Cities xxx (xxxx) xxx–xxx

Contents lists available at ScienceDirect

Cities

journal homepage: www.elsevier.com/locate/cities

Market transition, labor market dynamics and reconfiguration of earning determinants structure in urban China

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1. Introduction

Inequality has always been a major concern of general public in any society. The heightened social and economic polarization represents a potential source threatening social and political stability (Blau & Lawrence, 2009; Gilpin & Gilpin, 2000; Piketty & Saez, 2003). Eliminating excessive poverty, reducing income inequality, and promoting social and economic justice are one of the primary goals of public policy in a nation (Salverda, Nolan, & Smeeding, 2009). After nearly four decades of reforms, China has gradually but persistently eradicated the egalitarian systems of resource redistribution and allocation that were rooted in the planned socialist economy during the Mao's period. The adoption of a market-led development policy has introduced profound changes in Chinese society. The transition to a socialist market economy has not only increased the magnitude of social and economic inequality, but more importantly also altered the essential mechanisms upon which societal inequality is constructed and reconfigured (Bian & Logan, 1996; Liu, Xu, Shen, & Wang, 2016; Nee, 1989; Wei, Li, & Yue, 2017; Xu & Yang, 2013). Noteworthy, such transformation is not just confined to China, but widely witnessed elsewhere in many transitional economies (Bartolj, Ahcan, Feldin, & Polanec, 2013; Gerber & Hout, 1998; Heyns, 2005; Lane & Myant, 2016; Stoica, 2004; van der Lippe & Fodor, 1998). While emerging economies are becoming increasingly important players in a globalized market, however, classic development theories based on the western capitalist experiences provide limited explanatory power to the understanding of fundamental changes experienced in these countries.

From a labour market perspective, the pre-reform labor regime under the planned economy in China determines the demand and supply of labour and its allocation among various sectors and across different regions (Liu et al., 2016; Xu, Tan, & Wang, 2006). Labour income is set according to the egalitarian principle of "same job, same pay." The inequality under the state socialism is a planned product of the state development scheme designed to fulfill its ideological needs and growth targets. Rural-urban earnings differential, regional unevenness in pay schemes, and income inequality between the state-owned and collectively owned firms are rationalized in accordance with the economic development plans. In formulating these aspects of inequality, the role of markets is negligible. Rather, the political positioning in administrative hierarchy is of primary importance (Walder, 1995; Walder, Li, & Treiman, 2000). Such institutionally constructed societal inequality has been overthrown in the waves of market reform and replaced with market-led inequality (Nee, 1989). Labor markets start to emerge. Market mechanisms based on labour supply and demand relationship are formulated and perfected, and gradually become the dominant forces in Chinese labor market, especially in localities where market development becomes mature (Xu & Yang, 2013; Xu, Yu, Zhu, & Lin, 2016). There is a need to provide an understanding of such shift to market mechanisms that have reshaped labour market inequality and its new geography in China. In particular, what are the explanatory power and limitation of market transition theory on social and economic inequality? Are non-human capital factors even relevant in determining local labor market income in transitional economies? Does the level of marketization play a significant role in differentiating the reconfiguration of labor market income? Will an explicit geographic perspective help to theorize market transition processes?

This study attempts to investigate the relationship between market transition and structure of earnings determinants in China. In so undertaking, it adopts explicitly a geographic perspective by comparing earnings structure of three cities located from coastal China to its interior. It attempts to provide an understanding of whether the level of marketization plays a role in differentiating the reconfiguration of labour market income. The following section reviews the literature on market transition and its effects on social and economic inequality. The analytical methods will then be described and the empirical results reported. The paper will conclude by relating the findings of this study to the debates in the literature on the effects of market transition on social and economic inequality from a geographic perspective.

2. Theorizing market transition and income inequality

The transformation of economic and social systems may affect the mechanisms of how economic wealth is distributed and inequality shaped in a society. While there are continuing debates on the casual

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https://doi.org/10.1016/j.cities.2018.02.029
Received 12 September 2017; Received in revised form 2 February 2018; Accepted 28 February 2018

mechanisms of social stratification during the process of economic development, much effort has been devoted to the understanding of the relationship among market development, economic growth, and income distribution in various economic and geographic contexts. The early macroeconomic work is on the effect of economic transformation on income inequality in developing countries (Adelman & Morris, 1967, 1973; Chenery, 1974), and their findings indicate that there is no automatic trickling down of the benefits of economic growth to the poorest segments of the population in low-income countries. Others argue there is an inverted-U relationship between inequality and development in the 1970s in various countries but not in later periods (Bourguignon & Morrisson, 1998). Findings from recent studies on the relationship between economic freedom and inequality are not consistent either. For example, (Berggren, 1999) found that higher levels of economic freedom were associated with greater income inequality, while (Scully, 2002) found that higher levels of economic freedom were associated with lesser income inequality.

There are many channels through which social and economic changes may modify the distribution of income and welfare. Economic growth, demographic transition, and institutional change may alter the distribution of resources across sectors, relative commodity prices, production factor rewards and the factor endowments of agents, each of which may impact on the distribution of income in a society (Bourguignon, 2004). While labor-market imperfections and productivity differentials across sectors with changing importance in the economy may lead to the inverted-U curve relating inequality and development (Kuznets, 1955), the segmentation of the economy shaped by institutional structure may result in different outcomes in social stratification (Xu et al., 2006; Xu & Yang, 2013).

While studies on the relation of economic development and income distribution are largely focused on capitalist economies, however, the transition of the state socialist economy to market economy has attracted extensive scholarly attentions to the understanding of its dynamistic mechanisms and social and economic consequences. In his influential article published in 1989, Nee proposed his well-known market transition theory (MTT) that has subsequently generated long-lasting debates on the effects of market transition on social inequality in transitional economies (Guthrie, 2000; Shu & Bian, 2003; Szelenyi & Kostello, 1996). In his original thesis, Nee argued, "The transition from redistributive to market coordination shifts sources of power and privilege to favour direct producers (i.e., entrepreneurs) relative to redistributors (i.e., cadres)" (Nee, 1989, p. 663). The established market power during the market transition forms a new mechanism from which the interests of the powerless and disprivileged (i.e., the direct producer under the planned economy) can be best served (Nee, 1989; Szelenyi, 1978). The marketlike exchange and transaction systems tend to provide greater incentives for individual effort and as a result rewards to human capital are enhanced while political capital matters less. Market transition also gives rise to new opportunity structures upon which entrepreneurships become an alternative venue of socioeconomic mobility (Nee, 1989). Using his extensive field work and data collected for the early period of reforms in rural Fujian, Nee tested a set of relevant hypotheses and literally verified his predictions of the theory (Nee, 1989, 1991).

Nee's theoretical articulation about the new order of social stratification presents a fresh and arrogant explanation of the effect of transformation from a socialist economy to a market-based economy. Many scholars in different fields of social sciences began to test the validity of MTT in transitional economies, especially when more systematic and longer term income data became readily available. However, empirical evidence has neither supported nor rejected completely the arguments of MTT, which has consequently generated a heated debate on the changing mechanism of social inequality in countries experiencing market transition (Bian & Logan, 1996; Lin, 1995; Szelenyi & Kostello, 1996; Walder, 1992, 1996, 2002). Critiques of MTT are centered in four main aspects. First, it is argued that, different from what MTT has predicted, the initial narrowing inequality during the market transition process is short-lived. The deepening of reforms and furthering market transition have led to an increase in inequality. For example, Yang (1999) as well as The World Bank (1997) concluded that China experienced a sharp rise in income inequality during the reform period. Similar evidence was produced in a study by Hauser and Xie (2005). Based on the household surveys before and after the transition, Brainerd (1998) concluded that overall wage inequality nearly doubled from 1991 to 1994 in Russia. The study by Aghion and Commander (1999) confirmed that Inequality increased in many of the transition economies in Russia and the Former Soviet Union and they also argued that the policies selected in Central Europe engendered a relatively rapid spike in inequality but with a Kuznets curve. The U-shape trend of income inequality refutes the idea of a linear relationship between inequality and market penetration articulated in MTT (Bian & Logan, 1996; Verhoeven, Flap, Dessens, & Jansen, 2008). Second, the declining importance of redistributive power does not necessarily reduce the return to political capital. Xie and Hannum (1996) found that the rates of return to education did not increase with economic growth in reform-era urban China. Bian and Logan (1996) also concluded in their essay that there was a positive association among cadre status, cadre connections, and higher income in China. Using panel survey data from Hungary, Rona-Tas (1994) found political capital remained to be important for maintaining an advantaged position during Hungary's transition to a market economy. Alternatively, it is argued that the return to political capital during the market transition process may be dependent upon the inertia of redistributive power as well as the institutional structure that facilitate the penetration and expansion of the market (Szelenyi & Kostello, 1996). Third, there is little empirical evidence supporting the argument of declining significance of non-human capital articulated in MTT (Shu, 2005; Shu & Bian, 2003; Walder, 1996). For example, the analysis by Reilly (1999) identified that gender pay gap remained to be linked to the rising wage dispersion in Russia over the transitional period. Xu et al. (2006) found non-human capital factors such as gender, migration status, and place factors played a significant role in the segmentation processes of the Chinese labor market during the course of its economic transition. Finally, MTT is also challenged theoretically by scholars in terms of its teleological idea of transition (Grabber & Stark, 1998; Stark, 1996; Szelenyi & Kostello, 1996). For example, Walder (1996) argued that the impact of markets should be viewed skeptically during the economic transition and what matters are how the market is defined by the variable institutions and conditions. From an evolutionary perspective, Zhou (2000) articulated a conceptual model emphasizing the coevolution of politics and markets to theorize the transformation of state socialist societies. Using panel data of 4730 urban residents drawn from 20 cities in China, Zhou (2000) found that significant changes in returns to education and in the rise of private/hybrid firms were coupled with institutional persistence in returns to positional power and in the organizational hierarchy in the reform era. Gerber and Mayorova (2010) showed that personal networks led better jobs and higher pay in Russia and party membership was important in forming the social network that is significant in elevating ones' social mobility in income.

From a geographic perspective, the proposal of market transition theory is aspatial from its very beginning. The theory is grounded empirically in a location of several counties near Xiameng of Fujian province, and was then extrapolated to interpret the changing mechanism of social stratification under market transition of entire China. The local specificity and particular form of space upon which market transition unfolds itself was largely neglected. In fact, it is not surprising to see the controversial evidence on the prediction of MTT when it is further applied to other transitional economies such as East European countries because of a lack of spatial understanding within the theory in its original form. While there are studies that often highlight the significance of space in differentiating market transition (Appleton, Knight, Song, & Xia, 2009; Shu & Bian, 2003), little has been