Discussion: Decentralization, Inequality and Poverty Relief in China

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Can China’s scheme of revenue centralization and expenditure decentralization reduce urban-rural and interregional inequality?

Answer: Not in it’s current implementation.

Why not?

Allocation of local government revenues is not directed to poverty-alleviation projects.
A Puzzle

Christopher Candelaria, Mary Daly, Galina Hale. 2013. "Persistence of Regional Inequality in China." FRBSF
Sources

• Kuznets
• Market Barriers,
  ○ Human capital market failures, e.g. Loury
  ○ Migration barriers
• Political Economy
• Institutions
Consequences — What We Think

- Distributive justice

- Growth consequences
  - Political economy issues
  - Human capital dynamics
  - Social capital
The facts are that there are no facts about the relationship between inequality and growth.

- There is no systematic relation.
- The models are bad.
- There is a systematic relationship in each country, but each country is unique.
The model

• The budget constraint:

\[ R = I + P(1 - \tau) \]

- \( R \) — revenue;
- \( I \) — intergovernmental transfer;
- \( P \) — total tax revenue;
- \( \tau \) — share of local tax revenue going to central gov’t.

• The “behavioral relation”

\[ \Delta \log \text{Inequality} = \alpha + \beta \Delta \log \tau + \gamma \Delta \log I \]

• If you assume \( \Delta \log P = 0 \), then

\[ \Delta \log \text{Inequality} = \alpha + \beta \Delta \log \tau + \gamma \Delta \log I \]
The Model

- Is this a structural model? If not, where does it come from?
- Why is the behavioral relationship stable with respect to governmental policy in the labor market?
- How do I use this model to assess the instruments?
Going Forward

- What is the impact of local government expenditures on the poor?
- Can the central government align the incentives of local government officials with its income and wealth-distribution goals.
The Elephant in the Room