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## Social policy reforms and economic distances in China, 2002-2013

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## 2017-22 Social Policy Reforms and Economic Distances in China, 2002-2013

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**Social Policy Reforms and Economic  
Distances in China, 2002-2013**

by

**Qin Gao, Sui Yang, Fuhua Zhai and Yake Wang**

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## **ELEVEN**

### **Social Policy Reforms and Economic Distances in China, 2002–2013\***

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## Abstract

Using the data from the China Household Income Project (CHIP) in 2002, 2007, and 2013, this chapter examines the effects of a series of social policy reforms on the economic distance between the rich and poor in each of the urban, rural, and migrant household sectors. We find that over the years pensions in the urban areas consistently helped narrow the economic distance among urban households, whereas other social benefits—including health insurance, social assistance, supplementary income, and in-kind benefits—had little or no redistributive impact. Both rural and migrant social benefits changed from being regressive in 2002 to becoming progressive in 2013. Among all social benefits in the rural areas in 2013, supplementary income and in-kind benefits in the form of agricultural and livelihood subsidies played the most significant redistributive role, while private transfers also helped to substantially narrow economic distances. Among migrants, in 2013 health benefits and taxes and fees helped narrow economic distances, although to a lesser extent as compared to the rural social benefits. Despite the expansion of social policy during this period, in both urban and rural China market forces still played a dominant role in widening the economic distance between the rich and poor, which trumped the redistributive effects of the social benefits. These results suggest that China's future social policy reforms face continued challenges in terms of unifying the urban-rural-migrant imbalances and keeping pace with the disequalizing market forces.

**Keywords:** China, social policy, economic distance, inequality, pensions, agricultural subsidies

**JEL Classification:** H23, H55, O23, P35

## **I. Introduction**

The Chinese government has launched a series of social policy reforms during the past fifteen years that aim to provide basic social protection to its citizens and to unify the long-segregated social benefit systems across the urban-rural divide. Part of the reason for the expansion of social policy reforms has been China's rapidly rising income inequality in China that surpasses conventional alarm levels and threatens political stability and social harmony, both of which are high on the agenda of the ruling Communist Party. China's national Gini coefficient rose from 0.44 in 2000 to 0.49 in 2008, and then declined somewhat to 0.47 in 2012, but China remained among the most unequal third of all countries (Li and Sicular 2014; Ravallion and Chen 2007). The fast-growing number of Internet and social media users during this period also helped expose the widening income gaps and the imbalances in social benefits enjoyed by various groups, promoting awareness and demand for greater social protection among Chinese citizens.

To address these challenges and shift away from focusing solely on economic growth, the Chinese government launched significant social policy reforms that expanded its social insurance and social assistance programs to extend coverage from urban employees to urban non-employees, rural residents, and, to some extent, rural-to-urban migrants. In 2006 the government implemented an extensive campaign to "Build a New Socialist Countryside" based on a series of initiatives to improve the livelihood of rural residents. Enactment of the 2008 Labor Contract Law required that all employers sign labor contracts with employees and provide social insurance coverage for employees, including migrant workers.

How successful was this series of social policy reforms in redistributing resources and

narrowing the economic distance between the rich and poor? Existing studies have examined the redistributive effects of selected social benefits, but they have not examined the complete set of social benefits in its entirety. In addition, most existing studies rely on the widely used Gini coefficient to capture the redistributive effects of the social benefits on the overall income distribution. However, none of the studies have focused specifically on the economic distance between the rich and the poor, the two ends of the income distribution that are often most sensitive to the receipt of social benefit.

In this chapter, we use data from the China Household Income Project (CHIP) surveys in 2002, 2007, and 2013 s to investigate how the social policy reforms affected the economic distance between the rich and poor during the 2002–2013 period. We address this research question separately within the respective urban, rural, and migrant samples to better understand the different effects of these social policy changes on the various populations. Chapter 10 in this volume by Cai and Yue uses data from the CHIP 2013 survey to investigate the redistributive effects of social security expenditures in the national context, whereas Chapter 5 by Hoken and Sato utilize all five waves of the CHIP data to examine the effects of public policy on trends in long-term inequality in rural China.

In this chapter, we use an innovative and revealing method to examine the economic distance between low- and high-income households within the urban, rural, and migrant populations to shed more light on aspects of the income distribution that are beyond the overall level of inequality as captured by the Gini coefficient. Our findings, supplementing evidence based on analyses of selected social benefits that use on the Gini measure, suggest important policy implications as China continues its social reforms and expansions.

## II. Social Policy Reforms and their Redistributive Effects: 2002–2013

Scholars largely agree that the social policy reforms during the 2002–2013 period represent a significant expansion and shift in the policy direction from focusing on economic growth to focusing social development (Besharov and Baehler 2013; Carrillo and Duckett 2011; Leung and Xu 2015; Liu and Sun 2015; Ngok and Chan 2015; Saich 2008, 2015; Shue and Wong 2007). Duckett (2012) characterizes these reforms as a compromise between the social and economic agendas, whereas Frazier (2014) emphasizes the role of urbanization in driving the unification of the urban-rural social benefit systems. This literature, however, also points out the persistent urban-rural-migrant disparities in terms of social provisions and benefit levels and the gaps across employees and non-employees in the urban areas. Empirical evidence based on the 2002–2007 CHIP data suggests that social policy reforms during this period moved in the direction progressivity, but the urban-rural gaps remained substantial and migrants continued to be left behind in terms of social protection (Gao, Yang, and Li 2013).

First, during this period a comprehensive social insurance system began to take shape, with significant expansions of pensions and health insurance to urban non-employees, rural residents, and migrants. Specifically, the urban pension system gradually moved from covering only civil servants and employees of public institutions and state-owned enterprises (SOEs) to a dual system of social pooling (i.e., earnings-based and pay-as-you-go) and individual accounts (with mandatory individual contributions). In 2012, a nationwide urban resident pension system, funded by both government subsidies and individual contributions, was established for urban non-employees. A New Rural Social Pension System (NRSPPS) was launched in 2009 to provide pension coverage for rural residents. It also offered a national framework to allow participation



by migrant workers. This system was fully funded (in the central and western regions) or half-funded (in the eastern region) by the central government and a highly subsidized personal savings account. In 2014, the rural and urban pension systems were unified to allow equal access and equal quality of pension systems for urban and rural residents and to facilitate rural-urban mobility. Nevertheless, average benefit levels for urban non-employees and rural residents remained very low and varied substantially across localities, whereas urban employees received pension benefits in accordance with their job positions and ranks (Dorfman, Oltzmann, and O’Keefe 2012; Leung and Xu 2015; Liu and Sun 2016).

Another major development in the social insurance system was the expansion of health insurance. In particular, the Urban Employee Basic Medical Insurance (UEBMI) was expanded from covering only employees and retirees with urban *hukou* to covering migrant workers (Hu and Ljungwall 2013). The Urban Resident Basic Medical Insurance (URBMI, with significantly lower premiums and benefits than those of the UEBMI (Fang 2014; Ministry of Health 2010) was implemented nationwide in 2010 to provide health coverage for urban non-employees, including children, older adults who were ineligible for the UEBMI, and the poor and disabled. The New Rural Cooperative Medical System (NRCMS) was introduced in 2002 and implemented nationwide in 2008. Heavily subsidized by the central and local governments, it is a voluntary health insurance program for rural residents, with low premiums and benefits (Barber and Yao 2010; Fang 2014). By 2013, the coverage rate of the NRCMS reached 98.7 percent of the country and covered 802 million participants (Guojia weisheng jishengwei guihua yu xinxi 2014).

Wang and his colleagues (Wang 2013; Wang, Long, Jiang, and Xu 2016), using survey data from 2012, have examined the redistributive effects of social insurance programs. They

found that social insurance income lowered the Gini coefficient overall by 6.4 percent. This social insurance income included pensions, health, maternity, work injury, and unemployment insurance. However, the redistributive effects differed greatly for the urban-rural-migrant populations: social insurance helped reduce the urban Gini coefficient by 12 percent, the rural Gini coefficient by 3 percent, and the migrant Gini coefficient by only 0.1 percent. Pensions contributed the most to income redistribution, lowering the Gini coefficient by 5.88 percent. Much of this reduction (5.30 percent) was due to the pensions for urban employees and retirees, whereas the pensions for urban non-employees and rural residents had minimal effects (reductions in the Gini coefficient by 0.24 percent and 0.32 percent, respectively). Health insurance lowered the Gini coefficient by 0.49 percent, with 0.27 percent, 0.20 percent, and 0.02 percent respectively due to the NRCMS, UEBMI, and URBMI. Maternity, work injuries, and unemployment insurance together helped reduce the overall Gini coefficient by only 0.04 percent.

Second, this period also saw the establishment and expansion of a comprehensive social assistance system. The centerpiece of this system, the Minimum Livelihood Guarantee, or *dibao*, was initially established in cities in 1999 but it was expanded significantly during 2001–2002. It was further expanded to the rural areas in 2007. Meanwhile, the government also launched a series of supplementary social assistance programs to offer extra support to needy families and to integrate the traditional “three withouts” (*sanwu*, i.e., those without income, without a working ability, or without a legal guardian in the urban areas) and the “five guarantees” (*wubao*, i.e., guarantees to provide food, clothing, shelter, medical care, and burial services for rural residents who have no working ability or income source) programs into this system. These include medical, education, and housing assistance as well as temporary assistance to provide subsidies

and service referrals for individuals and families facing urgent or extreme difficulties (Gao 2017; Liu 2010).

Using data from the 2007 CHIP survey, Li and Yang (2009) found that the urban *dibao* had a very small impact on reducing income inequality, lowering the overall Gini coefficient by only 0.46 percent and the ratio between the average income of the highest and lowest income deciles by only 3.19 percent. A growing number of recent studies on the rural *dibao* have focused on its targeting performance and its anti-poverty effectiveness (Golan, Sicular, and Umapathi 2017; Han, Gao, and Xu 2016; Han and Xu 2013, 2014; Liu and Xu 2016), but none of these studies have examined its impact on income inequality. Given the small size of the *dibao* benefits, it is reasonable to speculate a similar small impact on inequality in the case of the urban *dibao*.

Using data from the 2009 China Health and Nutrition Survey, Lu and his colleagues (Lu, Lin, Vikse, and Huang 2013) investigated how pensions and social assistance affected income inequality. They found that pensions substantially helped lower the Gini coefficient (by 0.0595), whereas social assistance, including the *dibao* and disability subsidies, only lowered the Gini coefficient by 0.0046. However, pensions were distributed regressively, helping raise the ratio of those in the top-quintile income to those in the bottom-quintile income from 15.99 to 17.60. Social assistance also helped reduce this ratio from 15.99 to 14.80. In addition, the authors, in examination of in-kind subsidies that were mostly employment-based (e.g., assistance for food, gas, coal, electricity, and childcare), found that in-kind subsidies played a small but positive role in reducing overall income inequality and in narrowing the top-bottom income gap. Chapter 10 in this volume by Cai and Yue uses the CHIP 2013 data to examine the redistributive effects of public transfers in the national context. They find that the formal sector pension benefits and the

medical expense reimbursements were disequalizing, whereas the *dibao* benefits and rural pensions were equalizing.

Third, in addition to expanding social insurance and social assistance, the government launched a major campaign to Build a New Socialist Countryside through a series of initiatives to narrow the urban-rural gap and to improve the livelihood of rural residents. These initiatives included the abolition of agricultural taxes, the elimination of tuition and fees for rural compulsory education, increased investments for rural infrastructure, and the provision of direct subsidies to support the production and welfare of farmers (Fock and Wong 2008; Frazier 2014; Lardy 2012; Lin and Wong 2012; Wallace 2014; World Bank 2007). Based on an analysis of all five waves of the CHIP data, Chapter 5 in this volume by Hoken and Sato finds substantial improvements in the redistributive and poverty impacts of public transfers in the rural areas, signifying a historic reversal in the long-term urban-biased public policy in contemporary China.

Two other studies have examined the redistributive effects of specific components of these policies in rural China. Lin and Wong (2012) focus on direct subsidies to farmers, which include subsidies for farmland production, social welfare, and public services (e.g., pensions, health, education, and *dibao*), and subsidies for living condition. Using administrative data during from 2003 to 2009 published by the various Chinese commissions and ministries as well as in the *China Statistical Yearbooks*, they found that over time these subsidies played an increasingly larger role in narrowing the urban-rural income gap. However, their analysis of a 2005 Ministry of Agriculture survey dataset reveals these subsidies to have a strikingly regressive effect, with higher-income households, households with a Party member, and households in richer regions reaping greater benefits than others from these subsidies.

Using the CHIP 2002 and 2007 data, Li and Sicular (2014) focus on the redistributive

effects of the abolition of agricultural taxes. They find the average tax rate paid by rural households decreased from 2.8 percent in 2002 to 0.3 percent in 2007, suggesting that the abolition of agricultural taxes and fees had positive distributional effects. They also find that this policy change was particularly beneficial to low-income groups, with the average tax rate for those in the lowest income decile decreasing from 6.2 percent in 2002 to 0.3 percent in 2007, whereas the average tax rate for those in the highest income decile declined from 1.5 percent to 0.4 percent during the same period. However, they found this policy to have virtually no effect on overall income inequality in the rural areas.

Fourth, the government also made efforts to improve labor conditions for migrant workers. The 2008 Labor Contract Law required that employers sign labor contracts with employees and provide them with social insurance coverage. These stipulations were most beneficial to migrant workers, by improving labor conditions and increasing the subjective well-being of migrant workers, since previously they were largely ineligible for such protection (Cheng, Smyth, and Guo 2015; Gallagher, Giles, Park, and Wang 2015; Gao, Yang, and Li 2012, 2016; Li and Freeman 2015). Luo and Sicular (2013) use the CHIP 2002 and 2007 data to find that income from migrant employment contributed to robust economic growth in rural households and helped to reduce income inequality and narrow the urban-rural income gap. Because of this law, migrant workers were more likely to sign labor contracts, receive higher wages, and enroll in pension, health, work injury, and unemployment insurance.

In summary, existing evidence shows that social insurance—especially pensions—played a dominant role in reducing income inequality during this period, whereas social assistance had a negligible effect in narrowing inequality gaps. Both the campaign to Build a New Socialist Countryside and the efforts to support migrants helped improve the living conditions of rural

residents and migrants and to reduce income inequality. Building on this body of literature, in this chapter we use the CHIP 2002, 2007, and 2013 data to offer new evidence on the effects of these social policy reforms on the economic distance between the rich and the poor among each of the urban, rural, and migrant populations during the 2002–2013 period. We hypothesize that social insurance, particularly pensions, played the most prominent role in narrowing the economic distance between the rich and poor, whereas social assistance played only a minimal role. We also hypothesize that the economic distances among the rural and migrant samples were reduced due to the social policy reforms that aimed to increase living standards, especially among the most vulnerable population groups.

### **III. Data and Methods**

#### **A. CHIP Data**

This study uses the three recent waves of CHIP data, which collected information regarding family income, consumption, and demographics for 2002, 2007, and 2013. The CHIP samples were drawn from the larger National Bureau of Statistics (NBS) samples using a multistage stratified probability method to achieve national representativeness. For the 2002 and 2007 waves, the households were drawn from lists of households with official local urban or rural *hukou* to form the respective urban and rural samples. The urban and rural questionnaires were designed to capture the different income sources and structures of the two groups. However, as urbanization and migration accelerated, relying on the *hukou* as the sampling criterion was no longer feasible or accurate. At the end of 2012, the NBS launched its first national household survey using a unified sampling frame, income definition, and questionnaire. The sampling was stratified by province and based on information from the 2010 census. The sample households in

the 2013 CHIP survey were selected from the NBS sample using a multistage stratified probability method.

In addition to the urban and rural samples, the 2002 CHIP for the first time included a subsurvey of 2,000 migrant households, with the sample conveniently drawn from the same cities as those included in the urban survey. The 2007 CHIP used a more systematic approach and intentionally chose the cities most populated by migrant families to be part of the migrant sample, yielding a sample size of 5,000 households from fifteen cities. In the unified 2013 CHIP national sample, rural residents constituted the rural sample, urban residents with an urban *hukou* constituted the urban sample, and urban residents with a rural *hukou* constituted the migrant sample. Because migrants were not intentionally sampled, their sample size was quite small (957 households) in 2013. Such a small sample size raises concerns about its representativeness, even though we applied statistical weights to render the results more representative. Because the migrant samples in different years were collected using different sampling techniques, the migrant samples may not be comparable over time. These concerns are beyond the scope of this chapter, but need to be kept in mind when interpreting the results and drawing policy implications. The analyses in this chapter are based on analysis of the separate, mutually exclusive urban, rural, and migrant samples. Table 11.1 presents the CHIP sample sizes for the three years that are examined in this study.

[Table 11.1 about here]

As noted above, to make the results based on the CHIP samples nationally representative, the CHIP team constructed sampling weights for each wave, taking into consideration the distribution of the population among the urban-rural-migrant subgroups and among the eastern-central-western regions. All analyses in this chapter apply these weights so that the results can be

considered nationally representative for each of the urban-rural-migrant subgroups. The CHIP team also constructed 3-level weights that took into consideration the distribution of provincial-level populations. Since this chapter does not address provincial-level income distribution, we chose not to apply the 3-level weights.

### **B. Measuring Social Benefits and their Effects on Economic Distance**

Taking advantage of the detailed income measures available in the CHIP data, we define household final income as the sum of market income, social benefit income, and private transfers, minus taxes, fees, and payments for social insurance contributions.<sup>1</sup> Market income includes wage income, net business income, property income, and rental value of owner-occupied housing. Social benefits include pensions, health insurance, unemployment insurance, supplementary income, social assistance, housing, food, and other in-kind benefits.<sup>2</sup> The inclusion of these various cash and in-kind benefits enables us to provide a comprehensive examination of the recent social policy changes as reflected at the household level. In addition, private transfers include remittance income sent back by household members working away from the home, elderly support, alimony, and other gifts from family and friends.<sup>3</sup> All incomes are calculated at the per capita household level and are adjusted by the provincial price deflators compiled by Brandt and Holz (2006), which we then updated to 2013.<sup>4</sup>

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<sup>1</sup> In some cases, the CHIP questionnaire did not specify whether transfer income was from public or private sources; these items are grouped as “other transfer income,” as explained below in the results section.

<sup>2</sup> Some of these social benefits are measured differently across the various waves and across the urban, rural, and migrant samples. They are explained below in the results section.

<sup>3</sup> Our income measure is largely consistent with the CHIP income measure, as described in Chapter 2, and it is broader than the NBS income measure. Compared to the CHIP income measure, our measure, including a more detailed list of social benefits, is consistent across waves.

<sup>4</sup> As these provincial price deflators are somewhat outdated, we attempted instead to use the official urban and rural CPIs to adjust the prices. The results are not reported here but are very consistent with our main



We measure the size of the total social benefits by the percentage of social benefit income in the household final income. This measure has the advantage of taking into consideration changes in the overall income level over time and gauging the relative contribution of the social benefit income. The structure of social benefits is measured by the percentages of specific social benefits in the household final income.

We compare the economic distances at the bottom (i.e., the 10th percentile) and at the top (i.e., 90th percentile) of the income distribution between the pre- and post-transfer incomes to understand the redistributive nature of the social benefits and to detect whether the 2002–2013 social policy reforms during were progressive (i.e., supporting the poor) or regressive (i.e., favoring the rich). We use eight income definitions to examine how the cumulative inclusion of each additional income component changed the economic distance between the rich and the poor within the respective urban, rural, and migrant populations. These income definitions are: 1.) market income (i.e., pre-transfer, pre-tax income); 2.) plus pensions; 3.) plus health insurance; 4.) plus social assistance; 5.) plus supplementary income and in-kind benefits; 6.) plus private transfers; 7.) plus other transfers; and 8.) minus taxes and fees (i.e., post-transfer, post-tax income). Because these benefits and transfers are added cumulatively, it is important to note that the order in which they are added will affect the results. A comparison between the results based on the first definition (i.e., market income, or pre-transfer, pre-tax income) and the last definition (i.e., final income, or post-transfer, post-tax income) reveals the redistributive effects of the entire set of social benefits and transfers.

Based on each income definition, we identify the 10th, 50th (i.e., median), and 90th percentile incomes and use bar charts to capture the economic distance between the rich and poor households within the urban, rural, and migrant populations respectively. The bottom end of the

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results.

bar has the ratio of the income of the households in 10th percentile relative to the median multiplied by 100 (i.e.,  $p_{10}/p_{50} \times 100$ ). The top end of the bar has the ratio of the income of the households in 90th percentile relative to the median multiplied by 100 (i.e.,  $p_{90}/p_{50} \times 100$ ). The length of the bar, reflecting the economic distance between these two ends, is calculated as the difference of the two (i.e.,  $p_{90}/p_{50} \times 100 - p_{10}/p_{50} \times 100$ ). An increase at the lower end of the bar and a reduction at the higher end of the bar due to social benefits and transfers indicate progressivity, whereas the opposite case reflects regressivity (Gao 2010; Garfinkel, Rainwater, and Smeeding 2010). By comparing the lengths of the pre- and post-transfers bars and understanding whether the shift occurred at the lower or higher end of the bar, we can understand the extent to which the social benefits helped reduce the economic distance between the rich and poor and whether the nature of the social benefits was progressive or regressive.

#### **IV. The Size and Structure of the Social Benefits**

Before delving into the analysis of the effects of the social benefits on the economic distance, we first present the results regarding the changes in the size and structure of the social benefits during the 2002–2013 period. As measured by the percentage of social benefit income in the household final income, the size of urban social benefits decreased from 2002 to 2013, whereas social benefits for rural and migrant families increased because of the social policy reforms that aimed to broaden social protection for these groups. However, the urban-rural-migrant gaps persisted, with the size of the urban social benefits still substantially larger than the rural and migrant social benefits. Across the three groups, pensions dominated the social benefit package, with noticeable gains by rural and migrant families in 2013. Rural families also gained transfer

income through the Building a New Socialist Countryside initiative.

[Table 11.2 about here]

Table 11.2 presents the changes in the size and structure of social benefits for the urban, rural, and migrant samples from 2002 to 2013 respectively. For urban families, the share of social benefits in household final income on average decreased from 26.92 percent in 2002 to 20.05 percent in 2007 and then to 17.46 percent in 2013. In all three years, pensions were the dominant social benefit for urban families, constituting 14.80 percent of urban household final income in 2002 and increasing to 16.97 percent in 2007. But in 2013 pensions declined to 15.61 percent of urban household final income. This fluctuation reflected the requirement that urban employees had to shoulder more pension contributions through the urban employee pension system, which included both social pooling and individual accounts. Health benefits, however, declined sharply for urban families, from 7.29 percent of the household final income in 2002 to 1.60 percent in 2007 and 0.45 percent in 2013. This is partly because that our measure of health benefits only captures the self-estimated cash value of medical care expenses covered by employers or the government and not the value of health insurance coverage that was available but not utilized or claimed. Therefore, our estimate of health benefits is an underestimate, especially for urban residents who on average had access to much broader coverage than their rural and migrant counterparts. Housing benefits also declined sharply from 2.68 percent in 2002 to about 0.78 percent in the later years, mainly due to the housing privatization that was launched in the 1990s and completed shortly after 2002. Other social benefits—including social assistance—remained a small proportion of household final income in urban China despite policy expansions during this period.

Unlike the trends for urban residents, however, rural and migrant families both gained

significantly from social benefits during this period, especially from 2007 to 2013, as indicated by Table 11.2. In 2002 social benefits only accounted for 0.71 percent of rural families' final income, but this figure rose to 2.13 percent in 2007. By 2013 social benefits constituted 6.42 percent of rural families' final income, a significant increase from the earlier years due to the expansion of social insurance and social assistance as well as the Building a New Socialist Countryside initiative. Specifically, pensions increased from 0.58 percent of rural household final income in 2002 to 3.59 percent in 2013, a sixfold jump over the eleven-year period. Health benefits also increased substantially, from 0.02 percent in 2002 to 0.73 percent in 2013, due to implementation of the NRCMS. Social assistance rose from 0.06 percent in 2002 to 0.51 percent in 2013, also a significant increase, mainly due to the implementation and expansion of the rural *dibao* since 2007. In 2013, supplementary income in the form of agricultural and livelihood subsidies, an income item that was nonexistent in previous years, made up 1.30 percent of rural households' final income.<sup>5</sup>

For the migrants, social benefits constituted 2.96 percent of household final income in 2002.<sup>6</sup> However, most of these benefits were employer-provided food and housing, which in effect were wages paid in-kind. The same items were included in the wage income for 2007 and 2013. Social benefits for migrants increased significantly, from 0.57 percent in 2007 to 2.39 percent in 2013. The biggest boost came from pension income, which increased from 0.02 percent in 2007 to 1.44 percent in 2013. Other in-kind benefits increased from 0.42 percent in 2007 to 0.72 percent in 2013.

Despite the significant gains in social benefits for rural residents and migrants during this

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<sup>5</sup> The CHIP 2007 rural survey did not ask about specific social benefits. Therefore, for 2007 we are only able to estimate the size and redistributive effects of total social benefits in the rural areas but not the specific items.

<sup>6</sup> Similarly, the 2002 CHIP migrant survey also did not ask about specific social benefits.

period, especially from 2007 to 2013, they still lagged considerably behind the gains of their urban peers. In 2013 an average of 17.46 percent of urban families' household final income came from social benefits, but that for rural families was only 6.42 percent and that for migrant families a mere 2.39 percent. It is important to note that not only did rural households receive social benefits that constituted a much smaller share of their final income than that of their urban peers but also their final household income was much lower. Indeed, across the three years, after adjusting for consumer price differences the final household income of rural families on average remained less than one-half that of urban families. A much smaller share in the amount of final household income meant that the value of rural social benefits, as opposed to that of urban social benefits, was much smaller. The persistent urban-rural-migrant gap in social benefits indicates the continuing challenges to achieving a truly unified and balanced social welfare system in China.

## **V. The Effects of Social Benefits on Economic Distance**

We now turn to the effects of social benefits on reducing the economic distance between rich and poor families in the urban, rural, and migrant samples respectively. Figure 11.1 presents the results for urban China. Overall, we find that market forces played a dominant role in widening the economic distance between the rich and poor during the 2002–2013 period, suppressing the redistributive effects of the social benefit package as a whole. Among the social benefits, pensions consistently helped narrow the economic distance over the years, whereas other social benefits—including health insurance, social assistance, supplementary income, and in-kind benefits—had little or no redistributive impact despite the recent social policy expansions in

these areas.

[Figure 11.1 about here]

First and foremost, both the pre- and post-transfer economic distance between the rich and poor continued to increase from 2002 to 2013. This was clearly driven by market forces. The pre-transfer economic distance between the rich and poor, as measured by the length of the bar, increased from 186 in 2002 to 199 in 2007 and 216 in 2013, a 16 percent increase during the eleven-year period. The social benefit transfers helped narrow the economic distance somewhat, but the post-transfer economic distance continued to rise over time, from 151 in 2002 to 159 in 2007 and 179 in 2013, a 19 percent increase during this period. These trends suggest that the disequalizing force of the market dominated the equalizing role of the social benefits during the 2002–2013 period in urban China, producing a much more unequal society as measured by the economic distance between the rich and poor.

Second, throughout the period, pensions functioned as the primary equalizing social benefit that consistently narrowed the economic distance between the rich and poor in urban China. In 2002 pensions reduced the economic distance by 35 (from 186 to 151) as measured by the length of the bar. That reduction increased to 37 in 2007 (from 199 to 162) but the increase was slightly less in 2013 at 34 (from 216 to 182). However, the redistributive effects of pensions still trumped that of any other social benefits or transfers across all three years.

In contrast, Cai and Yue's chapter in this volume finds that urban pension benefits were disequalizing rather than equalizing, a finding that is different from the strong and persistent redistributive role of urban pensions identified here. This discrepancy may be due to several reasons. First, in this chapter the pre-transfer income is market income only, which does not include pension benefits. Most retirees belonged to the bottom income groups based on the pre-

transfer income. The inclusion of pension income lifted the relative positions of retirees and narrowed the economic distance between the rich and the poor. Unlike our approach, Cai and Yue's decomposition method focuses on how each income component contributed to overall inequality, and pension benefits are treated equally as other income components. Second, this may also be because this chapter examines the urban, rural, and migrant populations separately, whereas Cai and Yue's chapter investigates the redistributive effects nationwide.

Third, all the other social benefits and transfers—including health insurance, social assistance (mainly *dibao*), supplementary income and in-kind benefits, private transfers, and other transfers that cannot be designated as public or private, as well as taxes and fees paid—had little impact on the economic distance between the rich and poor across all three years, suggesting that the social policy reforms and expansions during the 2002–2013 period in these areas were not effective in terms of income redistribution. Specifically, in 2002 health insurance helped lift the relative positions of the rich (from 199 to 204), mainly because health insurance was closely tied to employment status and position, and those with better jobs tended to have better health coverage. By 2007 and 2013, health insurance had a minor impact on economic distance. In 2002, supplementary income and in-kind benefits helped narrow the economic distance somewhat, mainly because the in-kind benefits tended to go to the less advantaged, but their redistributive role diminished to become almost non-existent by 2013. None of the other benefits or transfers played a noticeable role in changing the economic distance between the rich and poor in urban China during the period of this study.

Figure 11.2 presents the results of the effects of social benefits on the economic distance between rich and poor families in rural areas. Rural social benefits were regressive in 2002 but they became slightly progressive in 2007 and substantially progressive in 2013. In 2002, social

benefits—mainly pensions—helped increase the P10/P50 ratio from 43 to 44, thus lifting the relative position of low-income households, but they also raised the relative position of high-income households, increasing the P90/P50 ratio from 214 to 217. Taxes and fees were also regressive in 2002: they lowered the relative position of low-income families by 1 (from 44 to 43) and raised the relative position of high-income families by 3 (from 218 to 221). In 2007 rural social benefits became slightly progressive and shortened the economic distance bar by 1 (from 180 to 179).

[Figure 11.2 about here.]

The social policy reforms since 2007 changed the redistributive nature of rural social benefits to become substantially progressive by 2013. Overall, social benefits and transfers helped narrow the economic distance between rich and poor families from 252 to 206, a 46-point reduction, which was larger than the reductions due to urban social benefits in any of the three years under study. Among the social benefits, supplementary income and in-kind benefits in the form of agricultural and livelihood subsidies played the most significant redistributive role, shortening the length of the bar by 7 points. Pensions remained regressive, benefiting the rich more than the poor and slightly increasing the economic distance. Health benefits and social assistance each helped narrow the economic distance by 2 points. Private transfers had the largest redistributive role, narrowing the economic distance by 36 points. Such transfers included remittance income sent back by household members working away from home, elderly support, alimony, and other gifts from family and friends. It is noteworthy that these private transfers played a dominant redistributive role in rural China in 2013, probably as a supplement to the still inadequate redistributive role of public transfers.

Despite the larger redistributive effects of both private and public transfers in 2013 in the



rural areas, the post-transfer economic distance (206) was still substantially wider than that in earlier years (178 in 2002 and 179 in 2007), suggesting that market forces had become much more disequalizing by 2013, a trend that is similar to that in urban China. The pace of social policy expansions lagged behind the pace of market forces.

Figure 11.3 presents the results of the effects of social benefits on economic distances among migrants. Similar to the trends in the rural areas, migrant social benefits also changed from regressive in 2002 to progressive in 2013, although to a smaller extent as compared to the rural social benefits. In 2002 social benefits for migrants helped widen the economic distance between rich and poor families from 154 to 162, an eight-point increase. In 2007, social benefits played a minimal role in impacting the economic distance, whereas private transfers helped lift the relative position of rich families. In 2013 health insurance helped narrow the economic distance by 1 point (from 166 to 165), private transfers reduced the economic distance by 2 points, and taxes and fees further reduced the economic distance by 4 points. Social benefits still played a very limited redistributive role, but they did become progressive.

[Figure 11.3 about here]

## **VI. Conclusion and Discussion**

Using data from the 2002, 2007, and 2013 CHIP surveys, this chapter examines the effects of a series of social policy reforms on the economic distance between the rich and poor among urban, rural, and migrant families during this period. These social policy reforms included expansion of social insurance and social assistance programs to extend coverage from urban employees to urban non-employees, rural residents, and migrants, provision of agricultural and livelihood

subsidies to rural residents through the Building a New Socialist Countryside initiative, and the enactment of the 2008 Labor Contract Law to offer greater social protection to migrant workers.

We find that pensions in urban areas consistently helped narrow the economic distance among urban households over the years, whereas other social benefits—including health insurance, social assistance, supplementary income, and in-kind benefits—had little or no redistributive impact. Both rural and migrant social benefits changed from regressive in 2002 to progressive in 2013. In the rural areas, supplementary income and in-kind benefits, in the form of agricultural and livelihood subsidies, played the most significant redistributive role among all social benefits in 2013, whereas private transfers also helped narrow the economic distance substantially. For migrants, health benefits and taxes and fees helped narrow the economic distance in 2013, although to a lesser extent as compared to the rural social benefits.

Despite the series of social policy expansions during this period, in both urban and rural China market forces still played a dominant role in widening the economic distance between the rich and poor, which trumped the redistributive effects of the social benefits. These results suggest that China's future social policy reforms will face continued challenges in terms of attempting to unify the imbalances in the urban-rural-migrant systems and to keep pace with the disequalizing market forces. Urban social benefits remain larger in size, more comprehensive in coverage, and they play a consistently larger redistributive role as compared to those for rural residents and migrants. It will take strong political will and a serious fiscal commitment to address the disparities in social protection among the urban-rural-migrant populations and to respect their equal rights.

Meanwhile, it is alarming that the levels of the pre-transfer income inequality in both urban and rural areas continued to rise and that the expanding social benefits were unable to

sufficiently curtail this trend. Despite a decline in national inequality from 2007 to 2013, an underlying factor being the narrowing of the urban-rural gap, the rising income inequality within the respective urban and rural areas is of critical concern and may threaten social stability and harmony. Given China's unique blend of socialist rule and state capitalism, an elevated level of income inequality may have more direct and serious political and social consequences in China than it does in other countries. This is partly why the government promoted the social policy reforms as part of an effort to provide a basic level of social protection and an equalizer across the urban-rural boundaries and income groups. The balancing act between economic growth and social harmony remains a serious challenge for current and future administrations in China.

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**Table 11.1. Sample sizes of the China Household Income Project (CHIP) survey, by year**

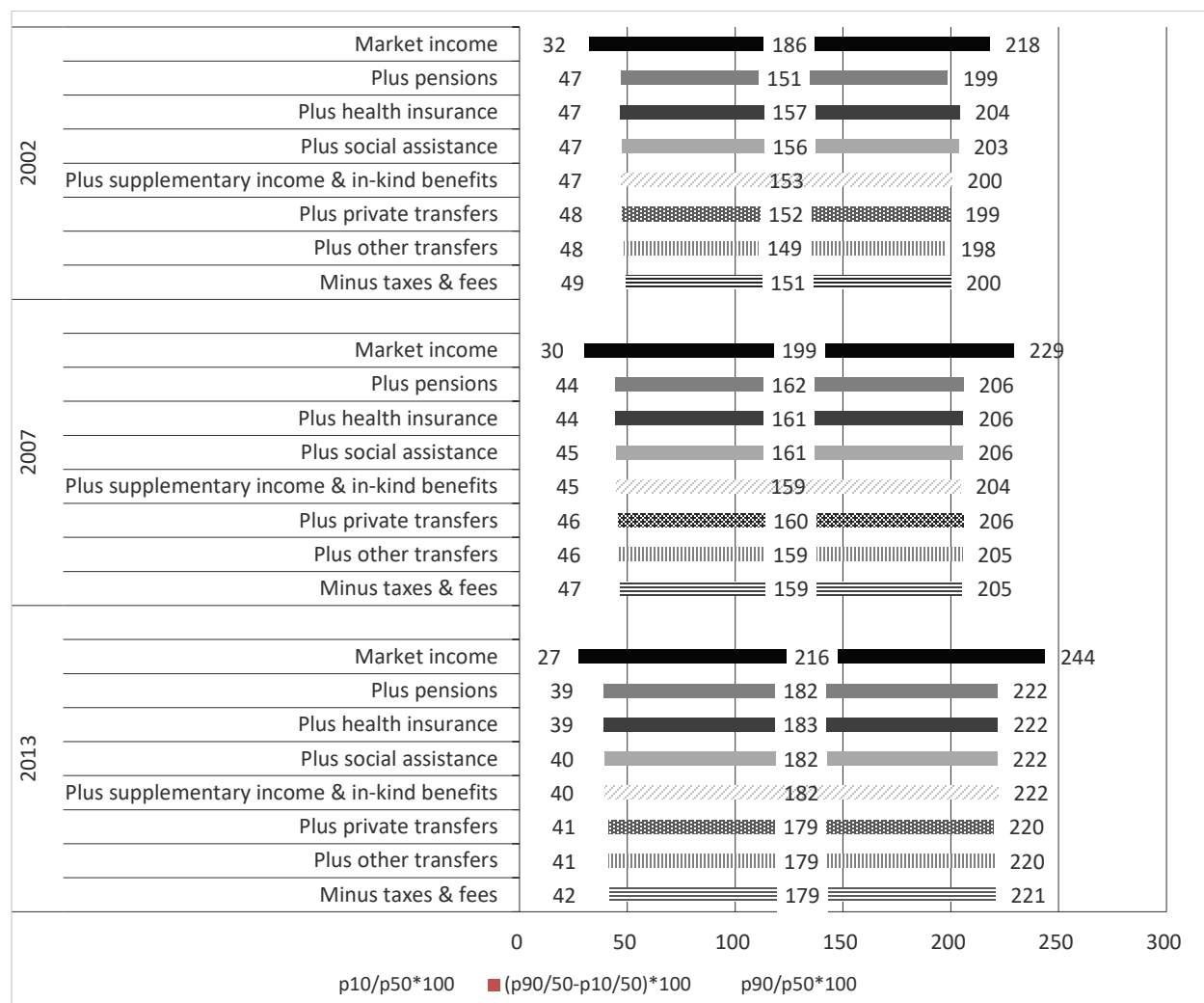
	2002	2007	2013
<u>Urban</u>			
Households	6,835	10,235	6,762
Individuals	20,632	30,340	20,414
Provinces	12	16	15
<u>Rural</u>			
Households	9,200	13,000	10,456
Individuals	37,928	51,847	39,869
Provinces	21	16	15
<u>Migrants</u>			
Households	2,000	5,000	957
Individuals	5,318	8,404	2,609
Provinces	12	9	15

**Table 11.2. Size and structure of social benefits measured as a percentage of household final income (%)**

	Urban			Rural			Migrants		
	2002	2007	2013	2002	2007	2013	2002	2007	2013
Pensions	14.80	16.97	15.61	0.58		3.59	0.02		1.44
Health	7.29	1.60	0.45	0.02		0.73	0.11		0.07
Unemployment insurance	0.27	0.15							
Social assistance	0.53	0.16	0.18	0.06		0.51	0.01		0.02
Supplementary income	0.69		0.12			1.30			0.08
Housing	2.68	0.77	0.79			0.01			0.05
Food	0.54	0.32							
Other in-kind	0.13	0.07	0.31	0.05		0.28		0.42	0.72
<b>Total Social Benefits</b>	<b>26.92</b>	<b>20.05</b>	<b>17.46</b>	<b>0.71</b>	<b>2.13</b>	<b>6.42</b>	<b>2.96</b>	<b>0.57</b>	<b>2.39</b>

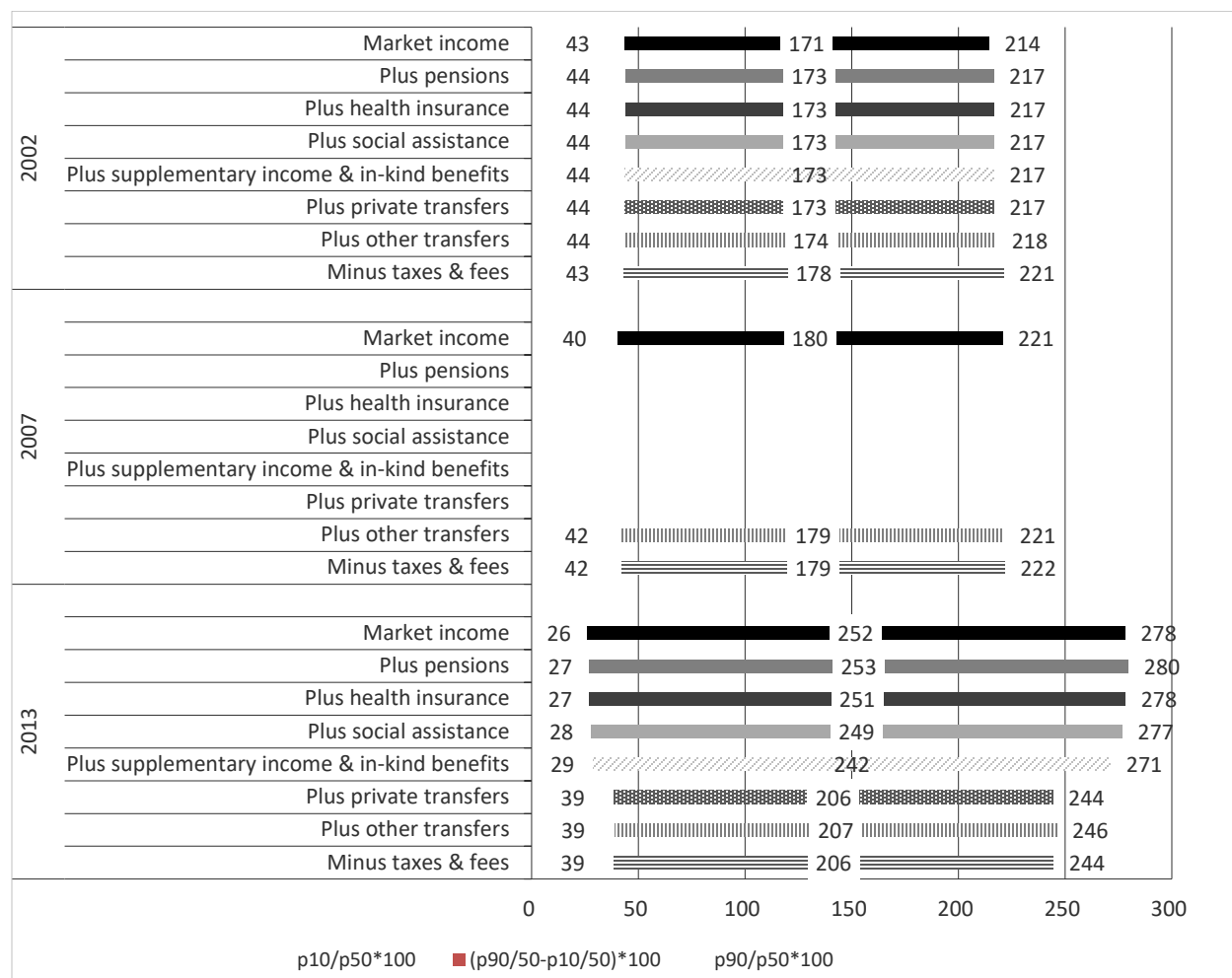
*Notes:* Household final income refers to post-transfer, post-tax income. All income and social benefits used for calculating these results are measured as household per capita values.

**Figure 11.1. Impact of social benefits on the economic distance between low- and high-income households in urban China**



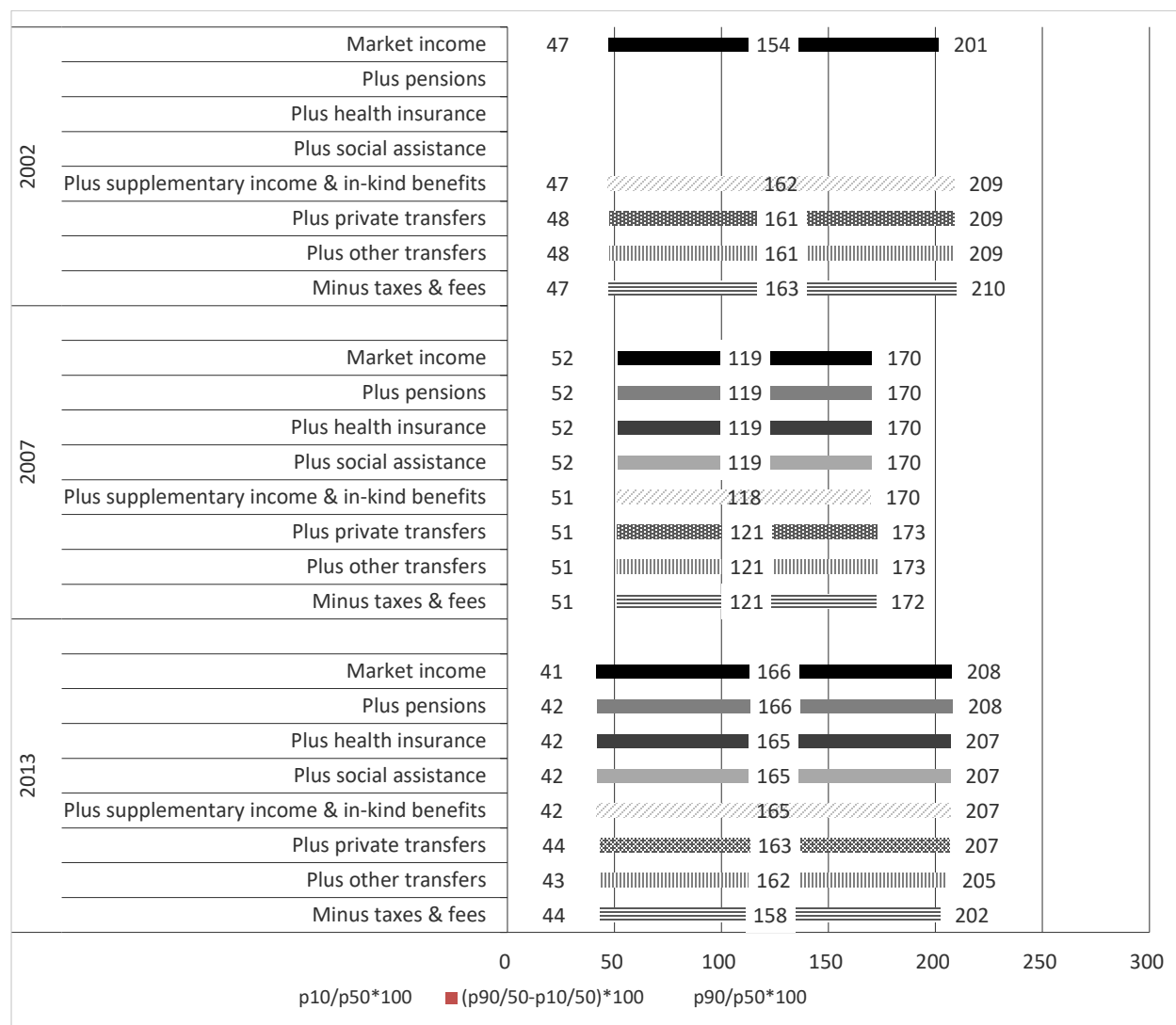
*Notes:* For each income definition, the bottom end of the bar gives the ratio of the household income in the 10th percentile relative to the median multiplied by 100 (i.e.,  $p_{10}/p_{50} \times 100$ ). The top end of the bar gives the ratio of the household income in the 90th percentile relative to the median multiplied by 100 (i.e.,  $p_{90}/p_{50} \times 100$ ). The length of the bar reflects the economic distance between these two ends and is calculated as the difference between the two (i.e.,  $p_{90}/p_{50} \times 100 - p_{10}/p_{50} \times 100$ ).

**Figure 11.2. Impact of social benefits on the economic distance between low- and high-income households in rural China**



*Notes:* For each income definition, the bottom end of the bar gives the ratio of the household income in the 10th percentile relative to the median multiplied by 100 (i.e.,  $p_{10}/p_{50} \cdot 100$ ). The top end of the bar gives the ratio of the household income in the 90th percentile relative to the median multiplied by 100 (i.e.,  $p_{90}/p_{50} \cdot 100$ ). The length of the bar reflects the economic distance between these two ends and is calculated as the difference between the two (i.e.,  $p_{90}/p_{50} \cdot 100 - p_{10}/p_{50} \cdot 100$ ).

**Figure 11.3. Impact of social benefits on the economic distance between low- and high-income households among rural-to-urban migrants in China**



*Notes:* For each income definition, the bottom end of the bar gives the ratio of the household income in the 10th percentile relative to the median multiplied by 100 (i.e.,  $p_{10}/p_{50} \times 100$ ). The top end of the bar gives the ratio of the household income in the 90th percentile relative to the median multiplied by 100 (i.e.,  $p_{90}/p_{50} \times 100$ ). The length of the bar reflects the economic distance between these two ends and is calculated as the difference between the two (i.e.,  $p_{90}/p_{50} \times 100 - p_{10}/p_{50} \times 100$ ).