

An immediate Chinese challenge: further addressing vast income inequality

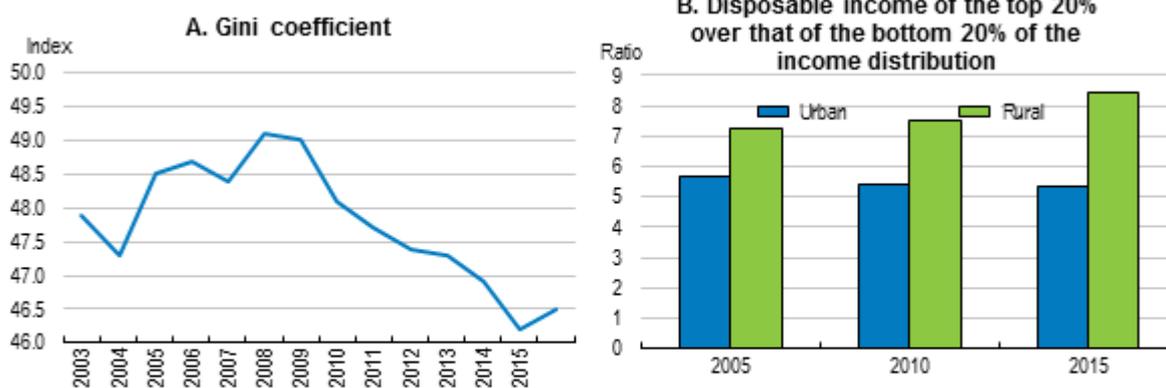
by Ben Westmore, China Desk, OECD Economics Department

The goal of the Chinese government to achieve a “moderately prosperous society in all respects” by 2020 is centred around improving social welfare throughout the population. One of the essential ingredients to doing this is a further reduction in economic inequality.

As underlined in the OECD 2017 China Economic Survey, China’s income inequality as measured by the Gini coefficient has been on a declining trend since 2008 after having climbed to a very high level (Figure 1, Panel A). This reflects some regional income convergence, as the central, western and northeastern parts of the country have made progress catching up with the east, and a narrowing of the urban-rural income gap. Across the income distribution, incomes of those in the middle have risen particularly strongly.

Nevertheless, there are signs that many of the poorest are being left behind. The gap between the richest and poorest urban households in terms of disposable income has barely narrowed. In rural areas, it has even widened (Figure 1, Panel B).

Figure 1. Aggregate income inequality has declined but some of the poorest are being left behind



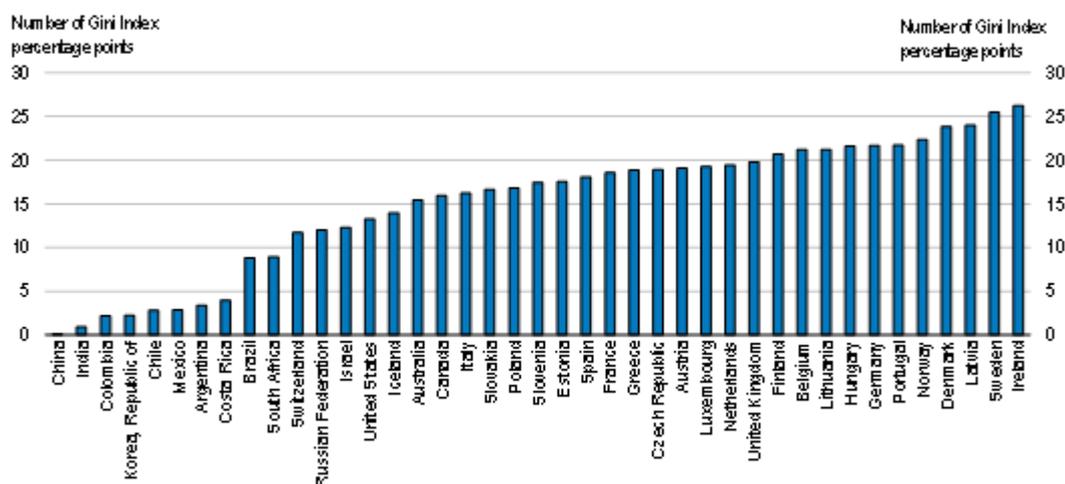
Note: The Gini coefficient presented here is based on income and has a range from zero (when everybody has identical incomes) to 100 (when all income goes to only one person). Increasing values of the Gini coefficient thus indicate higher inequality in the distribution of income.

Source: China National Bureau of Statistics, authors' calculations.

The large and persistent income gap is partly the fault of China's tax and transfer system (Figure 2). In particular, the redistributive influence of the personal income tax regime is stifled by a very generous personal income tax allowance and exemptions that favour high-income individuals. Rules around social security contributions are also regressive. For example, all workers need to make a minimum contribution irrespective of actual income earned and there is a cap on payments.

Figure 2. Redistribution by the tax and transfer system is very limited

Reduction in market income inequality due to taxes and transfers, 2013/15



Note: Data for China are for 2013. Data for other countries are the latest available observation (2013 to 2015, with the exception of India (2011) and South Africa (2012)). The metric presented here is calculated from data that are standardised to allow cross-country comparisons. Potential remaining comparability issues are detailed in [Solt \(2016\)](#).

Source: Standardised World Income Inequality Database (SWIID) Version 5.1.

On the transfer side, there has been a big increase in the coverage of the main social assistance scheme (the *dibao*) since 2000, especially in rural areas. However, there are massive discrepancies in benefits between locations depending on the financing capacity of local governments. While the coverage of unemployment insurance has picked up in recent years, it remains low. Moreover, for the unemployed that do receive benefits, the replacement rate is meagre by OECD standards.

There is also the need to enhance the opportunities of poorer households through reforms outside those relating to the tax and transfer system. Access to good quality education must be broadened, as educational performance is influenced more by socioeconomic factors than in OECD countries. Gaping disparities also exist in access to health resources, especially between urban and rural areas, which translate into inequities in overall wellbeing. Fortunately, the government is prioritising these areas, as there is much work to do over the next few years so that China can be confidently classified a “moderately prosperous society in all respects”.

References

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