the 2002 closure of the state run Ferro Alloy Factory that had employed five thousand Chinese, sent workers into the street demanding back pay, pensions and the arrests of their former bosses. The unemployed protesters were often joined by disgruntled workers from other local factories,

representing the growing solidarity between the disenfranchised of Chinese society, who are often ignored by the political leaders.

The Chinese Communist Party (CCP) has long been successful in suppressing popular desire for institutional change; the deaths of hundreds of pro-democracy activists in Tiananmen Square show the appalling lengths to which their leaders would go to ensure stability. It is on the mantle of this “stability” that the CCP rests their legitimacy, claiming that with China’s multitudes of rival ethnic and regional strata in existence, the mainland would dissolve into factional rule if their hierarchical influence were to ever be removed. But there are signs, from the demonstrations above, that the Chinese may not be placated forever by the economic growth that has already occurred, and are quickly coming to resent the economic progress and governance embodied by the CCP that is, in this assuredly short run analysis, seen as benefiting the minority.

It is important to remember that from its past there are still vestiges of an egalitarian ethos left inside China. While Communism itself betrayed any notion of equality or even fair play, still it would be foolish to assume that the vast populace will transition painlessly into a capitalist society resembling our own (China and the US have similar inequality—both around a .4 Gini coefficient—yet the poorest 10 percent of Americans are still better-off than two thirds of the world’s population).

In regard to global income distribution, the numbers seem to suggest that developed countries appear to be falling away from their developing counterparts. A world Gini measurement of purchasing power parity, or the price as proportion of income for a bundle of goods in France as compared to the same outlay in say Vietnam, increased by 6 percent from 1988 to 1993. In a study by Yuri Dikhanov and Michael Ward, shares of world income going to the poorest 10 percent of the world's population fell by over a quarter, whereas the richest share rose by 8 percent. All of this in a time when the globalization of late is supposed to have increased instances of global convergence and put workers in countries such as India or Malaysia on the path to catching up with their Western counterparts.

Of course, increased global trade and the necessary market reforms appear to be the only long-term guarantee to economic convergence for the simple fact that at this point no other feasible solutions have been offered. The development of industry in developing nations and the utilization in those same countries of their inexpensive human capital will hopefully, in the long-run, provide them with increased income and standard of livings, as well as the democratic self-rule that is the forerunner of such change. Still, in the present it is unclear whether the poor will accept pittance and the unavoidable job loss that is the proscribed antidote to their poverty, especially now when information is so freely disseminated that no longer are people ignorant of the inequality and standards existing outside their world. In the end, it is not so much the reality of the hardships that people face, which is usually so concealed as to be intangible anyway, but what people actually see existing in their own lives. In the end, all the well-intentioned pragmatism in the world might not be able to hold a candle to the insurmountable divide between the haves and the have-nots.

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