

5: The Urban-Rural Divide

The gap between urban and rural society is especially large in China. Today's system traces its origins all the way back to the 1950s, when the basic institutions of the command economy were first established. For sixty years, urban and rural areas have had different governance structures and different systems of property rights. Most important, because of the systemic differences, China has what amounts to two different forms of *citizenship*, one rural and one urban. Rural dwellers have fewer privileges and fewer entitlements than urban dwellers. In China, city and countryside often seem like two different worlds, running on different technologies, organized in different ways, and having different standards of living. For years, these differences were maintained by strict controls on mobility. The creation of a system of residence registration, or *hukou*, made it almost impossible, from the 1960s into the 1990s, for rural people to move to the city. In the past two decades, mass rural-to-urban migration has begun, and the invisible walls separating urban and rural society have begun to break down. While migration has begun to reshape Chinese society, the gap between urban and rural will take many years to disappear.

This system of separate rural and urban organizational structures has important consequences. It leads to an unusually large urban-rural income gap that is the largest cause of inequality in Chinese society. It shapes the urbanization process which is essential to development and growth. It presents an obstacle to China's conversion into a more efficient, knowledge-driven, middle income economy. It obstructs the development of efficient local government systems and the development of national social service systems. For all these reasons, reform of the *hukou* system and the related systems of urban and rural land management, have been near the top of the economic reform agenda in recent years. Nevertheless, as of 2015, these systems have proved stubbornly resistant to fundamental change.

This chapter first describes the origin and nature of the separate organizational, forms of citizenship, and property-rights regimes that characterize the rural and urban economies. These help explain the depth of the divide between urban and rural society, and also serve to introduce the peculiar Chinese property-rights regime. Property rights shape the structure of incentives in any economy, and thus shape economic development as well as market transition. The Chinese property-rights and governance regimes are unusual and differ substantially between urban and rural society. Barriers to mobility and different kinds of citizenship complete the institutional divide. Section 5.2 discusses the process of urbanization. Urbanization is a normal part of economic development, but here again China's extreme policies produced a highly distorted and extremely unusual pattern of urban development. During the Cultural Revolution rural-urban migration was

virtually nonexistent, and cities did not grow for 20 years. After these policies were relaxed at the end of the 1970s, the urbanization process restarted and then accelerated in the 1990s. Section 5.3 discusses migration, which, since its reemergence in the 1990s, has increased rapidly. Finally, the chapter discusses the economic consequences of the urban-rural divide. Chinese policy-making is characterized by substantial “urban bias,” and this is associated with a large urban-rural income gap. This differential increased through 2009, and has just begun to decline. This decline can be traced both to fundamental labor market conditions, and to an important shift in government policy that took place in the first decade of the 21st century. Despite these efforts to reduce “urban bias,” the urban-rural gap remains large in China. Moreover, new urban-rural inequalities are being created in domains that are much more important in today’s economy than in the past: education, house, land and investment opportunities are still highly unequal.

5.1 A Dualistic System: The Division between Urban and Rural

5.1.1 Origins of the Urban-Rural Divide

Today’s large urban-rural gap has its roots in the Socialist period. As described in Chapter 3, during the 1950s, every Chinese citizen was connected through his or her workplace to the socialist state. Virtually every business and productive enterprise was converted to public ownership, and became subject to direct or indirect government control. These institutions were implemented in systematically different ways in urban and rural areas. Urban residents were organized by their place of employment, that is, by their “work unit,” or *danwei*. Almost all urban work units were nationalized—converted to state ownership—and state ownership became predominant in urban areas, with two consequences. First, urban work units were knit into a formal hierarchy, directly subject to planning, command and control; the work unit was part of a “top down” system. Second, the work unit was put in charge of a comprehensive system of social benefits and welfare entitlements, which was gradually built up and extended more or less uniformly to urban workers. Urban residents became a relatively privileged group in Chinese society, and the work unit became the basic building block of urban society.

Rural institutions were quite different. Private property in land was eliminated in 1955, and the land in every village was pooled together and became the property of the village as a whole, of the “collective.” Collective ownership became the predominant form of ownership. Village residents automatically became members of the new agricultural collectives, and access to land and village resources was therefore equalized within the collective. However, there was no mechanism to redistribute resources across collectives, and there were no standards or entitlements that applied to all rural residents.

Rural residents were organized into a “bottom up” system. Collectives were encouraged to support social services out of their own local resources, but they had no claim on national resources. The agricultural collective’s primary function was to sell agricultural produce and earn revenue, and they could take on social service and public good responsibilities only to the extent that they could generate a surplus from the sale of agricultural produce. As a result, the level of benefits and public goods provided was much lower than in the city. Rural residents were poorer than urban residents, and they had a cheaper and less comprehensive set of social institutions to serve them as well.

The different urban and rural administrative systems were tools to carry out the socialist Big Push strategy. The two systems were used to carry out two drastically different functions: the rural system was used to extract low-cost food and fibers from the farmers. The most important functions of the collectives were to manage agricultural labor, and deliver grain to the government. In the urban areas, government invested directly into the work units, where urban workers (the vanguard class of socialism) produced industrial goods for strategic purposes. Thus, the roots of the dualistic system lay in the government’s strategy to extract resources for industrialization, as discussed in Chapter 3. The Chinese government purchased low-cost farm products, then provided a low-price grain ration to urban workers through their work unit. This enabled the government to keep wages low and state-owned factories profitable. Ration coupons were introduced in 1955 as a short-run expedient, but then stayed in place for over thirty years. The whole dualistic system worked as an implicit tax on farmers, who had lower incomes because they were compelled to sell grain to the government at artificially low prices. The result was that farming—and especially growing grain—became an even lower-return occupation than it had always been.

To keep the system functioning farmers had to be tied to the land. At first, during the 1950s, many farmers migrated to the cities to take up better-paying factory jobs, and social mobility was significant. However, when the Great Leap Forward collapsed (1959-61), everything changed. The government kept extracting food from the countryside, long after it became clear there was no more to take, and famine emerged and spread in the countryside, devastating predominantly rural provinces, such as Sichuan and Anhui (1960–1962). Throughout this period, urban dwellers continued to receive at least some of their grain ration, and so were spared the worst. As the magnitude of the post-GLF catastrophe became apparent, China’s leaders began to drastically limit the number of city dwellers with meal tickets. Six million urban residents, mostly recently arrived from the countryside, were cajoled into returning to their native villages in 1961–1962. The system of household registration, which had initially been meant to monitor population movements, not control them, became a tool for restricting rural-to-urban migration. Beginning in 1963, all household registrations

were strictly divided into those urban (or “non-agricultural”) *hukou* that entitled holders to grain rations, and all other “agricultural” *hukou* that did not. It became virtually impossible for a rural household to get an urban *hukou* after the early 1960s. Without an urban residence permit, a farmer could not go to work in the city, and even short trips to the city required him to bring his own grain with him. Rural-to-urban migration dwindled practically to zero. From the mid-1960s onward, the system hardened into a kind of caste system, with dramatically different entitlements and privileges to urban and rural people. The rigidity of the system grew directly out of the trauma of the GLF (Census Office 2014: 256-57; Cheng and Selden 1994).

Only much later, after successful rural reforms in the early 1980s, did China begin to soften this rigid institutional dualism. Successful rural reforms eased concern over basic food supplies and increased the availability of grain in free markets. Grain rationing was gradually phased out, and an urban residence permit was no longer required to eat. The government began to ease restrictions on migration to the cities, at first for smaller cities and for temporary migrants. Broad economic changes have increased opportunities for rural workers in the city, and since the 1990s, resulted in huge migration flows. However, the urban residence permit still exists, and possession of an urban *hukou* still marks a fundamental divide in Chinese society. For the average farmer, it has not actually become much easier to obtain an urban residence permit, although it has become much easier to live in a city without one. Without an urban residence permit, though, a rural migrant still has unequal access to the benefits of urban citizenship, including health care, social security, and education for accompanying children.

5.1.2 The Urban Economic System

5.1.2.1 The Urban *Danwei*.

Through the mid-1990s, urban life in China was defined by the privileges associated with an urban residence permit (*hukou*), and by membership in a work unit (*danwei*). The urban residence permit was a form of entitlement that guaranteed the holder membership in a *danwei*, and thus, of course, a job. When a city dweller graduated from middle school—or university, if smart and lucky—he or she was assigned employment as a matter of course. Thereafter, the work unit became responsible for providing services and benefits to the urban resident. During the peak period of the urban *danwei*, from the mid-1960s until well into the 1990s, urban residence conveyed the following benefits:

- Job security;

- ❑ Guaranteed low price access to food grains, as well as other scarce commodities;
- ❑ Health care (about 40% of all general hospital beds were in the state-owned industrial system);
- ❑ A pension and other benefits, including health care, upon retirement;
- ❑ Primary and middle school education for their children (70% of state enterprises ran schools of some kind); and
- ❑ Low cost housing, supplied by the work unit.

These extensive subsidies added significantly to the privilege of urban residence: many services were provided free and staple foods were priced well below cost. Of course, incomes at this time were low; and services and housing were provided in limited amounts and were generally low quality. A distinctive feature of the Chinese system was permanent employment. After the restrictions on rural-to-urban migration were put in place in the mid-1960s, job mobility between urban work units disappeared as well. In this sense—as discussed in Chapter 8—the Chinese work unit was quite different from the Soviet model from which it otherwise derived. Once a worker entered the *danwei*, he or she expected to remain a member of that *danwei* for life (Lü and Perry 1997)..

The most common type of urban work unit was the state-owned enterprise (SOE) which produced goods and services and earned revenues and profits; but a work unit could also be a public service unit (PSU, still owned by the government) that had revenues but not profits; or a government department. Despite their different primary functions, the different types of work units had many features in common. First, each was integrated into a national administrative hierarchy, with managers appointed by the Communist Party. Furthermore, the benefits each work unit provided to its workers were explicitly defined as entitlements, specified by statute or regulation. The benefits were thus part of an implicit urban social compact, which the government has consistently recognized and tried to protect (though not always successfully, as discussed below and in Chapter 8). Finally, in addition to its primary function, each unit had responsibility for social and cultural activities, and even for political coordination. The work unit was the fundamental building block, or cell, of urban society. Many work units even had the physical form of a cell, with a perimeter brick wall enclosing a nucleus of productive activity. The *danwei* was a microcosm of urban society, into which individuals were born, lived, worked, and died.

5.1.2.2 Urban Property Rights.

Just as urban work units and workers were incorporated into a single national administrative hierarchy, so, in similar fashion, all urban property was incorporated into a national, hierarchical system of state ownership. All urban land was nationalized during the 1950s. All large-scale urban businesses were state-owned. Municipal government budgets were treated as sub-divisions of the national budget. Thus, municipal receipts and expenditures were incorporated each year into the integrated national budget. That meant that, in effect, the government assumed responsibility for water, sewage, transportation, police protection and schools—the entire panoply of ordinary services. As Judith Banister (1987: 328) described the classic system: “urban areas are essentially owned and administered by the state.” This ownership system had different consequences for urban enterprises and land.

Most of the enterprises that were nominally “state-owned” were not actually managed by the national government. Especially after China embraced the development of small-scale enterprises, it was impossible for the national government to exercise effective oversight of its far-flung assets. Inevitably, the authority to manage state firms was delegated to local governments, even while nominal ownership remained with the national government. Successive rounds of decentralization, especially in the early 1970s, created *de facto* property rights for local governments. With day-to-day control over decision-making, local government leaders had significant authority both over cash flow, and decisions over use of land and other assets. But these rights were always seen as delegated to the local government by the national government, and local officials were formally agents of the central government and the Communist Party, part of a chain of authority leading to the highest political officials in Beijing. As a result, economic reforms after the 1980s consisted of repeated, careful renegotiations of the lines of authority within the state-run hierarchy.

Urban land markets developed in this hierarchical context. Even today, all urban land is theoretically owned by the state. However, a market for transferable urban leaseholds emerged during the 1990s, and a system has evolved in which rights to use land for up to 50 years are bought and sold. Under this system, existing occupants were allowed to sell the use-rights of their property—“squatter’s rights” were recognized—and urban land became an important source of revenue and wealth. Cities have no zoning laws, so there are no obstacles in principle that prevent urban land-holders from converting land to the most lucrative use.

5.1.3 The Rural Economic System

5.1.3.1 Rural Collectives.

In the countryside, villages were organized into rural collectives, but no attempt was ever made to integrate villages into the national hierarchical system of administration and ownership. There is of course a government hierarchy in the countryside. This hierarchy extends down to the level of the county, and today below that to the township level. However, the bulk of rural life is outside this governmental system, and the agricultural collectives were never part of this formal government hierarchy. Even today, villages, which have their own village councils and elect village leaders, are not formally part of the government hierarchy. Rather, they are theoretically autonomous organizations. (In practice, important decisions must be approved by government and party officials at the township and country levels.) The primary function of the agricultural collectives was always economic, and their organization is described further in Chapter 10.

The rural resident had membership in a local collective, rather than—like the urban resident—a compact with the state. Membership did not convey any entitlements to government services. Rural collectives could decide to tax themselves and provide services, but since few collectives had the financial resources to subsidize a large range of goods and services, rural residents were much more likely to pay full cost for the public services they received. Because of their position in the overall national system, agricultural collectives were “low power” organizations.

5.1.3.2 Rural Property Rights.

Just as rural collectives were never incorporated into the national administrative hierarchy, so, in similar fashion, rural property, including land, was never integrated into the system of national state ownership. The agricultural collective in principle owned the land that it farmed and any non-agricultural rural enterprises that it created. Households retained their own houses (and the land the houses were on, of course), and had access to farmland through the village collective. Thus, ownership rights in the countryside were never as centralized--as concentrated in the hands of bureaucrats--as was the case with urban state ownership.

During the rural reforms of 1978–1984, collective farming ended in almost all of China, and family farms returned as the dominant agricultural form. Each collective divided up the land among its individual household members, according to formulas negotiated within the collectives. Historical ownership (before collectives) was ignored in favor of formulas based on the number of workers and the number of mouths to feed in a household. By all accounts this process went smoothly, and it has been called, with reason, “the most egalitarian land reform in history” (Walder 2000). But even after dividing up the land, the land system did not change over to a simple private property system. Although land is worked by individual households, the formal ownership still remains with the “collective.” Farmers sign contracts with the collective giving them

land-use rights for periods that have gradually been lengthened, and now often extend up to 50 years.

This system has some peculiar features. Even today peasants do not own the land free and clear, and no Chinese farmer has the right to develop his own land for a completely non-agricultural purpose. Individual farmers cannot capture the value of land appreciation that comes from a favorable location near a city or highway. This is because “collective land” is, by definition, primarily for agricultural purposes and can only be converted to non-agricultural use through a collective decision. Land cannot be used as collateral for borrowing, and land use-right markets have been slow to develop. Collectives in many areas of China can and do redistribute land periodically. According to one large-scale study, farmland has been redistributed at least once in 66% of the surveyed villages, and three or more times in 25% of the villages (Rozelle and Li 1998). Usually, redistribution is carried out in order to accommodate natural population growth. Thus, although private households have (agricultural) use rights and cash-flow rights, they do not have strong security of tenure, and they do not have the right to convert land into other forms of wealth, neither directly by sale or mortgage nor indirectly by conversion to other uses.

These features of the land system have important effects on farmers, as well as important effects on the pattern of urbanization (discussed later). On the positive side, there is very little landlessness. With almost all peasants having access to some land, there is little of the crushing poverty caused by absolute landlessness found in many developing economies. Indeed, a rough guarantee of access to land is the most important form of social insurance in the countryside. On the negative side, the lack of completely secure land tenure affects farmer incentives. The rewards for investment in the land’s long-term productivity are diluted (since there is a possibility land may be redistributed). Moreover, the land system is an obstacle to permanent out-migration. First, families are unable to convert their land into capital, and bring that capital with them to found a start-up business in the city, as they would in a pure market system. Moreover, families that migrate away permanently may suffer a substantial loss: they might have to surrender their land to the collective, which would distribute it to a more “needy,” permanently resident family. To avoid such an outcome, a rural family has a strong incentive to leave some family members on the land while sending others out for temporary jobs outside agriculture. This is a traditional risk-minimizing family strategy, but the land system causes families to cling to it long after they would otherwise have been ready to move permanently into distant, non-agricultural jobs.

Land has become more valuable in China as the economy has grown and cities have sprawled out beyond their original limits. However, for the increased value in land

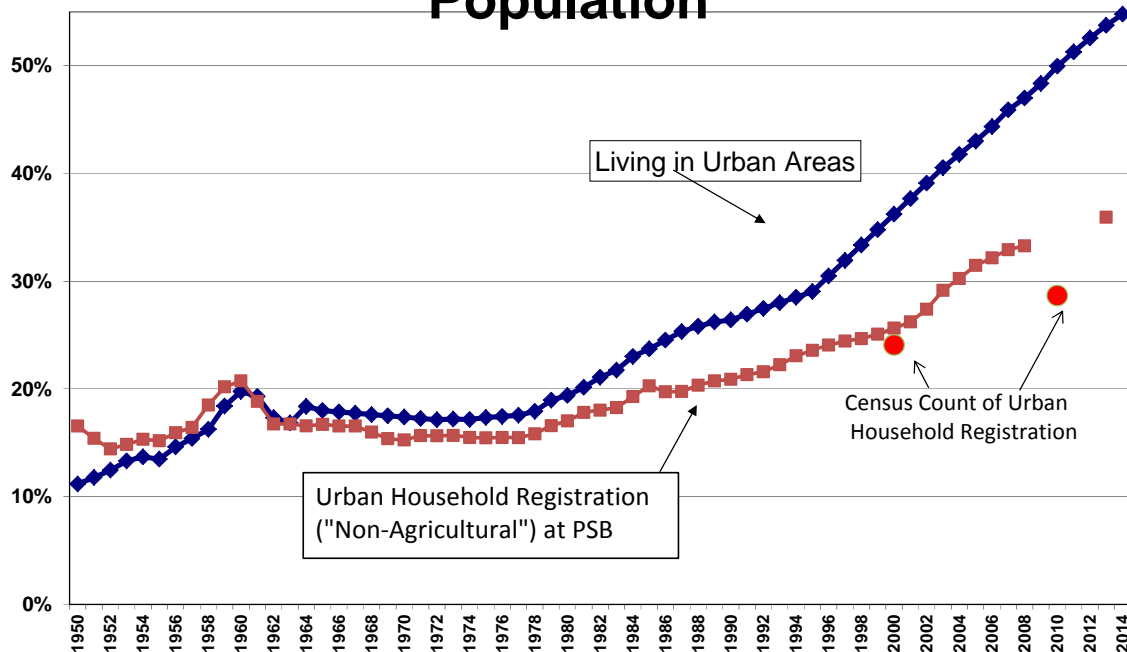
be realized, the land must first be converted to a non-agricultural use. For this to happen, there should be a quota for land conversion (distributed by the central government to the locality), and an agreement between the city government and the agricultural collective to purchase the land. The village head or township officials represent the collective in these transactions, while the individual farmers are not formally part of the process at all.

Honest and effective local leaders would represent the interests all the local residents in these commercial transactions; but selfish, disinterested or corrupt officials do a less than adequate job of reaping the benefits of land values for local citizens. Moreover, individual farmers are accustomed to having access to the land, which is their lifeline, and may feel attached to a specific plot. Rural collectives and individual farmers often disagree over the appropriate level and form of compensation for land transfers. When the land is sold or leased out from under them, rural people react with anger. The largest cause of social conflict in China today is almost certainly disputes over land deals (Yu Jianrong 2005). The rural land property system is an issue of central importance in China today, particularly for those on the periphery of the expanding urban areas.

5.2_Urbanization

Urbanization is a vital part of the development process. As development occurs, workers move out of agriculture and into industrial and service jobs that can be performed much more efficiently concentrated in cities, rather than dispersed in the countryside. China today is in the midst of rapid urbanization, and at the end of 2013, China's population was 54% urban. For millennia, China was a predominantly rural civilization, tied to the soil by work, culture, and, inevitably, by poverty. That is history now, and China's future is unmistakably urban. China's level of urbanization today is within the normal range for a developing country, but China reached its present stage through a trajectory that is utterly unique, and even bizarre. In most developing countries, the pace of urbanization is determined by the decision-making of millions of separate individuals, who assess their own life chances, and decide to leave the countryside and go to the city. But China's past process of urbanization was determined primarily by government policies that, until recently, tightly constrained the scope for individual choice.

Fig. 5-1: Urban Share of Total Population



5.2.1 Urbanization: Historical Trends

The data that describe the process of urbanization in China are shown in Figure 5.1. The series in shaded circles shows the percentages of Chinese citizens classified as “nonagricultural,” that is, those with urban residence permits. These numbers correspond to the discussion of the urban hukou earlier in this chapter and are unique to China. The series in dark squares shows the proportion of the Chinese population resident in urban settlements of a minimum size. These numbers are conceptually consistent with definitions of urbanization in other countries, and they can be used to make comparisons. Together, the series reveal China’s bizarre history of urbanization. Both series show that China *de-urbanized* between the end of the 1950s and 1978. This remarkable twenty year period of de-urbanization had two phases. First, after 1960, China was forced to wind down the unsustainable surge of urbanization during the Great Leap Forward. Millions were forced to leave the cities and millions more left of their own volition in search of food: urban population dropped by 14 million by 1963. Even more remarkable is what happened during the next phase, in the years after 1964 (a relatively normal year, and one with a population census). The urban share of population declined by more than a percentage point, and then stabilized through 1978. This de-urbanization has no real parallel in any other country, since it was sustained for such a long period during which the economy grew (officially at 7% per year), and the size of the urban economy tripled.

Throughout the 1964 to 1978 period, China maintained draconian restrictions on population movement. Access to urban residence permits was jealously guarded; and almost no farmers were allowed to move to the city. Indeed, there was even forced out-migration from urban areas. From the mid-1960s to the mid-1970s, millions of urban dwellers were sent out to the countryside. The largest group, around seventeen million, consisted of young middle school graduates who were “sent down” to the countryside in the wake of the Cultural Revolution. “Sent down” youth remained in the countryside for periods ranging from two years to a lifetime, instructed to learn the realities of work from the poor and middle peasants. Workers were also mobilized to leave big cities to build factories in Western China. Between 1955 and 1976, China’s largest city, Shanghai, experienced a net out-migration of 1.86 million people, and its total population did not grow at all. That such unusual population dynamics could occur is a testament to the extreme degree of political control and mobilization in Maoist China. As Ma Hong said, “Every time there was a political movement, one of the after-effects was that another big batch of urban people were sent to the countryside.” (Zhang Shanyu 2003: 362, 367, 376). Given that the rest of the world was steadily urbanizing, China became more and more unusual through the late 1970s. In 1964, China’s urbanization rate was 18.4%, compared with 26% for all developing countries. By 1978, China’s urbanization rate was only 17.9%, much further below the developing country average of 31% (World Bank WDI)..

Since 1978, China has begun to urbanize rapidly: by 2014, China’s urbanization rate had grown to 57%, finally reaching the developing country average. The broad social relaxation that accompanied the beginnings of reform in 1978 ended the most extreme forms of population control. “Sent down” youth and mobilized workers began to return to the cities, signaling the beginning of a process of gradual relaxation of controls on mobility and the resumption of urbanization. Urban population growth surged above 5% per annum in the nine years from 1978 through 1987. At first, government officials were extremely cautious, and tried to restrict this growth to the smaller cities while maintaining tight restrictions on migration to the largest cities. It was not until the mid-1990s that planners began to grudgingly accept the need for the largest cities to grow as well, and even accepted the idea that some mega-cities might even increase their share of total urban population in the long run. Urban population growth again surged above 5% per year in 1995 to 2003. In the last decade, the absolute increase in urban population has remained steady at about 20 million per year, and the rate of urbanization has continued to climb. The annual growth rate of the urban population has gradually declined, though, to under 3% per year. The overall demographic context has changed dramatically now that the urban population is so much bigger, and total population growth much lower (Chapter 7).

5.2.2 *Composition of Urbanization*

Growth in the urban population can come from three sources, and all have been important in China over the past 40 years. Migration to cities has resumed; cities have sprawled into the countryside; and natural growth of the urban population has continued until very recently. Chen and Song (2014) analyzed the rapid urbanization between 2000 and 2010 and concluded that migration from rural areas accounted for 40.6% of urban population growth; reclassification of population that lives in formerly rural and suburban land (sprawl) accounted for almost exactly 40% of urban growth; and natural growth of the urban population was almost 20% of urban growth. Migration is particularly important, not simply because it is the largest single source of urban growth, but because of the impact that it has on rural society and economic growth. It is covered separately in the following section.

Physical spread of urban areas, like many other features of the urbanization process, takes on a particular form in China. Because of the dualism of the urban-rural land systems, and because the administration of China's cities is embedded in the national administrative hierarchy, the classification of cities takes on a special importance. When China was trying to limit urbanization, the boundaries of Chinese cities were sharply defined. One could walk out from the densely packed urban areas and suddenly cross into farmland. As China has started to promote urbanization, the number of places classified as urban has increased dramatically, and existing cities have sprawled out into the countryside, producing distinctive new patterns of mixed urban, industrial, commercial and agricultural uses. In 1982, there were only 2,660 small towns with established urban management systems (*jianzhi zhen*); by 2001, the number had grown to 20,374 (Zhang Shanyu 321). The number of places classified as cities increased from under 200 in the early 1980s to just over 650 in 1996, after which the number did not increase. However, the land designated urban under those 650-some cities continued to expand, going from 24,000 to 40,100 square kilometers between 2000 and 2010 (Census Office 2015: 269). This dramatic expansion suggests that some of the increase in urban population is simply the result of reclassifying rural lands and the people on them as part of the city.

At the same time, the expansion of urban administration also follows a dramatic sprawl of urban uses into what was formerly countryside. Perhaps the most remarkable urban transformation has occurred in the Pearl River Delta, in Guangdong province. On the Eastern side of the Pearl River, a 120-kilometer stretch of land changed from entirely rural to predominantly urban in 25 years. Between Hong Kong and the provincial capital of Guangzhou, two entirely new cities have grown up—Shenzhen and Dongguan—creating a chain of four large cities of over six million population each. In the Yangtze Delta, urbanization took off about a decade later than in the Pearl River Delta, but the

same pattern of “urbanized countryside” seems to be emerging. In the north, Beijing has sprawled outward from its center, building out now beyond a fifth ring road. These transformations mean that urbanization statistics are not always entirely precise, but also reflect a genuine change: the boundaries of urban and rural, which were easily discernable thirty-five years ago, have blurred and become less distinct as urban and rural interpenetrate.

5.3. Rural-Urban Migration

Rural-to-urban migration has grown rapidly in China since the 1990s, but migrants still face discrimination and limitations on their ability to integrate into urban society. Most migrants remain on the fringes of urban society, sleeping in substandard housing, typically on the outskirts of the city, working long hours, and planning a return to the countryside. Indeed, in many respects, Chinese rural migrants in the city resemble undocumented Mexican migrants working in US cities. By migrating, they substantially increase their income generating potential, and begin to work their way upward. Moreover, they contribute both to the economy in which they are working, and in their home villages, largely by remitting funds home. But they remain in a kind of twilight status, subject to discrimination and mistreatment. Migrants need more effective channels to integrate into urban society. Inevitably, this means access to the education, housing, and social services that go with full urban citizenship.

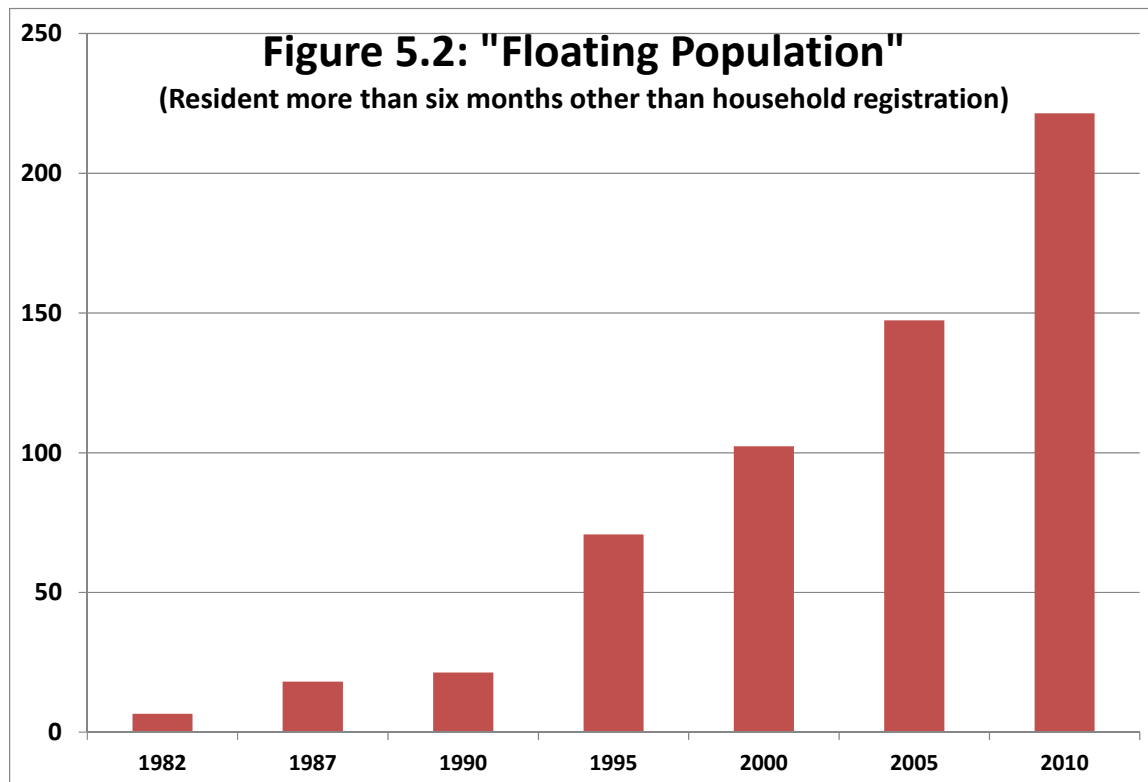
5.3.1 Overview of Migration

How large is migration in China today? The sudden emergence and growth of large-scale migration in China produced much initial confusion about the nature and magnitude of the phenomenon. In its broad outlines, migration in China—and especially rural-to-urban migration—is similar to migration in many other developing countries. But Chinese migrants had become unfamiliar visitors in China’s cities during the long period of population immobility. Their re-appearance evoked complex and sometimes negative reactions from city dwellers. The Chinese term “floating population” (*liudong renkou*) is widely used with a number of different definitions. The national population censuses count individuals who have been living for at least six months in a place other than that in which their household is registered. Using this definition, Figure 5.2 shows the remarkable growth of this population to 221 million in 2010 (excluding urban residents who moved within their native city). Back in 1982, less than 1% of China’s population were away from their place of registration for six months; by 2010, it was over 16%. We can get a sense of the *flow* of migration—that created this *stock* of migrants—by looking at a consistent series of net *inter-provincial* migrants compiled by Kam Wing Chan (the top US expert on urbanization and migration in China). Chan

(2012) tracks a total of 136 million inter-provincial migrants over 20 years, showing (Figure 5.2), inter-provincial migration got started in the early 90s and has increased steadily, such that 11 million people net moved across provincial boundaries annually between 2005 and 2010.

Table 5.1: Inter-provincial Migration

	(average annual net migration; million)
1990-1995	2.14
1995-2000	4.66
2000-2005	7.60
2005-2010	11.04



Migrants have especially been attracted to the booming southern coastal regions. Cumulative migration 1990 to 2010 to Guangdong province was 35.4 million, accounting for a quarter of the total. Large-scale migration to the three Lower Yangtze provinces of Shanghai, Jiangsu and Zhejiang started later than that to Guangdong, but has also grown rapidly. These three provinces received 28 million net immigrants by 2010, accounting for 21% of the total. In the north, Beijing, Tianjin and Liaoning together received 11.7

million, 9% of the total, and Fujian received 3.4 million, or 2.4%. The largest out-migration provinces were Sichuan, Anhui, Henan and Hunan.

Immigration has changed the character of China's cities. Figure 5-1 shows that, as described above, urban residence permit-holders have increased much more slowly than total urban residents. By 2013, there were 731 million urban residents, but only 491 million with urban *hukou*. Therefore 240 million people, or 17.6% of China's total population, was resident in an urban area, but without an urban residence permit. These numbers reflect a two-sided reality: it is still extremely difficult to get an urban residence permit in China, particularly in a large city, but it is much easier to live in the city without one than it used to be.

5.3.2 Characteristics of Migrants

Migration in China increasingly is similar to migration in most other developing countries, which are also undergoing extensive rural-to-urban migration and urbanization. Migrants are predominantly young people in search of better jobs. Research in China has consistently found that migrants are attracted to regions with higher wages and greater job opportunities. People move in search of economic opportunity. For rural residents, the probability of migration is by far the highest for those aged 16-20, and declines by about half for every ten years of age thereafter. When large-scale migration began, in the 1990s, a male was three times as likely to migrate as a female with the same characteristics. However, by 2000, female migrants had closed the gap and the floating population was equally balanced by gender. Women were concentrated in service occupations, and in export-oriented, light industry factories in southeast coastal areas which act as magnets for female migration. Male migrants are more broadly scattered across the construction sites, factories and businesses of urban China.

Migrants increasingly look to the city as a long-term home. Of the 102 million urban "floating population" counted in 2000, exactly one-third were still in the city in 2010. This is reflected in the household composition of migrants. In the 2010 census, only 27% of the "floating population" consisted of individuals; 30% had a wife or sibling; 38% had children with them; and 5% had a parent (Census Office 2014: 233, 238). Migrants are already long-term residents in the city, so their integration into urban life has become a topic of pressing importance.

5.4 Economic Consequences of the Urban-Rural Divide

Urban-rural income gaps inevitably open up during the development process. Industrialization begins in cities during the early stages of development, and at first

virtually all of the modern economy is located in cities. In comparison to urban residents, rural people have lower educational levels, are equipped with less capital, and suffer the economic impact of remoteness and incomplete markets for many needed resources. Not surprisingly, participants in the modern economy, namely urban residents, earn higher incomes; while rural dwellers, remaining within the traditional economy, have much lower incomes for a long time. The following section attempts to chart some of the impact on incomes and living standards of the urban-rural divide.

5.4.1 Surplus Labor Penned up in the Countryside

In the decades before the 1990s, given the restrictions on mobility imposed on the rural population, it is obvious that there was the possibility that surplus labor could build up in the countryside. Between 1957 and 1977, rural incomes stagnated. With increased population bottled up in the countryside, the marginal physical product of workers fell. Since government agricultural procurement prices remained roughly unchanged, the marginal value product fell as well. Membership in the agricultural collective assured ever rural resident access to the land. If population grew without an increase in agricultural productivity, average incomes declined, but the new marginal worker was still put to work (Chapter 10). Under these circumstances, it is obvious that “surplus” labor could build up in the countryside, in the sense that a worker's marginal product could be well below his income. Individual migration decisions did not serve as an escape valve to re-balance the economy. Moreover, as discussed in Chapter 8, migration could not be expected to limit the growth of income differentials: individuals were not able to

5.4.2 Full Employment in the Cities

The situation in cities was the mirror image of that in the countryside. While rural labor was penned up in the countryside, the urban population experienced new access to employment opportunities. Urban employment expanded to incorporate virtually all young women. Urban female labor-force participation became nearly universal during the 1960s and 1970s. As a result, almost all urban households came to have more than one breadwinner. Moreover, strict birth control policies, implemented first in the big cities, reduced the number of dependent children. The result was that the urban dependency ratio (total population/employed population) decreased steadily, from 3.4 to only 2.0 from 1957 to 1977. Thus, even though urban residents suffered under a wage freeze, the real per capita income of urban households increased significantly.

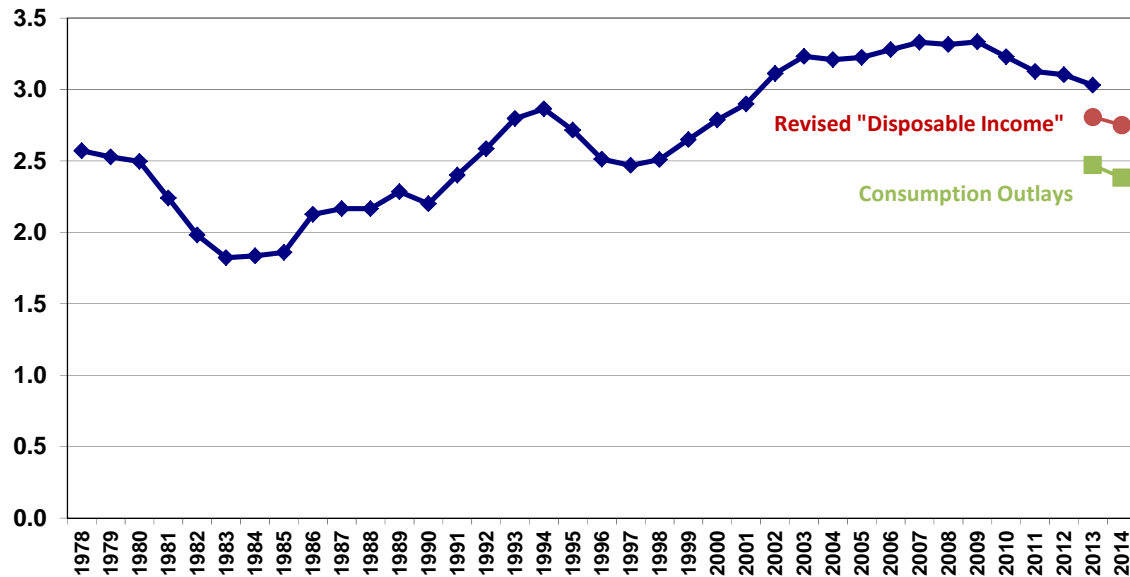
5.4.3 Living Standards and Restrictions on Mobility

The size and evolution of the urban-rural gap in recent years depends on the pre-existing demographic realities described in the two previous sections, along with the impact of migration and urban-centered economic growth. To track this evolution, we use the ratio between per capita money incomes for urban households and those of rural households, shown in Figure 5.3. This information is recorded in the large sample household surveys that are conducted by the Chinese National Bureau of Statistics. Of course, this ratio only reflects the simple money income differential between urban and rural residents. As described earlier, urban dwellers not only have higher money incomes than rural dwellers, but they also enjoy a range of subsidies that they receive in addition to their higher money incomes. However, it is difficult to quantify the monetary value of these subsidies, and this can only be done for a few benchmark years. (This topic is covered further in Chapter 9.) The fact that consumer prices are higher in the city partially offsets subsidies. Moreover, changes in the extent to which subsidies are implicit or explicitly provided as cash supplements (included in income) will affect the urban-rural comparison. Thus these figures have some limits, but the data show a very strong pattern that is unlikely to be overturned by more complete information. At the beginning of the reform era in 1978, the urban-rural divide was already rather wide. The average per capita income of urban residents was 2.6 times that of the rural resident, at the top of the range of comparable developing countries. In the early years of reform, the urban-rural gap shrank, as the success of rural reforms sharply boosted the farmers' income. However, starting from 1984, however, the gap widened steadily, reaching 3.3 times during the 2007 to 2009 period. Only then did the gap begin to narrow, reaching 3.0 by 2013, still well above the 1978 level, and substantially higher than other developing countries.

The increase in the urban-rural income differential between the 1980s and the 2000s is not easy to explain. In itself, we would have expected the lowering of barriers to immigration to have tended to equalize wages, at least of unskilled workers. However, the urban household survey predominantly covers households with urban *hukou*, few of whom are likely to be engaged in manual labor these days.¹ Moreover, the explosive growth of urban economies drove up urban wages faster than incomes from farming were growing. One thing is clear: the rapid increase in migration after 2000 is not surprising: not only were administrative barriers reduced, but income differentials stayed high, and even widened, continuously generating strong “pull” factors that drew rural residents to the cities.

¹ The revised “disposable income” comparison in Figure-3 reflects the effort by the National Bureau of Statistics to include more recent migrants in the urban household sample. As expected, this produces a modest reduction in the urban-rural income differential.

Figure 5-3: Ratio of Urban:Rural Per Capita Incomes (1978-2014)



After 2009, the urban-rural differential finally began to decrease. There were multiple reasons for this change. Perhaps most important has been the shift in underlying labor market conditions. As the size of age cohorts of new young rural workers has declined, and migration has remained high, the pool of surplus young workers in the countryside has been drained. As discussed in Chapter 8, wages of both farm workers and non-agricultural workers have begun to increase rapidly, a pattern that is consistent with the “Turning Point” in Lewis-type models of the development process. It is also broadly consistent with the experience of other developing countries. Henderson (2009) shows that the urban-rural income differential typically declines as a country’s urbanization rate approaches 50%. At this level of urbanization, the pool of under-employed labor in the countryside has been absorbed, and rural wages start to rise. In both Korea and Taiwan, where urban rural differentials were already small, they came down dramatically, and essentially disappeared in the Korean case. By this type of analysis, China is undergoing a similar turning point towards a smaller urban-rural differential. Nevertheless, as of today, that differential is still significant, and much higher than in comparable economies.

5.5 The Urban-Rural Divide in 2015

By 2015, economic growth had completely transformed the economic conditions that had caused the creation of a fundamental urban-rural dualism. Nevertheless, that dualism has not disappeared, but continues to shape many aspects of the Chinese economy, urban and rural. This is in spite of major changes in government policy which significantly improved the policy stance and reduced the degree of built-in “urban bias.” Here we look at the policy shift and then the most important continuing manifestations of urban-rural dualism.

5.5.1 A Fundamental Policy Shift

Central government policy-makers have steadily discarded all the fundamental policies that led them to reinforce the urban-rural divide. Around the turn of the century, and especially during the Wen Jiabao administration (2003-2013), rural incomes and the urban-rural gap became a major focus of policy attention. Motivated by the widening of the urban-rural income gap, the desire to rebuild social services, and anxiety about the anticipated impact of World Trade Organization (WTO) membership on farmer income, policy-makers began to shift attention to rural areas. The result has been, since 2003, the systematic adoption of policies designed to improve rural incomes, and prevent the urban-rural income gap from widening further. Cumulatively, these policies imply that for the first time in the history of the PRC, central government policy has begun to systematically correct for past urban bias, and tilt toward helping farmers. These policies involved a reduction in direct agricultural taxes, and a substantial increase in budgetary expenditures for education and health, and an expansion of government provision of social services in the countryside. The fundamental relationship between farmers and government established in the 1950s was thus finally being changed (see Chapter 18 for discussion). Moreover, concern about the impact of freer agricultural trade after WTO membership, led to direct subsidies for grain farmers, carefully designed to be compliant with WTO regulations. Thus, the historic legacy of taxation of grain producers was finally reversed (Chapter 11). Policy-makers finally discarded the ambivalence with which they had viewed rural-to-urban migration in earlier decades, and began to recognize the economic development required robust migration to the expanding modern sectors. During 2003, the government rolled out the “Sunshine Policy,” designed to provide prospective migrants with rudimentary job training and information about conditions in destination cities. Shortly thereafter, the government produced a strong affirmation of the right of rural people to migrate to cities and reside there without harassment. However, as we noted in the previous section, these policies had no impact on reducing the actual urban-rural income differential through 2009.

5.5.2 Relaxation of the Urban Residence Permit System

As part of the broad policy change outlined in the previous section, the national government has committed to gradually phasing out the urban *hukou* system. In February 2015, the system of selectively issuing temporary residence permits to migrants was abolished, and localities instructed to adopt automatic residence registration. Moreover, a number of provinces have abolished the distinction between urban and rural residence permits, issuing a single unified permit. Finally, a number of large cities, including Shanghai and Beijing, have introduced relatively more transparent points systems that allow migrants to qualify for a permanent urban *hukou*, typically after several years of work and paying into social security.

These reforms have broken important holes in the *hukou* system, but they have not abolished it. Progress has been really substantial only in the smaller cities, while barriers to the more desirable big cities have remained high. The points systems in places like Shanghai are laborious, involve satisfying numerous different bureaucratic agencies, and involve many years of work. Moreover, they are limited by quotas which mean that permanent residence is denied even to qualifying candidates. The larger problem is that cities continue to view the provision of social services to migrants as a huge burden. Since permanent residents receive a fairly high degree of services, and migrants will not contribute to the city tax base as currently structured, treating migrants like permanent residents means a huge burden on municipal finances. Under these circumstances, relying on city governments to further *hukou* reform is not likely to be successful.

5.5.3 Recreation of the urban-rural divide in the urban segmented labor market.

The flow of migrants into the city has transformed urban labor markets, since migrants account for well over half of the urban labor force. Yet the types of work—predominantly manual, unskilled—and the nature of employment are very different for migrants and permanent city residents. Migrants participate in segmented labor markets that reproduce much of the underlying urban-rural inequality that migrants sought to escape (Chapter 8). Migrants in the city typically work much longer hours for lower pay. They are less likely to be rewarded for investments in education and job skills, because many high skilled jobs are effectively barred to them.

Like “informal sector” workers anywhere, migrant workers are rarely covered by any social insurance programs. In 2011, of the urban “floating population,” only 16% were covered by any basic pension program, and 18% had health insurance (Census Office 2014: 239). Since that time, there has been an effort to roll out lower-cost programs of health insurance and pensions for which migrants may qualify, so these numbers have probably increased (Chapter 18).

5.5.4 Second-generation Inequalities

As the preceding section indicated, much of the persistent urban-rural divide is now manifested in so-called “second generation” arenas—education and housing above all. Rural people are doubly handicapped in access to education. They have difficulty finding good schools for their children in any case. Migrants to the city, despite central government encouragement, find it extremely difficult to enroll their children in urban schools. Additional fees are charged, and quantitative quotas enforced. Many migrants leave their children at home, or place them in special migrants schools in the city with sub-standard levels of education.

5.5.5 Dualistic Land System Still Intact

One area where there has been almost no progress is in the reform of the dualistic land ownership system. Earlier we discussed the conversion of land from the farmer’s perspective, showing that rural people are effectively locked out of the lucrative opportunities that come from land development in suburban areas. Here we examine the same process from the standpoint of the municipal authorities. The conversion of rural to urban land is completely controlled by local municipal governments. They have a monopoly position in negotiating with the representatives of agricultural collectives to requisition land, so they can play collectives off against each other and get the lowest possible price. Then city governments are monopoly sellers of the newly created urban land-use rights, so they can play developers off against each other, extracting high prices and playing favorites. Not surprisingly, land revenues have grown steadily and have become the most important part of municipal-level revenues. More and more Chinese cities are dependent on real estate development to fund their basic activities (Chapter 18). This dependence creates many negative side-effects. We noted above in 5.2.2 that the amount of land under the control of China’s cities grew rapidly between 2000 and 2010. Indeed, land increased by 79% while the urban population increased 46% between these years. Surely some part of this rapid expansion of land area is due to the enthusiasm shown by urban governments for land development, a role forced on them by the importance of those revenues in their total resource base.

A peculiar manifestation of these issues is the survival of “urban villages” in China’s cities. These are agricultural settlements that have gradually surrendered all their farmland for urban development, so that the original village is now surrounded by city. These urban villagers usually retain their rural household registration, but make use of the relative absence of urban regulation to run markets, services and housing for migrants. They are in the city, but hardly of it, and many are strongly conscious of the divide between them and their close urban neighbors, and worried about their economic futures.

5.5.6 Urban Governance

Ironically, the lack of enthusiasm shown by city governments for *hukou* reform, and the enthusiasm they show for land development, are both symptoms of the basic structures of urban governance. Mayors of cities are appointed by higher government and Party authorities, so they have only limited accountability to city residents. They are instructed by upper levels to maximize economic growth, and their careers depend on these objectives. They face limitations on potential revenue sources, since except for a few pilot cities, there are no property taxes. Land development provides them a way out of this dilemma. Migrants already contribute their labor, and the present system rules out their contribution through augmenting property tax collections. The existing fiscal system and urban governance mean that city officials have no incentives whatsoever to eliminate the remaining features of the urban-rural divide, and in fact have an interest in maintaining them.

5.7 Conclusion

The administrative barriers dividing urban and rural areas have economic origins and economic consequences. As socialist China underwent development, economic policies were created that affected the mobility of labor as well as the compensation structure in urban and rural areas. The most important economic consequence is that workers in the urban economy enjoy relatively generous wages and benefits, while rural labor remains penned up within the rural economy. The result is an extensive misallocation of labor, combined with excessive inequality. Rural workers earn below their marginal product, while urban workers may earn above their marginal product; and the income gap between the categories is larger than it would normally be. Economic reforms have begun a process of dismantling the barriers between the urban and rural economies, but they remain fundamental in understanding the functioning of the Chinese economy, as well as in determining the different life outcomes of Chinese households.

Suggestions for Further Reading

Knight and Song (1999) combines microeconomic analysis based on survey data with a broad structural view.

Sources for Data and Figures

Figure 5.1: NBS Department of Comprehensive Statistics (1999: 1) for series by residence permit; updated from SAC, various years; and Population Statistics Yearbook 2005: 265. SYC for standard urbanization series

Figure 5.2: Census Office (2014), p. 231.

Figure 5.3: SYC (various years).

Table 5.1: Chan (2012).

Urbanization Rate: Average of all low- and middle-income countries is from World Bank, World Development Indicators (average includes China). China data is from SYC and Annual Economic Report (2006), which differ slightly from World Bank reported data for China. The exact standard for judging an urban settlement differs significantly across countries, so cross-national comparisons of urbanization are not precise. Moreover, the Chinese data have been revised several times by Chinese statisticians, most recently in the wake of the 2000 census. The post-2000 definition includes people in settlements larger than 3,000, plus those under urban management (defined according to administrative criteria). Chinese statisticians have revised earlier data in an attempt to make them consistent and comparable across time, but some comparability problems remain. Zhang Shanyu (2003: 289–291) and Census Office (2014: 258–260) have good discussions.

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