

## In China, Growth at Whose Cost?

*Nation's Poorest Seem to Be Getting Left Behind,  
Raising Sticky Questions for Communist Party*

By ANDREW BATSON and SHAI OSTER

BEIJING -- China's economic miracle has lifted hundreds of millions of people out of poverty, but the country is showing signs that its poorest citizens are falling further behind.

The success of China's transformation into a manufacturing powerhouse has allowed Beijing to dismiss criticism of the downside of Chinese-style economic reform: a dismal environmental record, a repressive political climate and the breakdown of the country's health-care system.

As long as the country's newfound wealth eventually trickled down to everyone, the reasoning went, the benefits outweighed the problems.

But now, as the Chinese government worries about social stability and amid questions about the social costs of China's rapid growth, new figures suggest the poorest of the country's 1.3 billion people are getting even poorer.

From 2001 to 2003, as China's economy expanded nearly 10% a year, average income for the poorest 10% of the country's households fell 2.5%, according to an analysis by the World Bank that has been presented to the Chinese government. Those roughly 130 million Chinese earn \$1 a day or less, the World Bank's global benchmark for poverty.

Meanwhile, the nation's total income rose sharply, and other income groups saw gains, suggesting that the rich are getting richer at the expense of the poorest.

The reason for the income decline at the bottom isn't clear. The World Bank hasn't completed its analysis and its conclusions haven't been published. Even so, the data call into question an economic model that economists have held up as an example for other developing nations.

"This finding is very important. If true, it sheds doubt on the argument that a rising tide lifts all boats," said Bert Hofman, the World Bank's chief economist in China.

China's roughly 10% annual growth in the years since it has opened up to foreign trade and investment, dismantled or privatized state-run companies and encouraged entrepreneurship has made it the world's fourth-largest economy. Those gains have helped to persuade development experts that growth is the surest cure for poverty.

But the widening of China's income gap raises questions about the bargain its government made three decades ago when it agreed to accept a measure of social inequality as long as it improved the nation's welfare overall.

Many observers place part of the blame on the way China dismantled its social-welfare system as it phased out state control of the economy -- without building up much to replace it. Health care has become a point of particular concern, as costs shoot up without any widespread system of medical insurance to cover them. Patients who can't pay often-large sums in cash are frequently refused treatment at Chinese hospitals.

"Before the reform period, China's system of social security was already fragile. Now, after the reforms, it has almost entirely disappeared," said Li Zhining, a retired scholar in Beijing. That gives the government few tools to address the income gap, he said. "I think that the disparity between rich and poor in China will be impossible to resolve in a short time."

The World Bank's Mr. Hofman says the bank's analysis shows the majority of China's poorest 10% appear to be only temporarily poor, thrown down by some setback like sudden illness, the loss of a job or the confiscation of land. That suggests that a basic social safety net, like medical insurance or unemployment benefits, could help move them back out of poverty. Only about 20% to 30% of the poorest appear to be long-term poor, and even they have some savings.

It isn't clear what impact the World Bank data might have on Chinese policy. The World Bank and others are already recommending that China spend more on pensions, health care and other welfare programs.

Still, for the ruling Communist Party, which has staked its legitimacy almost entirely on its ability to make people richer, evidence that incomes are falling could be devastating. During its reform era, China has pulled off one of the greatest economic feats in history, bringing some 400 million people out of poverty in 25 years.

That era dates back to 1978, when former Chinese leader Deng Xiaoping abandoned the egalitarian principles of his Communist predecessors and inaugurated the world's biggest experiment in trickle-down economics. He famously declared that for China to rise out of poverty, some people would be allowed to get rich before others.

Mr. Deng's formula did work: While the manufacturing hubs on the country's south and east coasts got rich first, and are now much better off than the rest of China, average incomes nationwide have risen by about 7% a year since 1978, according to official figures.

In recent years, however, incomes in urban areas have outstripped those in the rest of the country, with city dwellers recording average annual gains of 8% to 9%, compared with less than 5% for rural households. Now, if a large segment of Chinese society has ceased to benefit from economic reforms, it weakens the rationale for continuing down that path.

Other, published figures have also shown that income inequality is rising in China. Its Gini coefficient, a widely used measure of income distribution that starts from zero at perfect equality and tops out at one, last year hit 0.4, up from 0.3 in 1981, according to the Asian Development Bank. That puts socialist China at a level of inequality similar to that of the unabashedly capitalist U.S.

The gap between the highest and lowest incomes is expanding whether one looks at rural and urban residents, inland and coastal cities, or even just high- and low-paying jobs, according to the ADB's analysis of Chinese data.

The rise in inequality has fueled a growing debate among China's intellectuals and politicians about whether the country has swung too far toward capitalism and is leaving behind the Communist Party's core constituency of workers and peasants.

Recognizing that corruption and inequality threaten its authority, China's central leadership has made addressing those issues its top priority. President Hu Jintao's signature slogan is the drive for a "harmonious society" -- one that would bridge the widening income gaps and ease the strains that are causing social unrest.

The World Bank's Mr. Hofman emphasized that the bank's findings, which are based on data collected through a massive household survey by China's National Bureau of Statistics, aren't definitive. For one thing, the survey compares snapshots of the lowest tier of Chinese society at two different points, rather than tracking the same group of households over time. So, it doesn't necessarily mean that the people who were in the poorest 10% of society in 2001 were all 2.5% worse off in 2003.

Moreover, the World Bank started its analysis in 2005, and so didn't have access to complete figures from that year or 2004. More recent data could help determine whether the decline has continued or was just an isolated phenomenon.