

**INEQUALITY IN CHINA:  
THE CHALLENGE OF  
COMMON PROSPERITY**

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According to World Bank data, only a handful of economies have risen from middle- to high-income status since 1960, when economic catch-up growth in many developing economies took off.<sup>1</sup> Examples include South Korea, Singapore, Israel and Ireland. Some countries that were high income in 1960 remain so today, such as Canada and France. Some that were poor, like Cambodia and Tanzania, have stayed poor. Many countries have stayed at middle-income status for decades, seemingly unable to reach high-income status.<sup>2</sup> They are in what is called the Middle-Income Trap, and this may include China too.

How does China compare to these other countries trapped at the middle-income level? Since the beginning of reforms under Deng Xiaoping in 1978, China has undergone remarkable development. After four decades of strong economic growth, China has become the second-largest economy (in terms of nominal GDP), the largest exporter and the second-largest importer in the world.<sup>3</sup> However, China's growth, even with double-digit growth rates, has relied heavily on unskilled labour. Most of the workers who have fuelled the country's rise come from rural villages and have never gone to high school. For all of its investment in physical infrastructure, for decades China failed to invest enough in the education and health of a large share of its people.<sup>4</sup>

One key factor that may account for disparate development paths among nations is education. According to the Organization for Economic Cooperation and Development (OECD), in 2015 in countries that graduated to high-income status (i.e. they escaped from middle income), 72 percent of the working age population (18–65 years) had completed secondary education when the country was still at middle-income status.<sup>5</sup> In countries stuck in the Middle-Income Trap, the share of the working-age population with a secondary education is much lower—only 36 percent on average.

Having a large supply of educated workers ensures that enough talent exists to meet and drive demand for high-value goods and services that drive an economy when it becomes a high-income one, thereby sustaining growth. When too many unskilled workers are squeezed out of upgraded industries, their wages tend to stagnate or fall, curtailing demand and hampering

growth. This eventually leads to serious social problems, such as higher rates of unemployment and increased crime and social unrest. Nations with socially polarised work forces also suffer from political instability.



**Young children in rural areas may be unprepared to learn complex skills as they age**

Source: Samuel Vigier, Flickr

## **Shortcomings in education and health threaten China's growth**

Education attainment metrics help reveal China's potential future development and growth trajectory. The share of uneducated workers in China's labour force is larger than that of virtually all upper middle-income countries. According to China's own 2015 micro-census data, there are between 450 to 500 million people in China between the ages of 18 and 65 who have never attended one day of high school, which is 70 percent of the labour force. This makes China one of the least educated middle-income countries in the world.<sup>6</sup>

A large population of uneducated workers was not a problem while China was moving from low- to middle-income status. Unskilled labour was in high demand. Unskilled wages were low, and low-cost manufacturing and construction were growing. But China's growth model has been changing over the past decade or more. Unskilled wages are much higher, so foreign investors have begun to shift their attention towards other countries with cheaper labour. China's own massive push to automate (also to avoid having to pay for labour that became increasingly expensive since the mid-2000s) also is rendering low-skilled workers redundant. Construction jobs have tapered off as investment in infrastructure cools as well. China's unskilled workers may become increasingly unemployable (and have actually begun to see wages falling) as the economy upgrades.

The only destination for China's unskilled workforce—new entrants to the labour force and laid-off workers alike—is the informal (or blue-collar) service sector. Data from the 2018 *China Statistical Yearbook* shows that informal employment is currently the fastest growing sector in China, increasing from 33 percent in 2004 to 56 percent in 2017.<sup>7</sup> A rising supply of unskilled workers (along with only moderately growing demand for services) means stagnating wages. With strong demand for skilled work in the white-collar sector, higher wages are going to those with higher levels of education. This result appears to have a large number of similarities to what happened in Mexico in the 1990s (although there are differences): Mexico had solid macroeconomic performance, export success and an accumulation of physical capital. However, despite these strengths, the nation's poorly educated labour force and the emergence of a dominating informal economy swamped and dragged down the development of the formal economy. Despite rapid growth in the 1970s and 1980s (which ended with Mexico being admitted to the OECD as a rapidly developing upper middle-income economy), Mexico has almost experienced no growth since the mid-1990s and today is a clearly a stagnant middle-income nation.

Recognising the critical need for secondary education, China's government expanded access to high school throughout the country in the mid-2000s.<sup>8</sup> High school attainment among the youngest cohorts in the labour force is close to 80 percent. But hundreds of millions of less educated people

will remain in the labour force for the next thirty years.<sup>9</sup> The government will face huge challenges trying either to retrain workers or to provide a social safety net.

The quality of China's expanded secondary school education is also uncertain. Almost all low-skilled labour comes from rural areas, where school and health systems are under-resourced due to the legacy of national policies.<sup>10</sup> The household registration (*hukou* 户口) system played an important role in the widening of China's rural/urban disparities. The system was introduced in the 1950s as a way of managing labour and population flows in an economy that was being run by central planners (as opposed to markets). Although *hukou*-related restrictions on labour mobility were relaxed gradually after the early 1990s, the system continued to limit educational, health and employment opportunities for rural *hukou* holders. Moreover, historically higher shares of public investments in infrastructure and services have been channelled towards urban areas in China. As a result, many of China's new secondary school graduates attended poor-quality vocational high schools and are not learning the maths, science, computer and language skills that China will need in the future in its labour force if the nation graduates to high-income status.

Systemic shortfalls in education and the health of young children in rural areas may also render many young people unprepared to learn complex skills as they age. Large-scale field studies showed that more than a quarter of Chinese school children were anemic; one out of five were myopic (and did not have eyeglasses); and one out of four children had intestinal worms. Soil-transmitted helminth infections are a threat to the nutritional status of children and their cognitive development.<sup>11</sup>

Increasingly, studies recognise that early childhood (up to three years old) is a sensitive and critical stage, foundational for lifelong human development.<sup>12</sup> In the international literature, delays in early childhood development have been associated with decreased cognitive functioning and lower labour productivity in adulthood.<sup>13</sup> Empirical evidence from China specifically demonstrates that the rural/urban education gap in the country emerges during the first years of life, when rural children start

lagging behind in their development.<sup>14</sup> A systematic review and meta-analysis calculated that the risks of delay to early cognitive development and language function for children younger than five years of age in rural study sites across China amount to 45 percent and 46 percent, respectively.<sup>15</sup>



**Most of the workers who have fuelled the country's rise come from rural villages and have never gone to high school**

Source: Wang Whale, Unsplash

A safe home environment with sufficient learning opportunities, healthy nutrition and responsive caregiving are essential for healthy development during early childhood. An optimal home is a clean and safe environment, sensitive to the nutritional needs of young children and equipped with developmentally appropriate objects, toys and books that provide opportunities for children to play, explore and discover. However, survey results have shown that parental investment in cognitively stimulating parenting practices and child nutrition in rural China is low. No more than 25 percent of the rural caregivers in large-scale field surveys in rural China report frequently reading or telling stories to their young children.<sup>16</sup>

Another study in China's rural areas found that no more than 30 percent of the caregivers provide a diet for their children that satisfies the WHO's minimum dietary diversity criterion.<sup>17</sup>

Parenting training programs focusing on cognitive stimulation can benefit the developmental opportunities of young children in developing countries.<sup>18</sup> Pioneering studies from the 1970s and 1980s, with long-term follow-up, include the Jamaican Nutrition and Cognitive Stimulation Program (or Reach Up and Learn). They found evidence of lasting positive impacts of small-scale parenting interventions on a range of adult outcomes, including lifetime educational attainment.<sup>19</sup> The promising results incentivised researchers and policymakers in the 2010s, in particular after the United Nations introduced Target 4.2 of the Sustainable Development Goals, which would 'ensure that all girls and boys have access to quality early childhood development by 2030', to replicate such interventions in resource-poor settings around the world.<sup>20</sup> Over the past decade, evidence from randomised controlled trials has confirmed the effectiveness of parental training experiments in resource-poor settings in a range of developing regions, including in rural China.<sup>21</sup> Therefore policymakers no longer debate the effectiveness of parenting programs, only how quality child and family services can be delivered cost effectively, sustainably and at scale.

China's government has announced its intention to steer China on a path of 'people-centred development' towards Common Prosperity. In 2010 China became the second largest economy in the world after the United States, and claims to have eradicated extreme poverty in 2020.<sup>22</sup> Despite achieving these milestones, 600 million Chinese had a monthly per capita income of US\$140 or less in 2020,<sup>23</sup> and regional and rural/urban inequalities have widened over the past decades.<sup>24</sup> In the face of these remaining challenges, China's central leadership has promoted the phrase 'Common Prosperity' 共同富裕 since 2020.<sup>25</sup> This signals an intent on the one hand to curtail income inequality and excessive wealth accumulation by individuals and on the other to help people achieve a better standard of living.

Investing in the developmental opportunities of disadvantaged children is crucial to improve equality of educational opportunity and social mobility and to build the large, high-skilled labour force China will need to support a strong, innovation-driven economy in the future. Providing young children with a fair start in life is crucial to address the ‘principal contradiction between unbalanced and inadequate development and the people’s ever-growing needs for a better life’ that China’s society faces today.<sup>26</sup> This principal contradiction was highlighted as the main stumbling block that needed to be tackled for further social development by Xi Jinping during his report to the 19th National Congress of the Communist Party of China in 2017.

## **Why we should want China to succeed ... or at least not to fail**

The risks of a stagnating China would reverberate far beyond its shores. China’s sheer size—one-fifth of the world’s population—means that what happens there will have outsized implications for foreign trade, global supply chains, financial markets and growth around the globe. There are political perils, too. An economically insecure China might boost nationalism to maintain legitimacy. No assessment of China’s growth is complete without considering the implications of China having hundreds of millions of underemployed people in its economy for the foreseeable future.



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