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## Unequal Distribution of Wealth in China: Do Inconsistencies in Government Policies Play a Role?

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## 1. Introduction

China's widening gap in the distribution of wealth following its transition toward a market economy has been the subject of debate among many scholars. It is widely agreed that the government plays a large role in the distribution of wealth, but how and to what extent is where most scholars diverge.

Gul and Lu (2011) argue that despite certain attempts to mitigate disparities, the Chinese government has negatively affected the distribution of wealth throughout the country. They suggest that the move toward a more capitalistic economy has increased competition between private and state owned enterprises, which in turn creates more differences in personal income. One of the specific policies they examine is the Hukou system, which was the housing policy that divided the economy and segregated urban and rural labor markets. This policy restricted labor mobility, thus preventing rural residents from opportunities to earn higher wages and denying them access to the network of urban welfare. Aside from the policy itself, they argue that various housing reforms have also had a negative effect on equality. Moving from a unitary housing authority to various public institutions and state owned enterprises have created an array of unintentional outcomes such as poor investment structure and unfair distribution of housing units (Gul & Lu, 2011c, 46). Another cause they examine is the flaw in the income redistribution system. Rural incomes are generally low while fees and taxes are relatively high. In cities incomes are higher while benefits and subsidies are more numerous (Gul & Lu, 2011a, 102). Lastly, they argue that growing inequality is largely rooted in urban biased growth strategies. State investment is disproportionately applied to urban industrialization, even though "the rural population represents 70 percent of the total population and agriculture employs over 50 percent of the labor force" (Gul & Lu, 2011a, 103).

The topic of policies that are biased toward the urban sector is further explored in Dennis' (1999) study on urban-based policies and rising income inequality in China (p. 306). In his study he uses household survey data from China's Statistical Bureau to examine the causes of rising inequality. Through his analysis<sup>1</sup>, he specifically examines inequality within urban areas, within rural areas, and between the two. His findings suggest that the sectoral disparity between urban and rural areas contributes the most to overall inequality. After discussing the immense role the alarmingly large gap between rural-urban wealth plays in overall inequality, he presents the idea that this disparity still exists as a result of government policies that are clearly biased towards the urban sector. He shows this by pointing out many advantages urban residents enjoy that are widely

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<sup>1</sup> Analysis used generalized entropy measures and Gini ratios

unavailable to rural migrants. For instance, state owned enterprises provide housing for employees and only permanent workers are able to receive health insurance and pensions. In addition to institutional barriers preventing rural migrants from having equal services and opportunities, he discusses how government expenditures and investments are disproportionately utilized in urban areas. Through the many examples discussed connecting government policies and rural-urban income inequality, Dennis inadvertently reveals some inconsistencies in what the policies seek to achieve and their affect on the widening income gap.

Another issue that directly affects the distribution of wealth is the availability and quality of educational attainment. Scholars widely agree that access to basic education has improved significantly within the last 40 years, however unequal access continues to be a severe problem and adds to China's widening wealth gap. Adams and Hannum (2009) look beyond only education policy and argue that as a result of the decentralization policies that started in the mid 1980s, costs increased for social services, which made it significantly harder for people to afford compulsory education in poor regions. They describe a direct link between changes in welfare policy decisions and descent into poverty. Specifically, they link the privatization and decentralization of health care to rising health care costs which has been known to bring people into poverty. The higher the health care costs, the less money there is available for educational attainment. They validate this through an analysis of a survey of households in Guizhou and Shanxi Provinces that showed that households with hospitalization had 26 percent less expenditures in education compared to households with hospitalization<sup>2</sup> (Adams & Hannum, 2009, p. 168).

Aside from incomes and costs, barriers to equal education access in China can be found between 6 different groups: between regions, rural and urban areas, types of schools, social classes, gender, and ethnicities (Wang, 2011a, p. 227). Wang proposes the idea that the unequal distribution of access to higher education between regions is a result of the provincial enrollment policy, which according to her has a poor rational basis and perpetuates regional and social differences that are already in existence. In regards to uneven access between rural and urban areas, she suggests that the difference lies in the quality of education offered as opposed to the amount of schools. Children raised in rural areas are more likely to attend regional institutions and enter less common programs because of lower quality schooling during childhood than that of urban residents (Wang 2011a, p. 237). The social class divide is argued to be a result different approaches that each social class has to the college entrance examination (Wang, 2011a, p. 239). As far as gender disparities are concerned, she attributes differences in enrollment

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<sup>2</sup> Hospitalization in what context was unclear.

between males and female to a preconceived societal notion that men's education is more important than that of women's (Wang, 2011a, p. 243). Overall, Wang (2011a) shows that while differences in educational opportunities have been gradually declining, differences are still apparent between the 6 different groups mentioned earlier. She calls for a shift from focusing on the amount of schools available to the quality of education provided in order to promote truly equal opportunities.

To this date, many scholars have examined the causes of the increasingly unequal distribution of wealth from a specific field of study. When policy is involved in such discussions, it generally only regards specific sets of policy and its affect on a certain aspect of the wealth divide. This paper intends to take a step back and examine the progression of policy in housing and education since right before the reform up to the early 2000's and how each ones implications affects the effectiveness of others. This paper discusses how the inconsistency in government policies has largely affected China's increasingly unequal distribution of wealth in a negative way. This is explored in a comprehensive overview through reviewing various policies and lack of policies regarding the market reforms in 1978, specifically, those associated with housing and education policy.

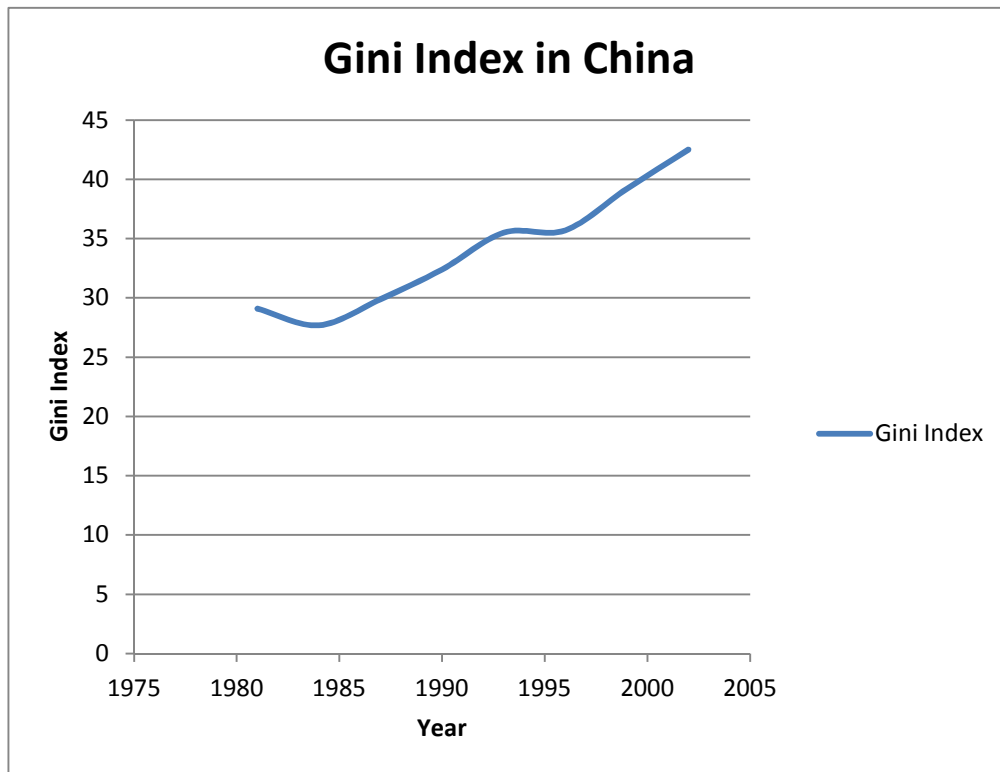
## **2. Switch to Market Economy and Effects of an Unequal Distribution of Wealth**

Although the tremendous growth China has seen in the last half-century has improved the standard of living for around 1.2 billion people (Wong & Lu, 2002, p. 370), it has also precipitated the substantial increase in the unequal distribution of wealth. This has eventually caused China to have more citizens that live below absolute poverty than that of states with similar per capita income (measured by purchasing power parity) (Liang, 2009, p. 389). For this reason, many scholars propose that the transition from a planned to market economy is the reason why China has experienced such a large increase in inequality. Bian and Logan (1996) argue that the ability to participate outside government run sectors have allowed people to earn more than would be possible in a planned system, therefore leading to inequalities (p. 743). Similarly, Kostello and Szelenyi (1996) suggest that growing inequality is a result of the transition to a capitalistic system (p. 1093). While these propositions seem to be valid, there is much more to the equation than simply the type of market system China uses. The transition has precipitated the changes in policies that will be discussed, however the inconsistencies of the changed policies played a large role in how inequality occurred to such a large extent. In the case of China, it seems that while the switch from a socialist to a more capitalistic system has created many changes in the structure in which markets operate and redistribution occurs, the state remains

to play a large role in how this all plays out through its power in state owned enterprises and the outcomes of its changes in policies. According to power persistence theories, stratification mechanisms in place under former redistributive economies are maintained even with the transition to a more capitalist economy (Xin, 2009, p. 85). While the causes of inequality change with the transition, the culprit, that is the government, remains the same.

Although different facets of inequality will be discussed throughout this paper, one set of data that is useful to examine when judging the unequal distribution of wealth in a country is the Gini index, which "measures the extent to which the distribution of income or consumption expenditure among individuals or households within an economy deviates from a perfectly equal distribution" (World Bank Website).

**Figure (1):**

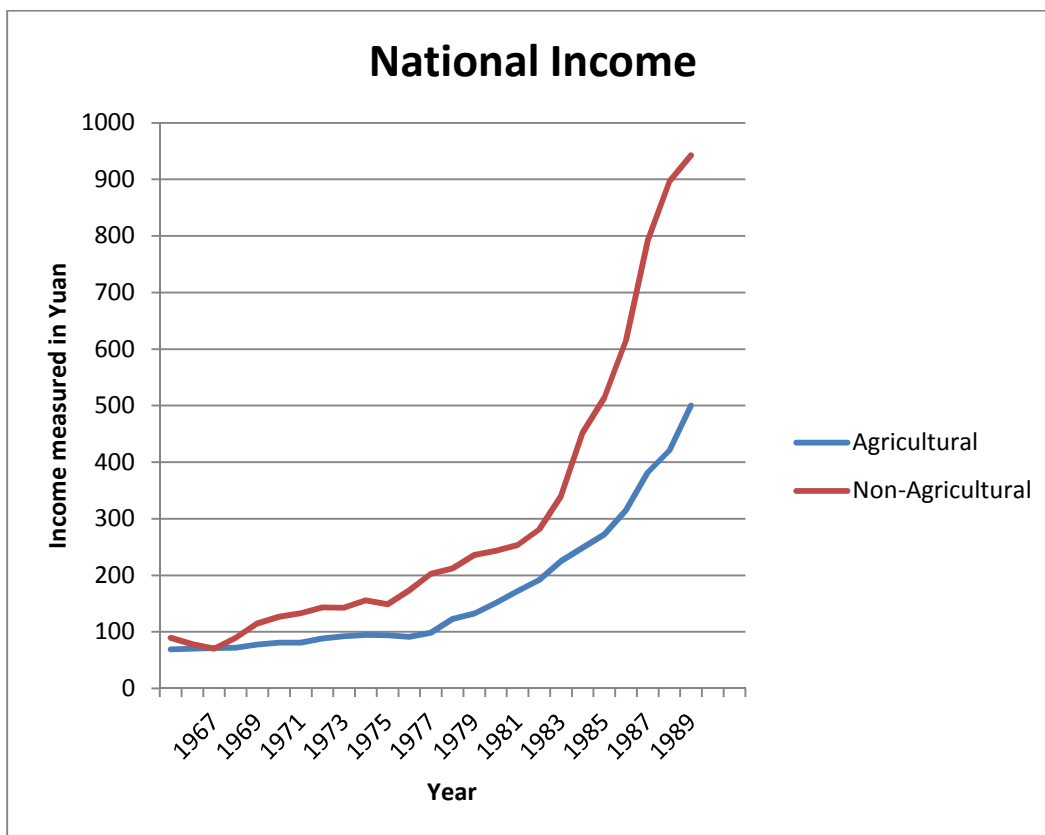


*Source: The World Bank*

Although data is not available for every year and for prior to the economic reforms in the late 70's, it is clear that overall inequality in China has been steadily rising. Figure (1) shows the Gini coefficient rising from 19.1 in 1981 to

42.5 in 2002. In less than 25 years, China managed to become one of the most unequal societies in the world (Wan & Zhu, 2012, p. 90). This inequality exists in many areas, most prominently between rural and urban areas, coastal and inland areas, between men and women, and different ethnicities. This paper will touch on a bit of each but primarily focus on the rural-urban divides, since it is one of the most apparent. The graph below shows the rise in income in both agricultural which will represent rural areas and non-agricultural<sup>3</sup> which will represent urban areas from 12 (1966) years before the reform to 12 years after (1990).

**Figure (2):**



*Source: China Statistical Yearbook 2000*

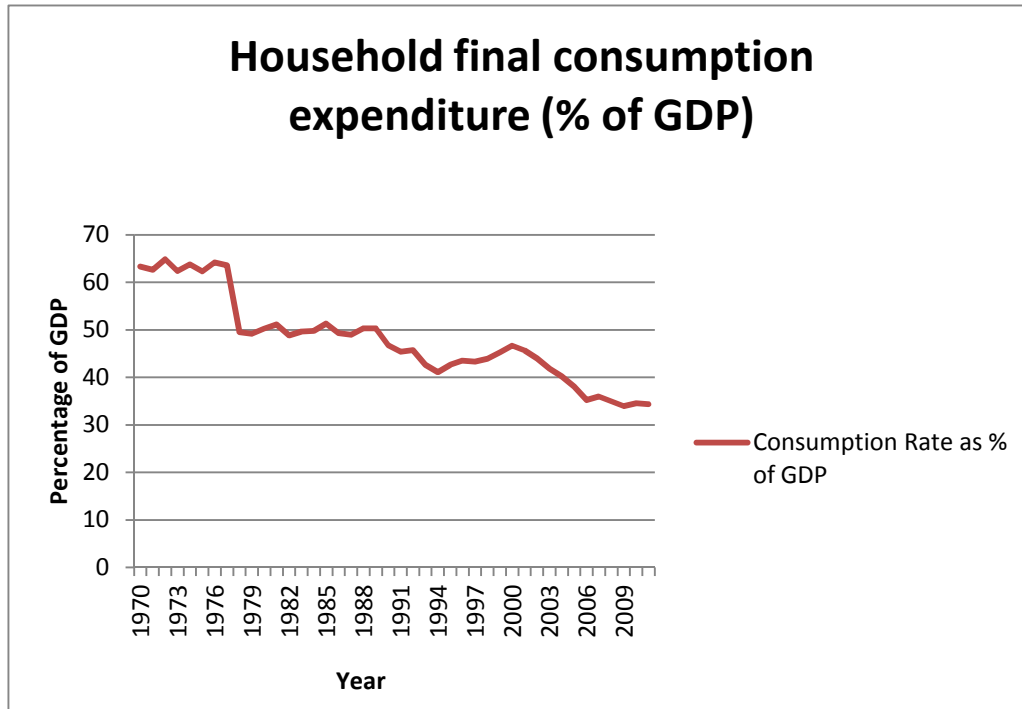
From the graph above, one can see that starting in the mid 80's incomes between the agricultural rural and urban sectors began to diverge, with non-agricultural income increasing at a faster rate than non-agricultural. In 1966 the

<sup>3</sup> Non Agricultural consists of the national income of industry, construction, transportation, and commerce combined

difference between urban and rural incomes was 20.2 Yuan while in 1990 it was 442.9 Yuan, showing a considerable rise in inequality. Due to a lack of availability of data, the graph above only shows the beginning of the divergence between rural and urban incomes, however an array of secondary sources confirm that this divide has continued to worsen. The inconsistency of government policies contribution to the widening gap between rural and urban incomes shown in Figure (2) will be discussed in following sections of the paper. While the distribution of wealth has been displayed solely in the context of income thus far, this paper will interpret wealth in much broader terms, including topics such as access to welfare benefits and property.

After examining some of the ways inequality can be measured, it is natural to ask why does this matter and what are the effects? While Figure (2) shows a positive result of market reform through the increase in incomes in both rural and urban areas, the rapid increase in inequality displayed as well cannot be ignored. A large degree of inequality has damaging effects and threatens the health of a country's economy and society. In the case of China, an increasing gap in the wealth distribution has lead to low domestic demand, threatens social and political stability, and affects the inability of those at the bottom to afford social investment (Wan & Zhu, 2012, pgs. 90, 91, 92) A better understanding of the implications of inequality in China will provide insight into what needs to be done in order to improve the current state of the distribution of wealth, while stressing its importance.

A large gap in the distribution of wealth suppresses private demand as a result of the poor not being able to afford basic consumption while the wealthy spend a smaller portion of their income, saving more (Wan & Zhu, 2012, p. 92). According to the law of diminishing marginal propensity of consumption and Keynesian consumption theory, people at the richer end of the wealth distribution are more inclined to save money while people at the poorer end are more likely to spend very little (Gao & Lu, 2011, p. 104). As a result, China's rising degree of inequality has a negative effect on both the national mean consumption rate and household consumption growth (Lu & Gao, 2011, p. 104). As you can see in Figure (3) The share of the household consumption rate of GDP changed from 49.49 percent of GDP in 1978 to 34.38 percent in 2011. The decline in household consumption's share of GDP shows that China's growth is primarily driven by exports and investment (Gong & Li, 2011, p. 325). This leaves China's growth at the mercy of outside forces.

**Figure (3):**

*Source: World Bank*

The declining amount of domestic demand shown through household consumption rates is unhealthy for China because it weakens economic growth, which in turn leads to "surplus liquidity, investment inefficiency and economic instability" (Wang, 2011b, p. 1). Aside from the unequal distribution of wealth, Chinese Household Consumption has been negatively affected by the uncertainty caused from the switch from a planned to a market economy (Xu, Dai, & Zhong, 2010, p. 344). With economic reforms across the board, consumers became unsure about the rate of their future consumption. This caused them to spend less and save more in order to be able to afford services such as health and housing that were previously provided by the government (Xu, Dai, & Zhong, 2010, p. 344). Overall, China's consumption pattern is similar to that shown in Engle's law, that is, the proportion of spending on necessary items usually decreases as income increases (Wong & Lu, 2002, p. 373). With incomes rising in most sectors, the distribution of wealth is negatively affected. This combined with the people living in poverty consuming very little maintains China's decreasing household consumption.



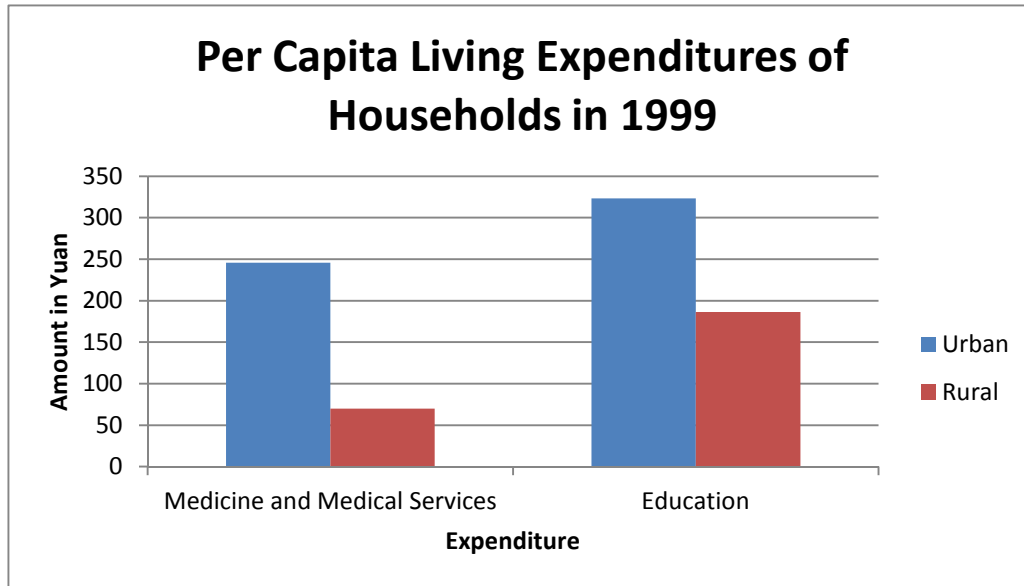
Another prominent consequence of a high degree of inequality is its negative effect on social and political stability. China's history is wrought with uprisings caused by a general feeling of unfairness. Through examining the nature of inequality since the market reforms, it is clear that China is prone to such instability once again. Nearly 75% of minorities reside in poor western regions, which houses 22% of the population and domestic migrants are becoming increasingly dissatisfied with government at the local level according to a recent study (Wan & Zhu, 2012, p. 90). This could lead to ethnic tensions, a lack of confidence in government policies (worsening the already inconsistent role of government policy plays in distribution of wealth), and pose a threat to China's sovereignty and unity. Aside from social unrest, rising inequality could lead to an increase in crime rates (Gao & Lu, 2011, p. 120). One study showed property infringement cases increase as urban-rural per capita income ratio rose (Gao & Lu, 2011, p. 120). Such internal problems have wide reaching effects, such as a decreasing investment and discouraging economic activity (World Bank on Poverty).

Another side effect of a large degree of inequality in China is that the poorer people are not able to afford social investment (Wan & Zhu, 2012, p. 91), in areas such as education, housing, and health. This makes it very difficult to reduce the level of poverty and also hinders national prosperity, for such social investments have spillover effects that make its negative impact much broader (Wan & Zhu, 2012, p. 91). Figure (4) shows the difference between urban and rural areas in per capita expenditures in medicine, medical services, and education in 1999.

**Figure (4)<sup>4</sup>:**

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<sup>4</sup> Consists of rural and urban areas in 31 regions of China (data was available on 31 regions)



*Source: China Statistical Yearbook 2000*

It is clear that people in urban areas spend a significant amount more than the traditionally poorer rural regions at a difference of 175.57 Yuan in medicine and medical services and 137 Yuan in education. This contributes to the ongoing cycle that can only be stopped with a reduction of barriers from receiving the social capital needed to lift them and their family out of poverty. This effect and its correlation with inconsistency in government policies will be further explored throughout the paper. Aside from those at the poor end of the distribution not being able to afford social investment, increasing inequality and its relationship with growth prevents poverty reduction (Wan & Zhu, 2012, p. 91). When inequality is high, as it is in China, the impact growth has on reducing poverty is smaller than it would be in a more equal society, and rising inequality also offsets the aspects of growth that reduce poverty (Wan & Zhu, 2012, p. 91). As a result of this, redistribution could be viewed as more important than growth as a method of reducing poverty in China (Wan, 2006, p. 21).

The impacts discussed resulting from the unequal distribution of wealth are very important to the success and future outlook of China. The combination of low domestic demand, threats to social and political stability, and the inability of those at the bottom to afford social investment create a difficult situation in China's efforts to become and economically strong 'harmonious society.' Now that the effects of an unequal distribution of wealth and therefore the importance of a more equal society are established, the role of government policies in the education and housing sector will be explored.

### **Part 3: Education**

#### *Primary and Secondary*

Considering the strong correlation between educational attainment and higher income (Wei, 1999, p. 167), the education system in China is very important topic when studying the distribution of wealth in a state. Following the economic reforms in the late 70's, the economic returns to education in the urban sector have risen significantly, and nearly tripled between 1992 and 2003 (Adams & Hannum, 2009, p. 156). In rural areas on the other hand, education became the main factor behind one's ability to find off-farm jobs by 2000 and each additional year of schooling increased wages by 6.4 percent (Adams & Hannum, 2009, p. 156). The increasingly important role of education in one's eventual economic status leaves those who lack basic schooling very prone to living a life of poverty, therefore contributing to the China's unequal distribution of wealth. Fortunately, access to all levels of education had risen significantly since the economic reforms in the late 70's. However, access to educational opportunities remains very unequal with disparities existing between different ethnic groups, genders, urban and rural areas, coastal and inland areas, and between provinces. My research focuses on the inconsistent impact of policy on education, specifically between the rural and urban sector, since it is one of the more prominent issues.

The disparities in education between rural and urban areas stem from a multitude of policies that are specifically prejudiced towards urban areas. Such policies have direct effects on income, which therefore affects the distribution of wealth and the ability for parents to afford to send their children to school. Dennis (1999) argues that "...urban biased policies and institutions, including labor mobility restrictions, welfare systems, and financial policies of inflation subsidies and investment credits to the urban sector, are responsible for the long-term rural-urban divide and the recent increases in disparity" (p. 306). Despite a series of reforms to reduce the urban-rural division such as increases in procurement prices for agricultural products, the implementation of household responsibility systems, and the ease of restrictions on labor mobility in rural areas to non-agricultural sectors and employment in urban areas, urban residents remain significantly advantaged due to the presence of certain policies (Dennis, 1999, p. 308). For example, urban residents receive far more welfare benefits than rural migrants. State-owned enterprises and other government agencies still are able to provide housing as well as health insurance and pensions for their permanent employees, leaving rural migrants to cover these costs on their own (Dennis, 1999, p. 309). Additionally, childcare and elementary and middle school educations are not available to the children of migrants that lack the ability to obtain urban registration (Dennis, 1999, p. 309). They end up paying up to three times the

amount that locals pay for the often lesser quality education through 'temporary student fees'. (Gul & Lu, 2011b, 160). Moreover, they are often segregated into different classes because of urban parents fear that migrant children would take away from their own child's education (Gul & Lu, 2011b, 160).

Aside from the lack of benefits rural migrants receive in urban areas, the disparity is also a result of the government's financial transfer programs, which are biased towards the urban sector. The 8.5 percent inflation experienced between 1985 and 1992 affected the entire country, however the investments and government spending that was held responsible for this inflation were allocated to urban areas disproportionately to rural areas (Dennis, 1999, p. 309). Furthermore, discretionary policies have been found to negatively affect the income of people living in rural areas. For instance, following inflation in the late 80s, discretionary policies were implemented that constricted investment credits mainly to rural areas in 1989 employment (Dennis, 1999, p. 309). This led to a reduction in township and rural enterprises as well a drop in employment and real output. On the other hand, from 1989-1992 real output of state owned enterprises rose as well as employment (Dennis, 1999, p. 309). From these examples it is clear to see that policies biased toward the urban sector create severe disadvantages for rural residents, which either directly or indirectly worsen the unequal distribution of wealth.

Through the increases in urban subsidies, investments, and credits, the rural are left severely disadvantaged when it comes to being able to afford education for their children because of their lower income. In a study done on the educational barriers in rural areas of Gansu, where 76 percent of the population lives in rural areas, one of the top reasons for children leaving school according to village leaders, mothers and children was the inability to afford costs, such as school supplies and fees charged by the school in order to stay open (Adams & Hannum, 2009, p. 161). The difficulties of staying school can be seen when looking at the percentage of dropouts in any given year. In 1990, an average of 1.4% and 4.9% of students dropped out of primary school in urban areas and rural areas respectively (China Statistical Yearbook 1991).<sup>5</sup> In conjunction with this, about one-fourth of children stated that they didn't attend school because they were needed at home, suggesting that the opportunity cost of them going to school

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<sup>5</sup> Calculated by averaging the difference of students at the beginning of the year and end of the year in rural areas (Inner Mongolia, Anhui, Jiangxi, Guangxi, Hainan, Guizhou, Tibet, Shaanxi, Gansu, Qinghai, Ningxia, Xinjiang) and urban areas (Beijing, Tianjin, Hebei, Shanxi, Liaoning, Jilin, Heilongjiang, Shanghai, Jiangsu, Zhejiang, Fujian, Guangdong). How area was determined rural or urban is discussed on page 23.

were just too high (Adams & Hannum, 2009, p. 161). This combined with the disequalizing effects of the funding policy has put poor rural families in a tough position. This is especially damaging considering the lack of education is perpetuated for future generations. As former head of the Education Commission of Hunan Province put it, "a lack of education is the beginning of a vicious circle that leads to social inequality and traps people into poverty" (152).

Although there are policies in place that are specifically intended to reduce the income gap between rural and urban areas, the presence of urban biased policies either lessen or prevent them from having any positive affect. Considering the importance of a more equal society to the success of China, each policies' potential affect on the distribution of wealth needs to be examined before they are implemented to insure policies targeted towards reducing the problem can take full effect.

One of the more important laws that have the potential to mitigate education disparities is the Compulsory Education Law. Established in 1986, it intended to expand education by providing nine free years of education to all children. As the law states, it also intended to "improve the quality of instruction and enable children and adolescents to achieve all-round development--morally, intellectually and physically--so as to lay the foundation for improving the quality of the entire nation and for cultivating well-educated and self-disciplined builders of socialism with high ideals and moral integrity" (Compulsory Education Law). Starting at age 6, children were to begin school regardless of sex, race, or nationality (Compulsory Education Law). In theory, this law would greatly lessen the gap in China's distribution of wealth. Guaranteeing a basic education for everyone in China puts those children who didn't have access schooling before the law in a better position to further their education and obtain a better job with higher income. However, this has not occurred to the extent it should have. As a result of drastic and frequent changes in it's funding and the presence of 'mixed changes,' the compulsory education law is wrought with inefficiencies. Frequent changes have prevented the law from lessening inequality through creating difficulties with implementation and wasting financial resources while the presence of 'mixed changes' have weakened funding.

Within the last 20 years, Chinas Compulsory Education Policy has experienced many adjustments. The time between major changes in the compulsory education laws funding policy range between .5 years to 8.3 years, with an average of every 2.5 years (Wei, 2008, p. 118). This leads to a number of issues regarding fairness, effectiveness and efficiency. The table below shows the amount of time that passes between each major change in the compulsory education policy from 1986-2006.

**Figure (5):**

Major policy changes from 1986-2006	Amount of time between changes in years
Jul '86 - established "township input"	
Nov '94 - Taxsharing system	8.3
Jan '00 - Tax and fee reform	5.2
May '01 - Responsibility handed to local governments	1.3
Jul '04 - One fee system	3.2
Mar '05 - 2 remission and one subsidy	0.7
Dec '05 - Rural tuition and fees waived	0.8
Jun '06 - New Compulsory Ed. Law	0.5

Source: (Wei, 2008, p. 117)

As the table shows, the more time passes; changes in policy seem to occur more frequently. In general, numerous rapid changes to policies tend to lead to the policies unfairness because "policy impartiality requires a series of explicit, fixed, universal, objective conduct rules, if a policy is changed arbitrarily and frequently, which will have an impact on the distribution of authority of wealth, power, social status, opportunities to lead to unfair results" (Wei, 2008, p. 118). This generalization proves to be true in the case of drastic changes in China's compulsory education policies. The changes listed mostly deal with the source of funding and where the responsibilities of certain duties lie and were formulated upon realization that adjustments needed to occur. They essentially provide the structure of how the law should be funded, ran, and maintained.

One of the negative side effects to the radical changes in funding policy includes creating issues for the implementation of each new policy. As Wei (2008) argues, "educational policy gains recognition and builds consensus on the basis of deep interpretation. Only in this way can it be implemented actively, properly and effectively" (p. 118). When policy is changed so often, it is difficult for education policy makers and implementers to fully understand and contextualize what exactly the changes mean, making it more difficult for the goals of the new policy to be implemented successfully (Wei, 2008, p. 118). With such a short amount of time between changes, the intended result of each change is not reached because there is a lack of time for policy reorientation to occur (Wei, 2008, p. 118).

Another negative effect of rapid policy change is that it is very cost inefficient in a couple of ways. One way is through the costs associated with

terminating a policy that is still in effect. The legal procedures required do so costing money, and when a policy is terminated before its goal has been reached the resources already put into that policy going to waste. Another way it is cost inefficient is because both formulating and changing a policy are very expensive (Wei, 2008, p. 118). When the policy changes frequently, costs accumulate and funds are funneled from the education system to unnecessary costs. Through wasting funds and creating problems with implementation, the frequent changes hinder the compulsory education law from being as effective as it was designed to be, therefore preventing it from having the intended result of reducing inequality through providing equal access.

In addition to drastic changes in funding policy, the presence of 'mixed changes' can cause previously existing policies and new policies to be mutually weakening (Wei, 2008, p. 120). For example, China's fiscal and tax reform in conjunction with the compulsory education investment policy creates challenges for funding education through weakening the main source of funding, local government funding (Wei, 2008, p. 120). The tax sharing reform changed the way revenues were shared between the central government and provincial governments by dividing tax revenue into 3 categories: central, local, and shared (Shaoguang, 1997, p. 2). This led to a divide between financial rights and administrative power, which caused the decay of public spending at the county level (Wei, 2008, p. 120). It also gathered financial rights on higher governments, which gradually caused financial power at county levels to weaken significantly, disturbing the flow of education spending (Wei, 2008, p. 120). Without a strong and clear source of funding, chances for successful implementation were weakened. Another example of 'mixed changes' is the effect of the one fee system on compulsory education's financial input. Prior to the one fee system, schools were able to charge students for things such as school maintenance, newer facilities, use of supplies, etc. While preventing the charge of extra fees to students could be beneficial for children from low-income, it has not been supported through additional funds in the compulsory education financial input by governments, therefore "confusing the investment system" (Wei, 2008, p. 120). Despite the one fee system many schools still frequently charge students various fees out of necessity, making it more difficult for lower income families to send their children to school.

The effects of both drastic changes in China's Compulsory Education Law funding policy and the mutually weakening effect of 'mixed policy' can be seen when examining the percentage of provinces that are able to fulfill the nine-year compulsory education program. Although it was implemented in 1986, as of 1998 seven of the 22 provinces had an education supply below 60% and at the start of the new millennium this education program was still not available in 20 % of

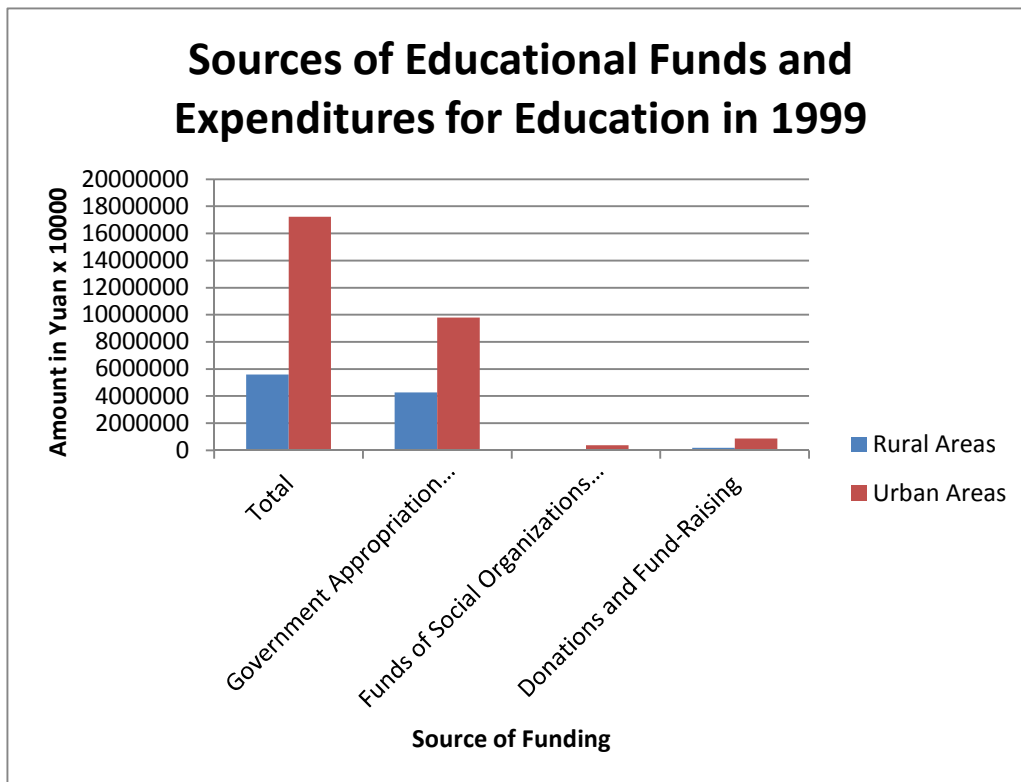
China's rural villages (Gul & Lu, 2011b, 152). When examining these figures it is important to keep in mind that Chinese officials are known to artificially inflate enrollment figures, (Gul & Lu, 2011b, 152). As a result of this, it is reasonable to state that the Compulsory education law has been even less effective than official Chinese statistics show. There are also problems with getting accurate data at the local level where education officials make sure that the attendance roster has every child's name that is supposed to be on it, whether or not they are actually ever able to attend a single day of school (Gul & Lu, 2011b, 152). Students are also borrowed from other schools when inspectors come around in order to receive funding that would have been allocated to the missing students (Gul & Lu, 2011b, 152). Whether enrollment rates are exaggerated or not, judging from the data that is available, the Compulsory education law has not been as effective as intended and huge disparities in educational attainment still exist across China. If frequent and mixed changes were not an aspect of the policy, it would have been efficient and properly funded, therefore increasing access to education to the most disadvantaged areas of the country. This eventually would have helped in the reduction of inequality.

Along with frequent and mixed policies, a lack of compensation for schools requiring additional funding also significantly reduced the ability of the Compulsory education law to help narrow the gap of the unequal distribution of wealth. Tsang and Dings (2005) study "Resource Utilization and Disparities in Compulsory Education in China" revealed that inequalities in access to funding and resources between the different regions in China. They found that the top-spending region on primary education spent up to 5.2 times as much as the bottom-spending region (p. 5). This is partly due to differences in the breakdown of where the funds and resources come from. Schools in less privileged areas rely more on funds from the government and are mainly used for paying personnel (Tsang & Dings, 2005, p. 21). This is especially true in poor rural areas where the inability to obtain funds and resources outside the government leads them to spend very little on non-personnel inputs. Although government funding is similar for urban and rural areas, urban areas have a huge advantage due to their ability to obtain additional resources from both government and non-government sources (Tsang & Dings, 2005, p. 21). This allows urban schools to spend more on non-personnel inputs such as better facilities, school supplies, teacher's aides, etc. therefore enhancing the overall quality of education they receive over rural students (Tsang & Dings, 2005, p. 21). Although data regarding the source of education funding is not available specifically between urban and rural areas, proxy data could be used to obtain a general idea of the said difference. Regions whose percentage of employees that are in primary industries exceeds 50 percent represent rural areas while regions whose percentage of employees in secondary



and tertiary industries exceeds 50 constitute the urban areas.<sup>6</sup> The graph below displays the disparities in funding between 13 regions representing the urban sector and 13 regions representing the rural sector.<sup>78</sup>

Figure (6):<sup>9</sup>



<sup>6</sup> Data for found in China Statistical Yearbook 2000, page 117

<sup>7</sup> Data was available for 31 Regions. 18 fit under the rural category and 13 under the urban category. 5 random rural regions were not counted in order to make it an even comparison of 13 regions from both sectors.

<sup>8</sup> Urban Regions - Beijing, Tianjin, Hebei, Shanxi, Liaoning, Jilin, Heilongjiang, Shanghai, Jiangsu, Zhejiang, Fujian, Hubei, Guangdong  
 Rural Regions - Inner Mongolia, Anhui, Jiangxi, Guangxi, Hainan, Chongqing, Guizhou, Tibet, Shaanxi, Gansu, Qinghai, Ningxia, Xinjiang

<sup>9</sup> Amount of funds from social organizations and citizens were not available for Beijing (Urban) and Tibet (Rural)

*Source: China Statistical Yearbook 2000*

Although the data shown is only from one year (1999), secondary sources suggest this has been the trend of funding for an extended period of time. The first observation to be noted is that amount of funding for urban areas far exceeds that of the rural areas at 172,386,680,000 Yuan and 56,014,140,000 Yuan respectively. When examining the breakdown of the source of these funds, the urban proxy receives 57% of its funds from the government at 97,898,690,000 Yuan and the urban proxy receives 76% of its education funds from the government at 42,582,060,000 Yuan. This shows that the urban areas receive a significant amount more from outside sources than rural areas. The consequences of additional funding in urban areas can be seen when looking at the difference in the number of students per staff between urban and rural areas. In primary schools in 1999, there were 17.17 and 22.3 students per staff member in urban and rural areas respectively (China Statistical Yearbook 2000). In Secondary schools there were 11.8 and 16.52 students per staff member in urban and rural areas respectively (China Statistical Yearbook 2000).<sup>10</sup> Considering the inequalities that are created through unequal access to funds and resources for schools across the country, the Compulsory education law's funding policy should take these differences into account and respond accordingly. Without measures in place to counteract the disadvantages that exist between not only urban and rural-areas but minorities and gender as well, direct charges are increased to parents which create more barriers for poor students. For these reasons, the compulsory education law does less than it is capable of to narrow the unequal distribution of wealth in China.

### *Higher Education*

China is now the third largest higher education provider despite developing its higher education fairly recently (Wang, 2011a, p. 231). While it has experienced tremendous growth in higher education since expansion in the late 1990's, there still remains the issue of unequal access and its negative effect on economic and social inequalities. Most national higher education institutions are located in major cities such as Beijing, Shanghai, and Nanjing (Gul & Lu, 2011b, 167). Twenty six percent of the top 100 universities and 30 percent of central government managed universities are in Beijing, where enrollment of 18-22 year olds in higher education institutions is more than double that of the

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<sup>10</sup> Calculated using the student enrollment of schools in the rural and urban areas of 31 regions in China divided by the number of teachers and staff in the same areas in both primary and regular secondary schools in 1999.

national average (Gul & Lu, 2011b, 167). Such statistics illustrate the divide in access to higher education between rural and urban areas.

Although the differences in rates of admission between urban and rural areas vary depending on the type of institution, urban residents remain more likely to attend a university than rural residents for a variety of reasons. One major source of unequal access stems from the disparities in education access at the primary and secondary level. As a result, the various policy effects on lower levels of education discussed earlier have an impact on higher education as well. Through less education and poorer quality schooling rural students are subject to, they are not as prepared to pass the college entrance exam as more privileged urban students are. Aside from being more inclined to have a better access to primary and secondary education, urban students are better equipped to have better scores on the exam because of the importance it stresses on Chinese and English language skills, which are not taught in rural areas to the degree they are in urban areas (Wang, 2011a, p. 235). In this way, many of the differences in access to higher education between rural and urban areas are caused by the same sources of inequality that we see in primary and secondary education. This allows such policies to continue to contribute to the unequal distribution of wealth.

Another impact that access to higher education has on the distribution of wealth relates to the differences between demands for different majors. Popular programs are generally more competitive because they are more likely to lead to higher paying jobs and social status (Wang, 2011a, p. 236). This raises tuition fees for these majors, making it less accessible to rural students. A study conducted in 2009 assessing the likelihood of rural and urban students to be accepted to 11 different programs showed considerable disparities. In economics, law, and management, urban students were admitted respectively 4.32, 3.15, and 2.68 times more than rural students (Wang, 2011a, p. 236). Agricultural science, history, and education on the other hand showed considerably more equal results. A likely cause of this is that students from rural areas are more inclined to choose a major with low tuition fees. Considering the majors with higher tuition fees are more likely to lead to a higher paying job in the future, this disparity effects the distribution of wealth down the line.

The relationship between government policy, education, and the distribution of wealth consists of a very complex web of relationships. Since each additional year of education provides additional income, a lack of education can lead to life of poverty. Once this cycle of poverty has begun, it becomes very difficult for parents and future generations to break out of. Since government policy dictates the education system, it naturally has a very large effect on the degree and quality of access. The drastic changes in the compulsory education

laws funding policy, mutually weakening 'mixed policies,' and the lack of compensation for disadvantaged rural schools create a domino effect that eventually assists in the creation and maintenance of China's huge gap in the distribution of wealth. It first makes it more difficult for marginalized children to receive a primary and secondary education, and eventually makes it more difficult to attend a higher education institution. The resulting consequences are significantly lower incomes for the already disadvantaged and higher incomes for the more privileged urban residents.

#### **Part 4: Housing**

Another important subject to examine in the context of inequality is housing policy. As one of the most important elements of social policy, it gives us a clear picture of social stratification and varying income levels. As Zhang (2010) states, "House, the most basic and essential resource of human survival and development, is one of the key indicators in building a harmonious society, which measures the quality of life in a country or region" (p. 97). Like education policy, housing policy has undergone many radical transformations since market reforms in the late 70's that directly affect its method of distribution and therefore its impact on the unequal distribution of wealth. Each one of these policies contains its own sort of 'self closeness' that neglects to improve the fairness of access to the housing market (Zhang, 2010, p. 99). Through the disregard for the pre-existing structure of the housing system when developing housing policies, the affects of housing reform have been inconsistent and have significantly contributed to China's widening gap in the distribution of wealth.

Much of China's housing inequality stems from unintentional affects of housing reforms since 1978. Regarded as one of the most important facets of public-sector reform in China, housing reform seeks to improve competition, privatize housing stock, and achieve equity and efficiency (Tolley, 1991, p. 1). This mainly consists of decreasing the role the government has in the housing market through encouraging private home ownership. Although each change in housing policy pushes for more decentralization and privatization, housing resources remain to controlled by "gate keepers or cadres" through redistribution (Lee, 2000, p. 62). The main 'gate keeper' in the distribution of housing is the work-unit, otherwise known as Danwei, which plays a very active role in people's lives through providing jobs as well as social and political needs (Xing, 2000, p. 523). Prior to housing reforms launched 10 years after the market reforms in 1988, public housing was predominately constructed, owned, distributed, and ran by work-units (Xing, 2000, p. 523). In order to obtain housing, nearly everyone had to go through a work unit, which received budgetary funding for the distribution of housing from the government. Following the reforms, the

responsibility of the government and work-units changed from being that of providers to "enablers and mediators" in the housing process (Xing, 2000, p. 523). Instead of directly providing housing to its employees, work units bought housing on the market at full price from development companies then sold it to its employees at greatly discounted prices (Zhang, 2002, p. 11). Significant portions of these development companies were run by the state. In 1997, 8,164 out of the 21,286 development companies in China were government owned, maintaining its important role in housing (Xing, 2000, p. 522). This created an unusual situation in which the supply side of the market functioned as a market basis while distribution functioned similar to welfare (Xing, 2000, p. 524). Although work units went from directly providing housing to facilitating it through a system of re-selling at significantly lower prices, its role in the housing system was strengthened through formation of partnerships in other market forms of housing supply (Xing, 2000, p. 524). Since work-units are better equipped to afford housing at full price than individuals and are a much more dominate force in the housing market, housing prices rapidly rose making it very difficult for individuals to seek housing options on their own (Xing, 2000, p. 524). This strengthens the responsibility of work-units in the housing system and makes people more reliant on the services of work-units to obtain affordable housing. This combined with the varying degree of work unit's ability to afford the purchase of housing in the market for the resale to employees creates a significant equity problem in access to housing. Not only are people now more reliant on the work-unit for affordable housing, the profitability of the work-unit is much more important in its ability to facilitate the purchase of housing for resale to its employees. Basically, the housing reforms in 1988 were successful in eliminating the socialist method of directly providing housing to all workers, but it failed in its to shift to an efficient private market while controlling for a sharp increase in inequality.

The housing market reforms in 1988 also worsened equality through its affect on overall income given by work-units. Prior to the reform, the government strictly mandated wages and there was little room to receive a higher salary (Xie & Wu, 2008, p. 598). Workers salaries were based on "occupational status, seniority, and administrative position (Xie & Wu, 2008, p. 598). Following the reforms, many changes occurred that pushed for less regulation of work-units, allowing them more autonomy to function like an economic entity in a capitalistic system (Huang & Deng, 2006, p. 628). Base salaries remained to be mandated by the government, however, work-units gained more control over the distribution of other benefits and bonuses. One of the main desired outcomes of this was to have the additional income workers received through these bonuses and benefits depend more on their productivity in order to improve the performance of workers

and the work-units themselves. This goal was not achieved for a variety of factors. One reason is that it was soon evident that the success of a work-unit was contingent on multiple factors aside from the productivity of workers, such as the number of similar enterprises, technology, and geographical advantage (Xie & Wu, 2008, p. 563). These circumstances had more of an effect on the bonus workers received than their work ethic, therefore failing to develop a connection between worker productivity and additional income. Another reason is the dynamic of the manager-worker relationship didn't allow bonuses and additional benefits to be distributed strictly by level of productivity. Prior to the reform, managers and workers were codependent; meaning managers needed the workers to cooperate to maintain credibility as leaders while the workers relied on the managers for promotions and positive evaluations (Xie & Wu, 2008, p. 566). The structure of this relationship enabled workers to encourage their managers to push for raising their incomes through additional sources other than the government mandated base salary. This put managers in a difficult position, who as a result of the reforms were pressured to increase workers productivity while continuing to be responsible for their well being (Xie & Wu, 2008, p. 566). Managers tended to side with workers through utilizing funds available to upgrade their workers living situation, which maintained a positive relationship and fulfilled the parental image that China held as an ideal of local officials during its imperial years (Xie & Wu, 2008, p. 566). This not only separates a workers final income from their level of productivity, it makes it contingent on the profitability of the work-unit they belong to. When bonuses and benefits become a large portion of final income, a huge equality problem is created. Estimates show that in the 1980's additional income from work units accounted for about 33 to 40 percent to total income and in the 1990's it passed 50 percent (Xie & Wu, 2008, p. 566). Additionally, members of high earning work-units can have an income that is up to 2.5 times more than members of less profitable, yet similar work units (Xie & Wu, 2008, p. 579).

Considering the obvious importance the work-unit had in the distribution of housing prior to the reforms, reform policies should go deeper by mandating the relationship between work-units and their employees in order for policies to achieve their goal. For instance, the government could limit the amount of housing work-units are allowed to buy off the market and the amount of discount they are able to give to their employees. This would promote healthy competition and prevent housing prices from rising due to work-units comprising the majority of demand. The lack of oversight has caused housing distribution to more or less remain the same. Although the method of providing housing has been changed, at the end of the day the work-unit remains mostly responsible. The only difference it has created is that now the housing provided is based on the profitability of the

work-unit, which has not been successfully contingent on the productivity of its workers. Although the reforms created a private market for housing, it is mainly utilized by work-units, who drive up housing prices. If the government wants to achieve its goal of a healthy private market with fair access, it needs to recognize the persisting role of the work-unit in the housing market and act accordingly.

Another fundamental source of housing inequality in China is the Hukou policy, which is a status given at birth that subjects one to the agricultural (rural) or non-agricultural (urban) sector order to control the flow of people between these areas. It has been an agent of stratification and inequality since its initiation in 1955 and its disequalizing affects have only been exacerbated since 1978. Prior to the reforms, it was successful in restricting migration in rural areas through requiring participation in agricultural production through communes in order to receive food (Wu & Treiman, 2004, p. 364). In urban areas, it was difficult to live outside the tightly controlled and government run work-units, which made it even more difficult from migrants to move to cities to find work (Wu & Treiman, 2004, p. 364). Ascribing whether one must live in a urban or rural area and at birth as well as restricting mobility strongly dictated which 'life chances' one had available to them (Wu & Treiman, 2004, p. 365) through automatically determining one's access to jobs, level and quality of education, health care, and other welfare benefits (Wu & Treiman 363). The restrictions on migration have been eased since market reforms, which only increased inequality through the discrimination and lack of resources available to rural migrants in cities. Through policies that called for the elimination of the commune system and the changes in the role of work-units, rural peasants were allowed to enter cities in order to find employment in the expanding market sector (Wu & Treiman, 2004, p. 365). As a result of urban biases present throughout the system, families migrating to urban areas pay much higher prices for the same goods and services, their children have less access to the education system, and they are forced to live in substantially worse living conditions (Dennis, 1999, p. 309). So despite the ease of restrictions on migration, the inequality caused by the household registration system was worsened through the creation of a 'second class' of rural migrants living in cities without the same rights as those with urban hukou status (Wu & Treiman, 2004, p. 365).

Huang and Jiang's (2009) study of the housing inequality in Beijing in the late 90's provides a strong example of how hukou status can determine ones access to quality housing. They found that the housing reforms improved housing consumption for nearly all groups except migrants with rural registration status living in the city (p. 953), which represents this 'second class'. They were much less likely to have access to public rental housing and own homes with the help of subsidies (Huang & Jiang, 2009, p. 953). Around 8 percent of urban migrants and

4.5 percent of rural migrants owned their home while 58% of local urban residents and 52% of local urban movers were homeowners (Huang & Jiang, 2009, p. 943). They also found a connection between education and quality housing. Their study showed that people with a college education had the highest rate of homeownership at 59% as well as consuming the biggest and best housing (Huang & Jiang, 2009, p. 943). Access to housing is not just connected with higher education, but primary and secondary as well. As stated earlier, childcare and elementary and middle school educations are not available to the children of migrants that lack the ability to obtain urban registration (Dennis, 1999, p. 309). They pay up to three times the amount that locals pay for the often lesser quality education through 'temporary student fees'. (Gul & Lu, 2011b, 160). Moreover, they are often segregated into different classes because urban parents fear that migrant children would take away from their own child's education (Gul & Lu, 2011b, 160). Considering the correlation of education and higher income described earlier, the discriminatory aspect of housing policies exacerbate inequalities.

One could argue that the government has duly noted the equity problem caused by housing policy and policies have been put in place to correct it. For instance, the Economically Affordable Housing Policy attempts to assist low income families to purchase their own housing through enlarging the housing supply, managing the structure of real estate investment, and encouraging demand in the housing market through a variety of policies (Zhang, 2010, p. 101). While this was a valid effort, it was largely unsuccessful due to the lack of strict eligibility criteria. In some areas, the low-end houses were purchased by mid-high income earners (Zhang, 2010, p. 101). In order for the Economically Affordable Housing Policy to be consistent and affective, it needs to put measures in place to ensure that affordable housing goes to people who need it, such as assisting those whose work-unit is unable to provide assistance. It also could put a rule in place to ensure that low-income housing is only sold to low-income families instead of being bought up by the middle and upper class. Just like the work-unit, the hukou system was in place long before the reforms and has significantly shaped the structure of the housing system. Policies need to weigh the importance of these two forces and act accordingly. Without effective measures in place to counteract the disequalizing effects the work-units and registration system have had after the reforms, policies will remain inconsistent with what they aim to achieve.

Overall, one of the main goals of the housing reforms is to encourage people to buy their own homes in the private market. This is thought to be beneficial to individuals and society as a whole through providing better opportunities (Zhang, 2010, p. 101). Unfortunately, such positive effects are not realized due to inconsistent housing policies. One of the main issues is that they



do not take into account how the pre-existing housing structure and policies will react to attempts of decentralization and privatization. As a result, the work-unit has strengthened its necessity in obtaining housing and the hukou status has caused rural migrants in urban areas to be severely disadvantaged. This has prevented the market from having equal and fair access. Government policies regarding housing should be more consistent through implementing measures in work-units and the registration system considering their strong influence in housing distribution.

### **Part 5: Conclusion**

Policies following the switch from a planned to market economy for the most part have increased educational attainment and the amount of housing available in China. At the same time, it has severely increased the unequal distribution of wealth. While some may argue that this is a direct result of the nature of a capitalistic system, I argue that the causes are deeper than that, with the severity of inequality being a product of inconsistent policies. As far as education is concerned, an increase in inequality has occurred as a result of urban biased policies, and the presence of frequent and mixed changes in the compulsory education policy have prevented it from assisting in the reduction of inequality. As far as housing is concerned, pre-existing housing institutions such as the work-unit and Hukou registration status have not reacted well to changes in policy, with their stratification mechanisms heightened in the light of reforms.

One of the primary sources of these issues is the inconsistency in government policies. Unlike the 'big bang' approach many Eastern European countries have taken in order to transition from socialism, China's reforms have been piecemeal, with reforms taking place gradually in many sectors. Each reform has a different agenda, which often conflicts with existing policies and does not work efficiently to the overarching goal of achieving private markets that promote fair competition. Considering the negative effects this has on China, leading to low domestic demand, threatening social and political stability, and affecting the inability of those at the bottom to afford social investment, action needs to be taken in order to improve the large gap in the distribution of wealth. While the elimination of inequality in a capitalist system is highly unlikely, making sure the structure of the education system and housing market is free from institutional barriers that decide one's place in society is not.

In order to address inequality, policies should take into account how it will affect vulnerable groups such as people living in rural areas, women, ethnic minorities, and have a system in place to assist them through the process until they are at a place where they could fairly search for goods and services on the

open market. While this may sound for a call for regressive move back to a more socialist system, it is not. The government does not need to directly distribute to its citizens in order to obtain a better degree of equality. It needs to have a system in place to make sure that the market is free of 'gate keepers' and that it runs efficiently and fairly in the short term so vulnerable groups can get their feet on the ground and be able to participate fairly in the future. For instance, when drastic reforms of the housing market are put in place, so should reforms for the agents of distribution such as the work-unit. In the new planned economy, the achievement of fairness and equality should be an overarching goal when it comes to making new policies in order to develop a healthy system that can continue to compete on the world stage. This will help promote political and social stability, maintain a healthy household consumption, and help people at the low end of the income spectrum afford social investment, which all will contribute to China's success in the long term and maintain a 'harmonious society'.

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