SURPLUS LABOUR AND URBANIZATION IN CHINA†

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Abstract: This paper distinguishes two types of urbanization and argues that urbanization without sufficient employment creation in the urban sector might have no economic benefit as it only involves surplus labour in the rural areas becoming urban surplus labour. It argues that China’s Hukou system that has restricted rural-urban migration did not necessarily reduce economic efficiency rather it might have raised urban welfare at the expense of rural welfare. An under-discussed feature of the Hukou system is that it ties people not to just either rural or urban areas but to particular geographical locations. This paper argues that many of the recent “rural land for urban Hukou” programs, in the name of reducing the rural-urban income gap, do little to address the geographic specificity of the Hukou restrictions but may in effect amount to a land appropriation by local governments. This paper suggests that to improve economic efficiency and welfare, a “real” reform of the Hukou system should reduce barriers for cross regional migration.

Keywords: Surplus Labour, Urbanization, Employment Creation
JEL Classification: J21, J30, O13, O18

1. Introduction

Along with its significant economic growth, China has undergone an enormous increase in urbanization over the past 30 years. The number of people living in urban areas has grown from less than 18 percent of total population in 1978 to 51 percent in 2011 (NBS, 2012). That is, more than 520 million more people are now living in urban areas in China.

Although the level of urbanization is still below that of many developed countries which have more than 80 percent of urban population, the scale and the speed of Chinese urbanization is astonishing. There is a great urgency to have a better understanding of the urbanization process.

The literature on urbanization is wide ranging, from work examining why economic activity is so geographically concentrated, work looking at the questions about the efficiency of rural to urban migration, work discussing the way cities interact with each other and work on governance, institutions, and public policy and their effect on urbanization (Henderson, 2005). However, there are still many questions that need to be answered regarding China’s urbanization, given the scale and the speed of its urbanization process, given that China has huge number of surplus labor, given that China’s rural-urban migration is strictly controlled by the government.

Many countries have pursued an urban bias policy. For example,
Public infrastructure investments in cities are enormous as compared to rural areas and government policies concerning land markets and migration are often favoring urban areas. Urban bias is more so for China as it explicitly controls population movement. As a result, the rural-urban income gap in China is now amongst the biggest in the world (Wang and Piesse, 2010). Not only income, the rural-urban divide is multi-dimensional. China’s rural-urban divide and inequality have risen both across regions and over time.

A big rural-urban divide in many countries has led to mass rural-urban migration.

However, China’s urbanization process has been subject to very heavy distortionary government policies. China’s unique Hukou (Household registration) system which is a de-facto internal passport and visa mechanism, where no unauthorized movement across regions or from rural areas to urban areas was legally allowed, means that this migration has been less. The Hukou system created invisible walls and administrative barriers that divided China into two: those with urban Hukou who have access to certain government subsidies and those with rural Hukou are guaranteed a land use rights and access to subsistence.

Since the reforms began, there has been a continuous loosening of controls and restrictions on rural labour moving to cities. Although it still remains extremely difficult for a rural person to become a permanent urban dweller (that is to obtain an urban Hukou), many of them live in cities on the “temporary” basis without urban Hukou status. As of 2011, it is estimated that roughly 250 million people with rural Hukou status were resident\(^1\) in urban areas (NBS, 2012).

Despite continuing government efforts aimed at improving rural development the rural-urban divide is still increasing. This has led many researchers to place the blame for this on the Hukou system. They have added their voice to calls for the abolition of the system. Some local governments, such as Chongqing municipal provincial government, began to encourage some farmers to give up their land rights in exchange for urban Hukou status. However, this paper puts those questions into a theoretical framework and argues that this is not likely to reduce the divide or improve economic efficiency. Quite the contrary, it is likely that such policies would be used by local authorities as an excuse for land expropriation, which would tend to hurt vulnerable rural people.

The presence of a large rural population and a fast growing industrial sector means that China has a typical “dual economy” structure, which can be examined using Lewis’ framework (Lewis, 1954; Wang and Piesse, 2013\(^2\)). We examine the two types of urbanization: one with industrialization and employment creation and the other without. The latter urbanization will

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1 Residency here in this data is defined by the Chinese State Council as “at least three months” in the particular urban area.

2 Wang and Piesse (2013) provide a detailed study of microfoundations for dual economy models, which made it possible to examine the micro mechanisms of dual sector economy.