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Poverty Reduction and the Income Inequality in China

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CORNHUSKER ECONOMICS

Poverty Reduction and the Income Inequality in China

Market Report	Yr Ago	4 Wks Ago	6/25/10
<u>Livestock and Products,</u>			
<u>Weekly Average</u>			
Nebraska Slaughter Steers, 35-65% Choice, Live Weight.....	\$80.31	\$97.50	91.23
Nebraska Feeder Steers, Med. & Large Frame, 550-600 lb.	125.35	130.98	135.88
Nebraska Feeder Steers, Med. & Large Frame 750-800 lb.	*	116.61	117.50
Choice Boxed Beef, 600-750 lb. Carcass.	140.00	168.19	154.50
Western Corn Belt Base Hog Price Carcass, Negotiated.	56.53	80.53	77.56
Feeder Pigs, National Direct 50 lbs, FOB.	31.36	*	*
Pork Carcass Cutout, 185 lb. Carcass, 51-52% Lean.	56.26	88.45	84.08
Slaughter Lambs, Ch. & Pr., Heavy, Wooled, South Dakota, Direct.	111.00	137.00	130.75
National Carcass Lamb Cutout, FOB.	261.06	311.89	312.37
<u>Crops,</u>			
<u>Daily Spot Prices</u>			
Wheat, No. 1, H.W. Imperial, bu.	5.35	3.66	3.39
Corn, No. 2, Yellow Omaha, bu.	3.74	3.52	3.26
Soybeans, No. 1, Yellow Omaha, bu.	11.75	9.47	9.59
Grain Sorghum, No. 2, Yellow Dorchester, cwt.	6.14	5.64	5.14
Oats, No. 2, Heavy Minneapolis, MN, bu.	2.06	1.94	2.65
<u>Feed</u>			
Alfalfa, Large Square Bales, Good to Premium, RFV 160-185 Northeast Nebraska, ton.	*	140.00	150.00
Alfalfa, Large Rounds, Good Platte Valley, ton.	*	67.50	82.50
Grass Hay, Large Rounds, Premium Nebraska, ton.	*	67.50	*
Dried Distillers Grains, 10% Moisture, Nebraska Average.	130.37	115.00	92.50
Wet Distillers Grains, 65-70% Moisture, Nebraska Average.	47.45	35.00	32.00
*No Market			

In 2000, the United Nations adopted the Millennium Development Goals which set targets for raising living standards in low-income countries. The first goal was to “eradicate extreme poverty and hunger” (United Nations). The World Bank defines extreme poverty as income of less than \$1.25 per day (World Bank, 2010a). Based on this definition, the World Bank estimates that the percentage of the population in China living in extreme poverty has fallen from 84 percent in 1981 to about 16 percent in 2005, a period during which China’s population grew by more than 300 million people (see Table 1 on last page). Because China is a very large country with a current population approaching 1.4 billion (more than four times the United States population), its dramatic reduction in poverty over the past 30 years has had a profound effect on global poverty measures. In fact, poverty reduction in China is the main reason that the incidence of extreme poverty in developing countries has fallen from about 52 percent in 1981 to 25 percent in 2005 (Table 1). While the absolute number of poor in China fell by some 627 million, the number of poor in other developing countries actually grew slightly (from 1,065 million to 1,166 million). These figures represent a decline in the percentage of the total population in poverty in other developing countries because of general population growth over that 25-year period (World Bank, 2010b).

China’s success in reducing poverty stems largely from economic reforms initiated in 1978. Interestingly, a major thrust of these reforms involved the elimination of strict agricultural production quotas and collectivized farming, allowing Chinese farmers to benefit from their efforts to expand production. As economic reforms spread to the industrial sectors, the Chinese economy began growing very rapidly, with average annual growth rates of more than ten percent over the past twenty years (for reference: average annual economic growth in the United States was about three percent over the same time period).

Between 1995 and 2008 China's Gross Domestic Product increased by a factor of six, and by 2008 China's economy had become the third largest in the world. Annual per capita income, measured in constant dollars adjusted for inflation and purchasing power, increased from \$523 in 1980 to \$5,515 in 2008 (for reference: U.S. per capita income in 2008 was \$42,809; see World Bank 2010b). These economic gains have meant higher living standards, increased educational opportunities and healthier populations. For example, life expectancy at birth has increased from 65 years in 1978 to 73 years in 2008 (2008 U.S. life expectancy was 78; in Japan it was 83; World Bank, 2010b).

At the same time, inequalities in the distribution of income in China have increased sharply. Prior to the economic reforms of the late 1970s, Chinese leaders emphasized egalitarian policies that gave rise to a fairly equal distribution of income. People were poor, but there were few significant disparities in the amount of income individuals were able to earn. It is not unusual for inequalities in the distribution of income to arise as countries begin to experience growth and industrialization. As long ago as 1955, Simon Kuznets noted that poor countries tend to have fairly equal income distributions that become more unequal as they begin to grow. Countries that pass a certain level of income begin to implement redistributive policies and to enhance opportunities for the poor, with the result that inequality tends to be lower in high-income countries. The United States is an exception to this generalization, with much higher levels of inequality than most other countries with similar income levels (Figure 1). According to Kuznets's hypothesis, it is not surprising that inequality in China began to rise as per capita incomes grew.

incomes are on average 65 to 75 percent higher than rural incomes. Much of China's rapid economic growth has been concentrated in coastal areas, while inland regions have lagged behind. Increasing interpersonal inequality has been driven in part by growing returns to skills and education, which favor urban residents working in manufacturing industries (Wan, 2008).

Income inequality can be measured in many different ways. Most analyses of this subject begin with measures of the percentage of total income that flows to individuals or households, ranked from the poorest to the richest. In the United States, the income share of the richest ten percent of the population is about 30 percent, while the share of the poorest ten percent is less than two percent. A completely equal income distribution (something that has never existed) would mean that everyone has the same income, so the poorest ten percent would have the same share of income (10%) as the richest ten percent. The most common measure of income inequality is the Gini ratio, which can take values from zero to 100, with higher values representing greater inequality. The Kuznets relationship based on per capita income and the Gini ratios are illustrated in Figure 1, in which a typical Kuznets curve has been superimposed on the data. It is clear that the countries included in Figure 1 do not follow the Kuznets prediction very closely. The history of inequality in China, however, seems consistent with the Kuznets hypothesis. Chen et al. (2008), estimate that China's Gini coefficient increased from 30.29 at the beginning of the economic reforms in 1978 to 41.53 in 2006, signaling a substantial increase in income inequality.

As the Chinese economy continues to grow, income distribution may become even more unequal. Income inequality can be a problem, as it may lead to social and political instability. If China follows the pattern predicted by the Kuznets curve, however, the government will eventually respond to this potential problem by establishing social safety nets that will help reduce these income inequalities. That has been the pattern in today's high-income countries, with the exception of the United States where income inequality has grown over the past 30 years. Most analysts seem to agree that the main source of inequality in China is the gap between the incomes of rural and urban households (Chen et al., 2010; Chan and Hu, 2003). Migration of workers from rural areas to the cities could contribute to a more equal income distribution through two avenues. First, wages in manufacturing are generally higher than wages in agriculture. Second, migration from rural areas to the cities means an increase in the urban labor supply that could result in lower urban wages. It would also reduce rural labor supply, leading to higher wages in the countryside (Bjorn, 2008).

In Europe, industrialization was driven by the release of excess rural labor that could be employed in the growing manufacturing industries. The economic transition was

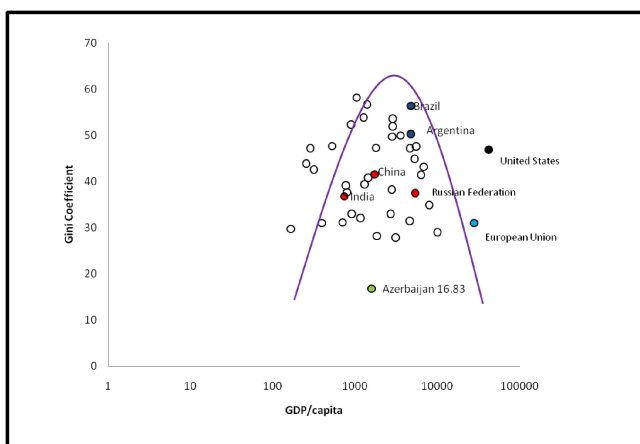


Figure 1. Income Distribution and the Kuznets Curve

As a practical matter, growing income inequality in China may have been driven by economic reforms that allowed some people to "get rich first," a term developed from Deng Xiaoping's well-known statement (Wan, 2008). In addition, inequality has been exacerbated by the significant gap between rural and urban residents. Urban

facilitated by increased agricultural productivity that allowed fewer farmers to produce enough food to feed the growing urban populations. It is likely that similar changes will be necessary in China to complete the change from a predominantly agrarian society to an urban-industrial country (Chen et al., 2008). The transition can be facilitated by appropriate government policies, for example, greater investments in agricultural research can lead to increased agricultural productivity and growing rural incomes. In May 2009, the Chinese government announced major reforms to the country's health care system, aiming to reduce the number of uninsured and improve health-care delivery in rural areas (MacLeod, 2009). It is likely that more initiatives of this nature will be needed if China is to slow, and eventually reverse the rising inequality that has accompanied its rapid economic growth.

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Table 1. Percent of Population in Extreme Poverty (less than \$1.25 per day adjusted for currency purchasing power), 1981 - 2005.

Region	1981	1984	1987	1990	1993	1996	1999	2002	2005
East Asia-Pacific	77.7	65.5	54.2	54.7	50.8	36.0	35.5	27.6	16.8
China	84.0	96.4	54.0	60.2	53.7	36.4	35.6	28.4	15.9
Europe-Central Asia	1.7	1.3	1.1	2.0	4.3	4.6	5.1	4.6	3.7
Latin America-Caribbean	12.9	15.3	13.7	11.3	10.1	10.9	10.9	10.7	8.2
Middle East-North Africa	7.9	6.1	5.7	4.3	4.1	4.1	4.2	3.6	3.6
South Asia	59.4	55.6	54.2	51.7	46.9	47.1	44.1	43.8	40.3
India	59.8	55.5	53.6	51.3	49.4	46.6	44.8	43.9	41.6
Sub-Saharan Africa	53.4	55.8	54.5	57.6	56.9	58.8	58.4	55.0	50.9
All Developing Countries	51.9	46.7	41.9	41.7	39.2	34.5	33.7	30.5	25.2

Source: World Bank (2010b)

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