

Confronting Rising Inequality in Asia and the Pacific

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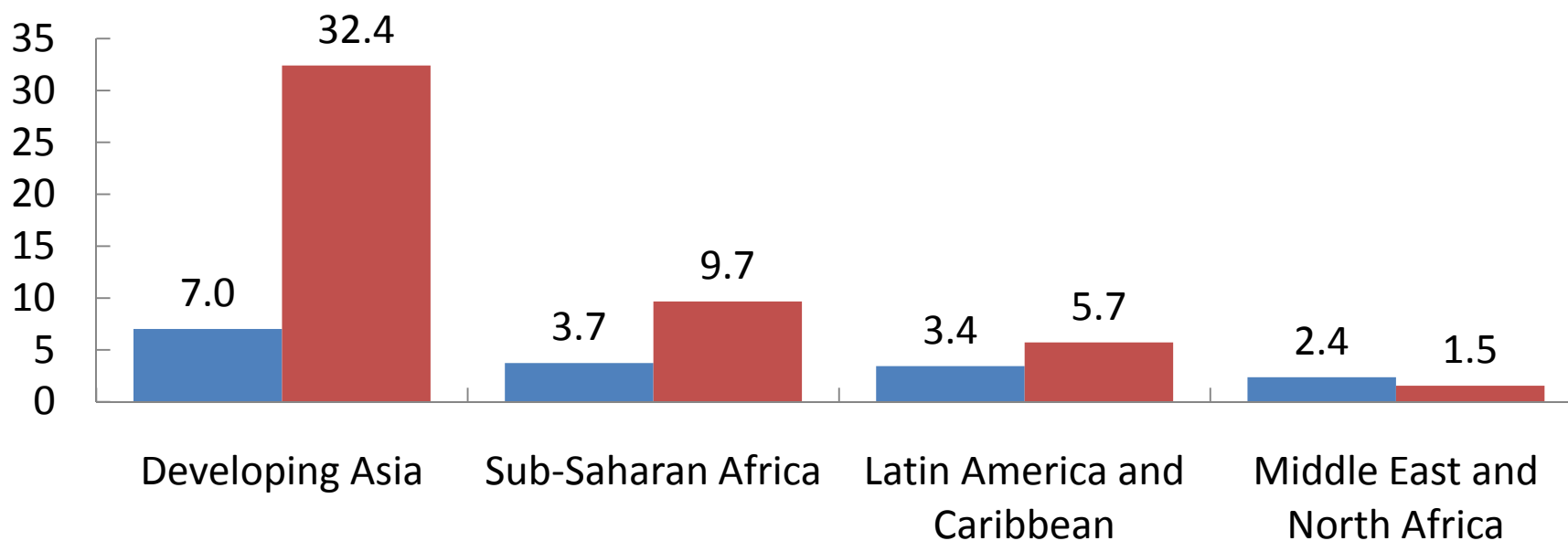


Outline

- Recent trends of inequality in Asia
- Why inequality matters
- Drivers of rising inequality
- Responding to rising inequality
- Moving towards inclusive growth

Asia's high growth has led to large reduction in poverty ...

GDP growth and poverty reduction



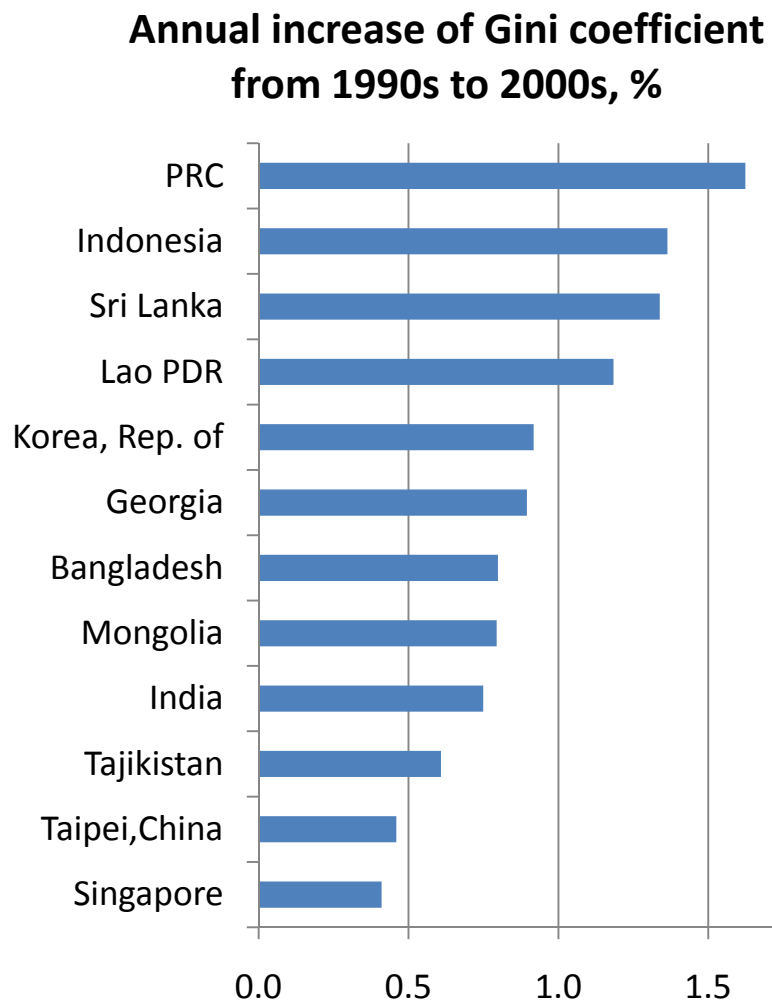
■ Annual GDP growth (1990-2010), %

■ Cumulative reduction in poverty rate (1990s-2000s), percentage point

... but has been accompanied by rising inequality in many countries

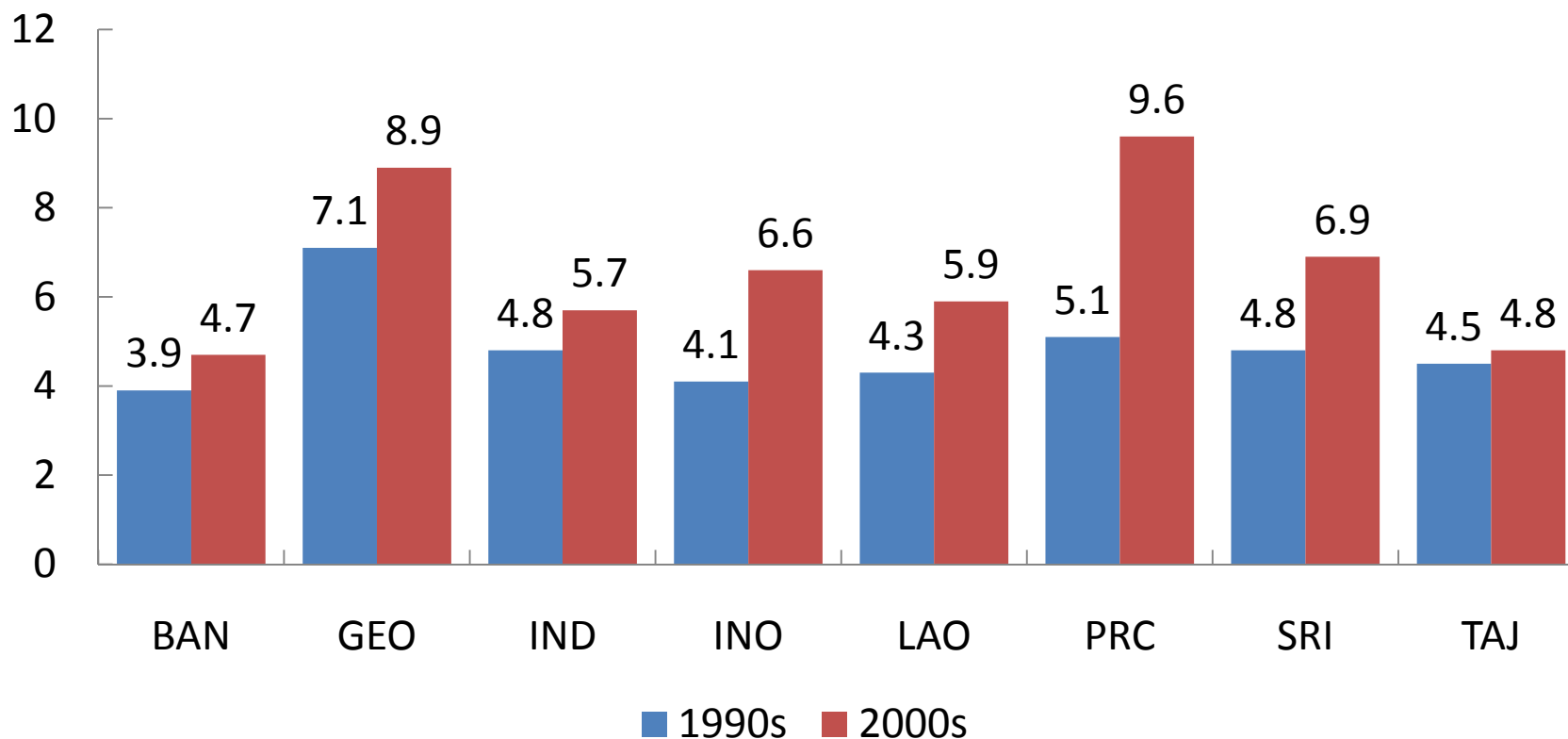
- Inequality increased in 12 out of the 29 countries with comparable data
- The 12 account for over 80% of Asia's population
- Expenditure-based Gini coefficient worsened from:
 - 32 to 43 in P. R. China
 - 33 to 37 in India
 - 29 to 39 in Indonesia
- Taking developing Asia as a single unit, its Gini coefficient rose from 39 to 46 in the last 2 decades

Annual growth of Gini reached more than 1% in some countries



The rich are getting richer much faster than the poor

Quintile ratios, countries with rising inequality



Globally, Asia's inequality is lower, but its rise over time is a concern

	Median Gini	Maximum Gini	Minimum Gini
Developing Asia (consumption)	37.0	50.9	27.8
OECD (income)	30.0	49.6	23.0
Latin America & Caribbean (income)	52.3	59.5	44.7
Middle East & North Africa (consumption)	36.8	41.4	29.8
Sub-Saharan Africa (consumption)	42.8	65.8	30.0

Why inequality matters

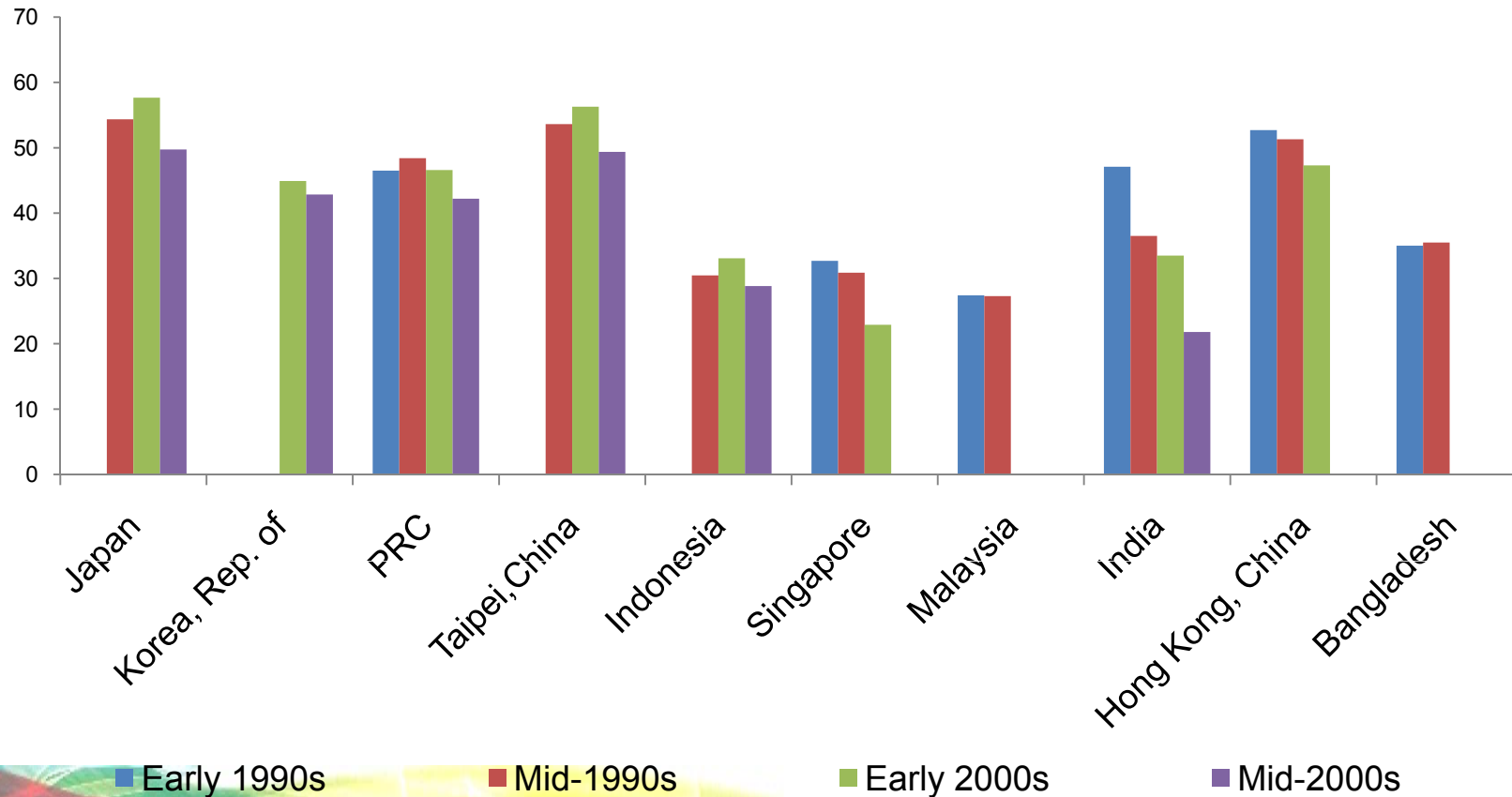
- If inequality had been stable, additional 240 million (6.5% of Asia's population) would have been lifted out of poverty
- Inequality can weaken the basis of growth itself by:
 - leading to a waste of human capital
 - undermining social cohesion
 - hollowing out the middle class
 - worsening the quality of governance
 - increasing pressure for inefficient populist policies

Why inequality has risen

- Technological progress, globalization, and market-oriented reform have led to rapid growth in Asia, but working together they have favored:
 - capital over labor
 - skilled over unskilled workers
 - Cities/coastal regions over rural/inland areas
- Distributional impact of the drivers of growth has been compounded by unequal access to opportunity due to social exclusion.

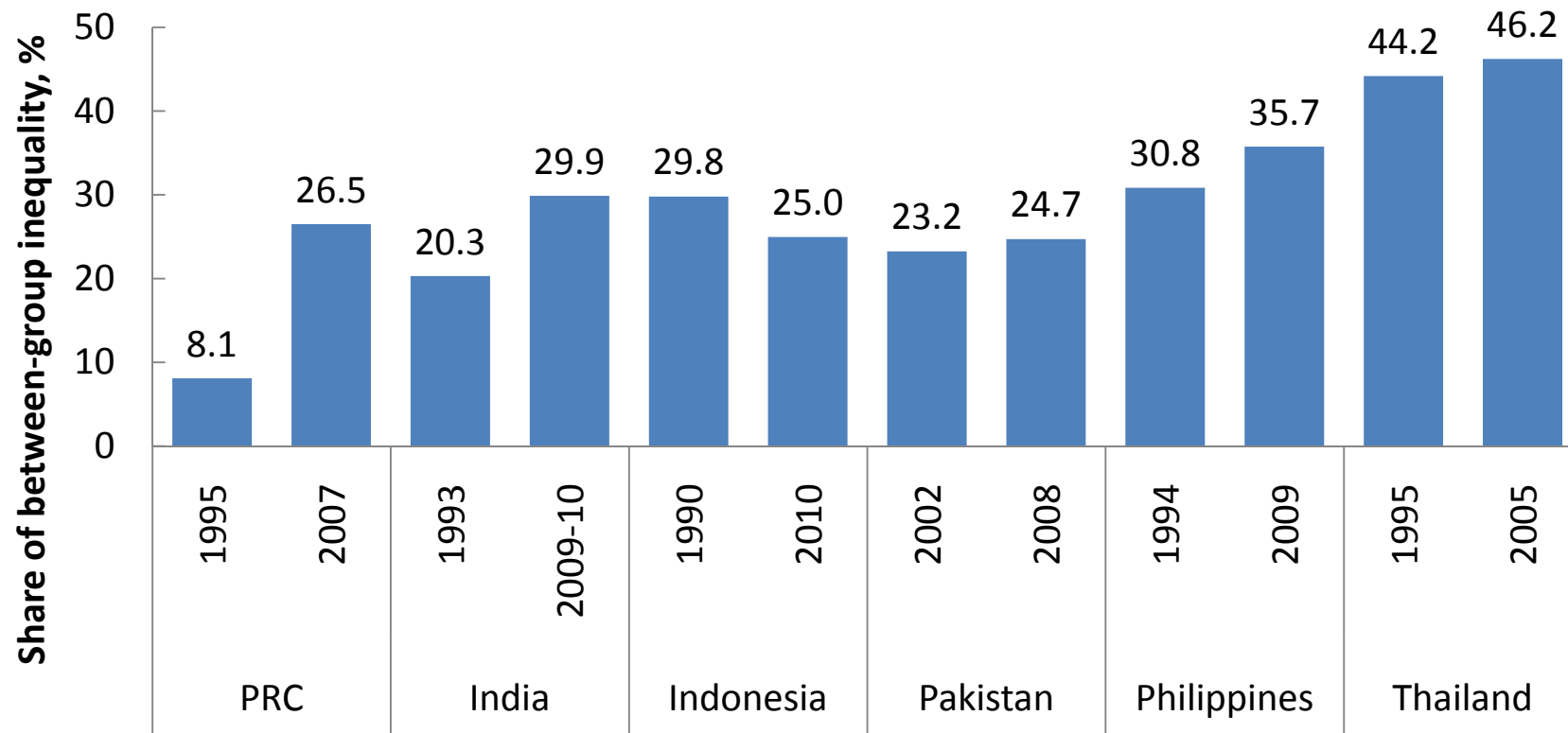
Share of labor income declined, and share of capital income— which is more unequal—increased

Labor Income Share
Manufacturing

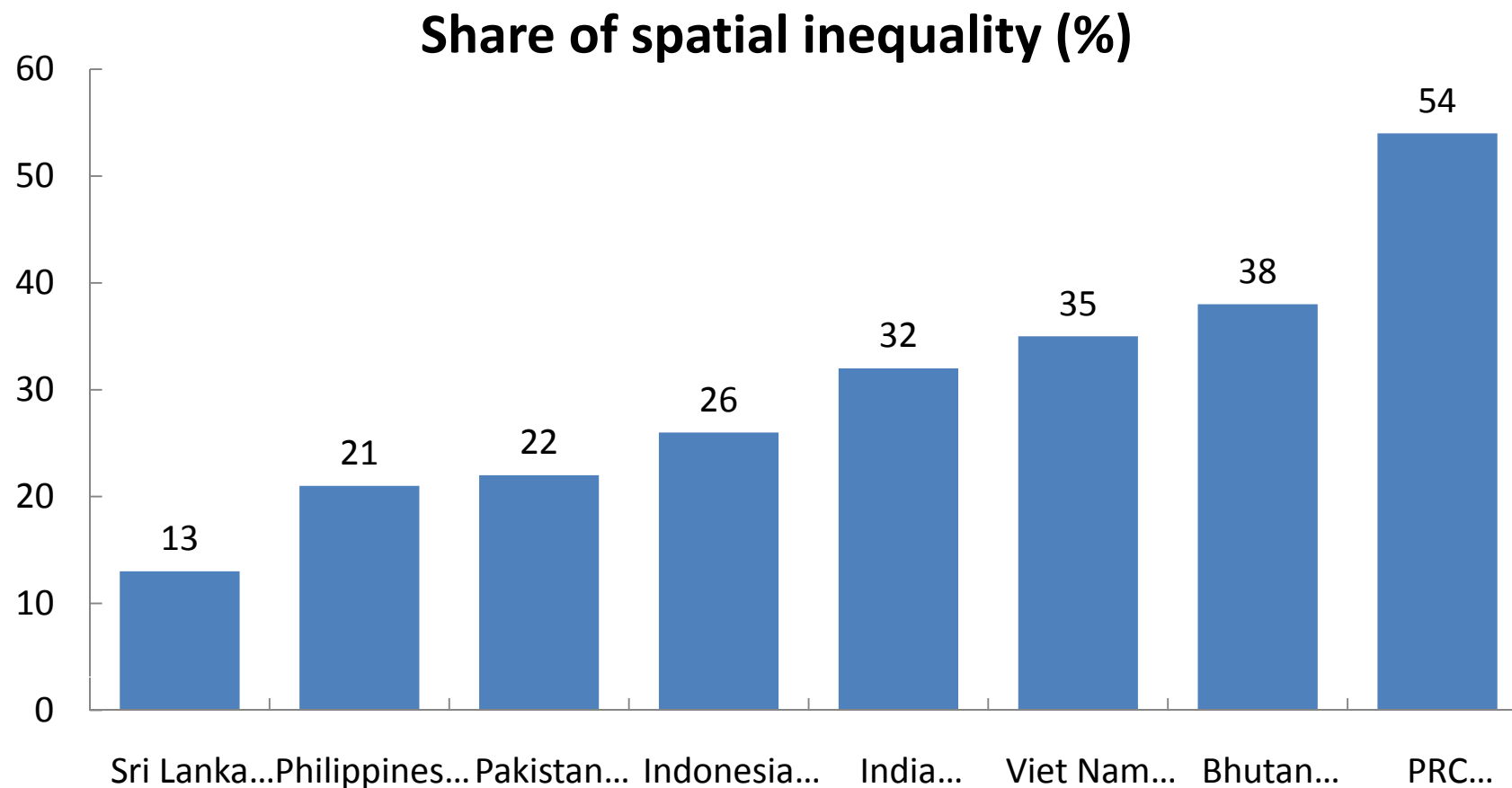


Skills premium has risen; education inequality accounts for 25–35% of total inequality

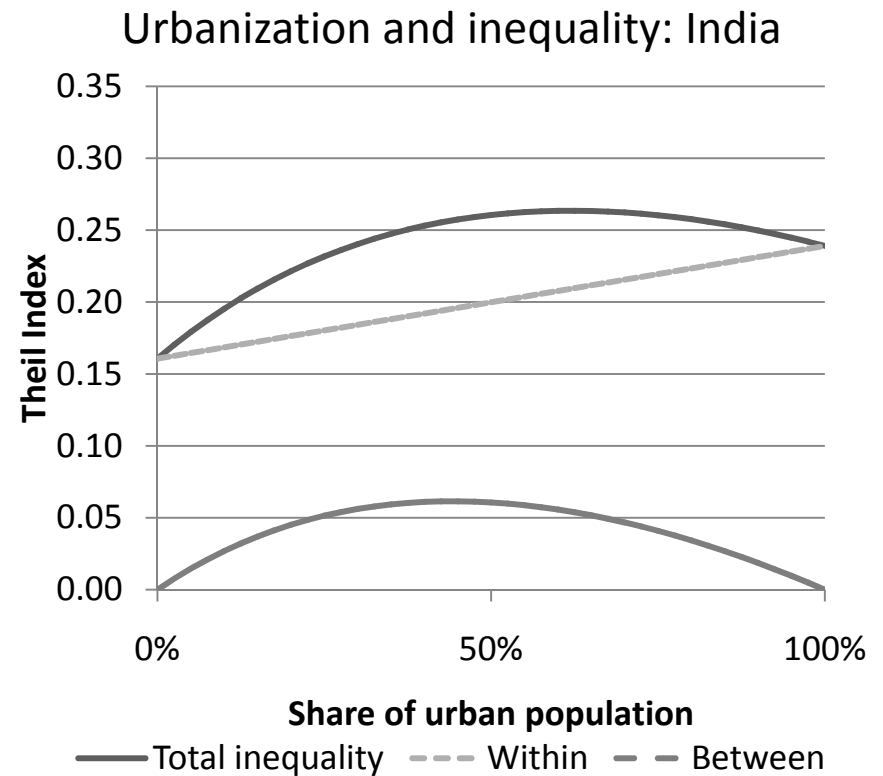
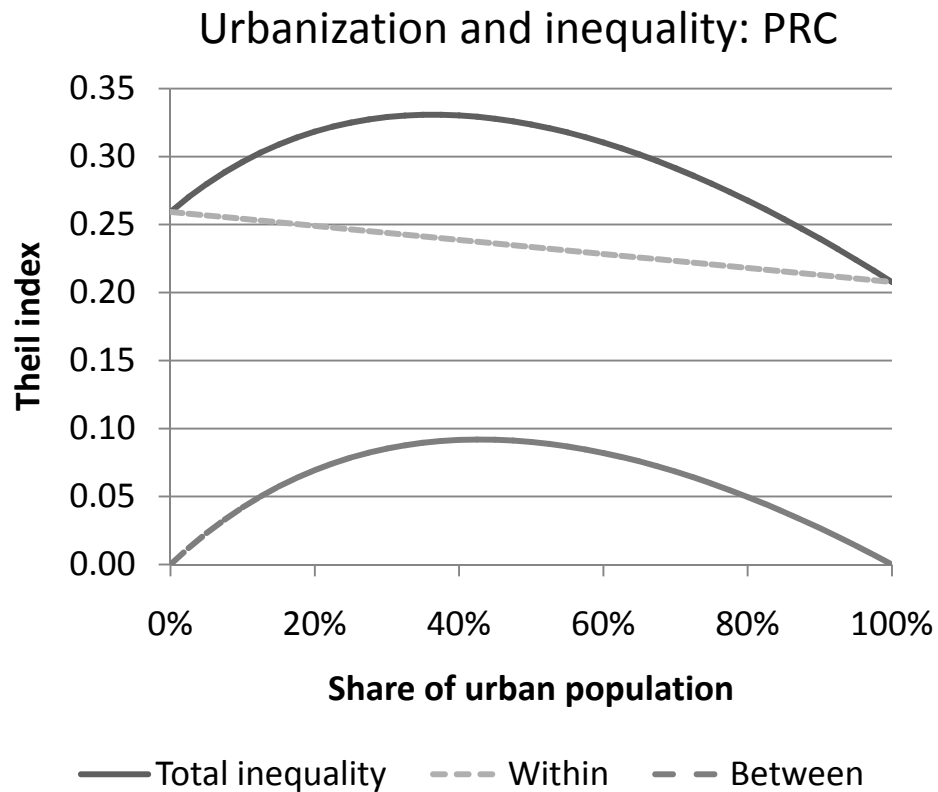
Income inequality decomposition by educational attainment of household head



Spatial inequality—urban-rural and inter-province combined—accounts for a large share of total inequality



Urbanization also affects inequality



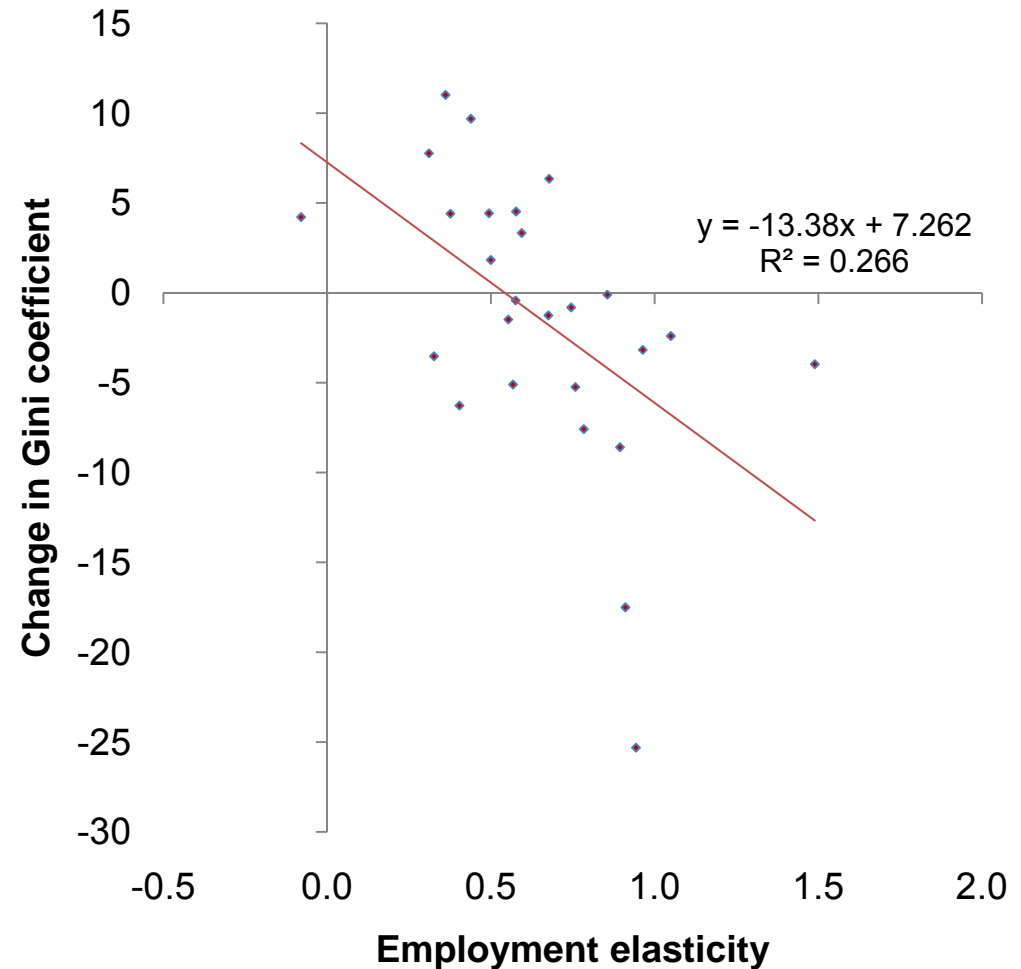
- Assuming urban inequality, rural inequality and urban-rural income ratio remain constant, Kuznets (1955) shows mere population shift from rural to urban areas leads to an inverted-U curve: inequality first increases, reaches a turning point, and then decreases.
- Analysis shows PRC has already passed the turning point, and India has a long way to go.

How to respond to rising inequality

- Three drivers of growth cannot be hindered
- Governments can reverse rising inequality through
 - Growth that is more employment-friendly to increase labor's income share
 - Interventions to address lagging regions to reduce spatial inequality
 - Efficient fiscal measures to reduce inequality in human capital
 - Move towards an inclusive growth strategy

Make growth more employment-friendly

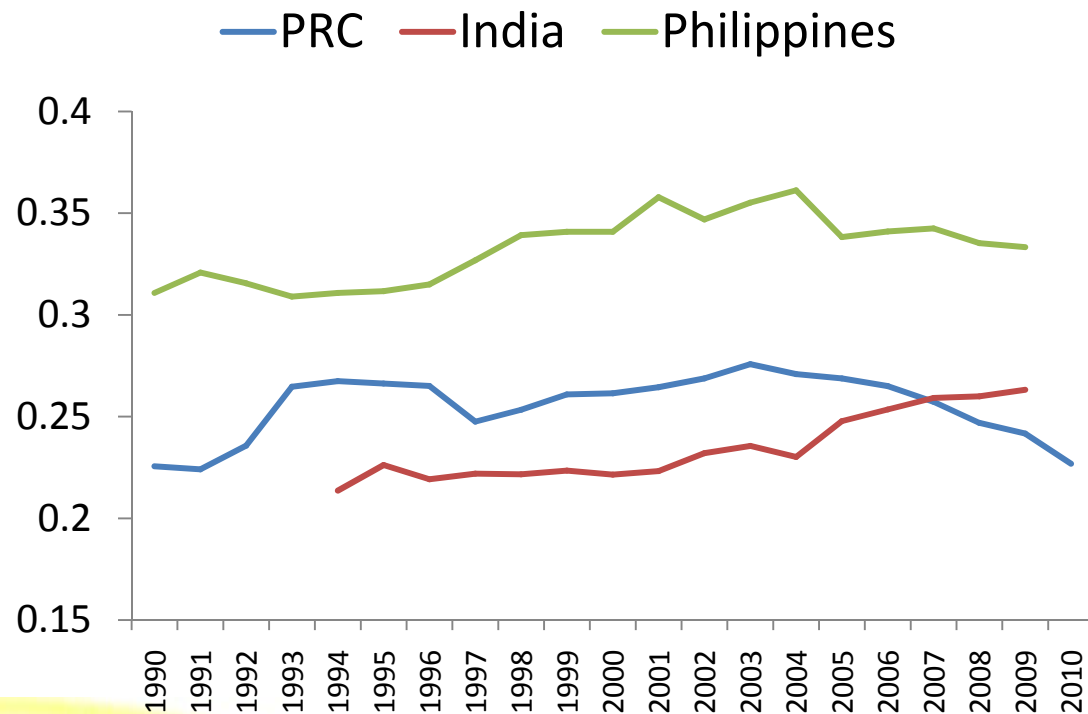
- Structural transformation for more balanced composition of growth
- Support development of SMEs
- Remove factor price distortions that discourage the use of labor
- Strengthen labor market institutions



Interventions to address lagging regions

- Improve regional connectivity
- Develop growth centers in lagging regions
- Fiscal transfers to poorer areas to enhance human capital
- Remove barriers to within-country migration

- PRC's Great Western Development Strategy: Inequality of provincial per capita income has been on the decline since 2004 in PRC



Efficient fiscal measures

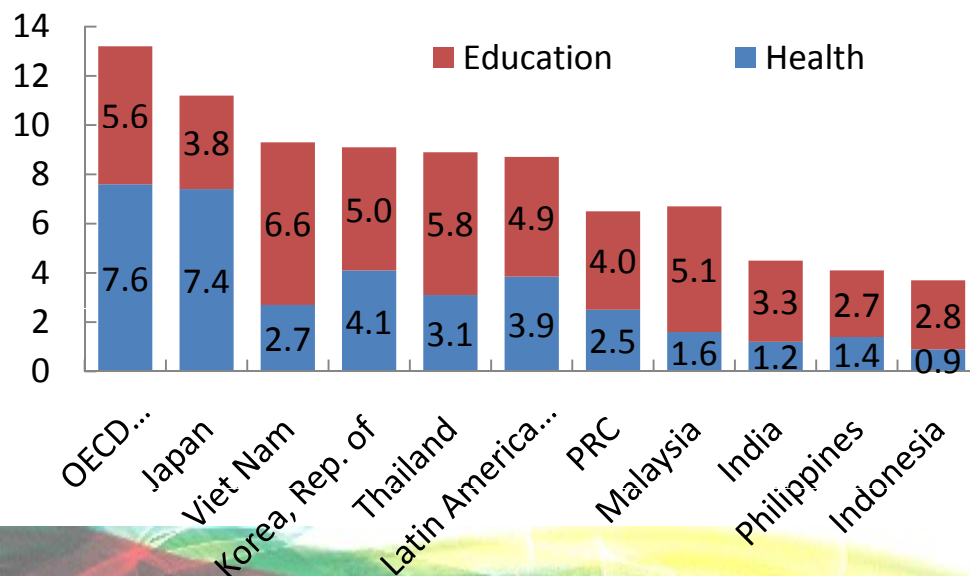
- More spending on human capital and social protection

Estimated marginal impact of government spending on the Gini coefficient

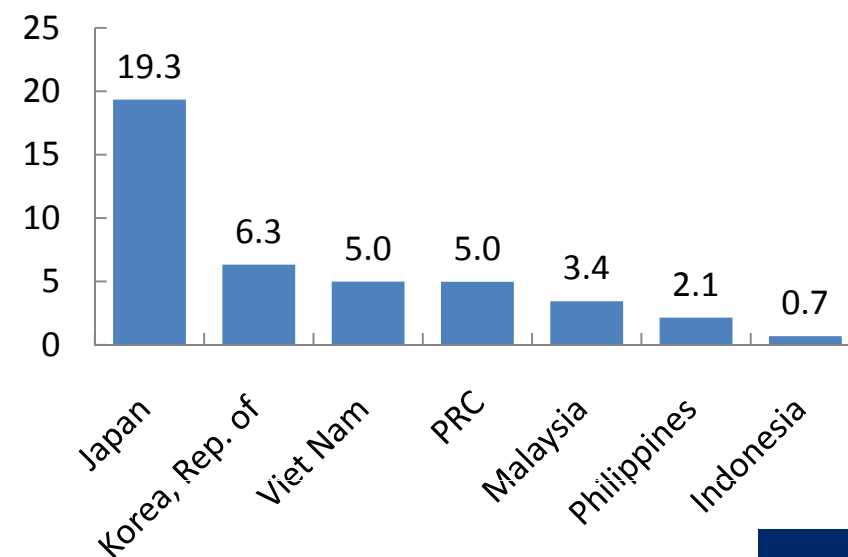
	Asia	Rest of the world
Social protection	0.490	-0.276
Education	-0.486	-0.034
Health	-0.241	-0.330
Housing	2.162	-0.614

Source: Claus, Martinez-Vazquez, and Vulovic (2012).

Government spending on health and education, 2011 or latest year available (% of GDP)



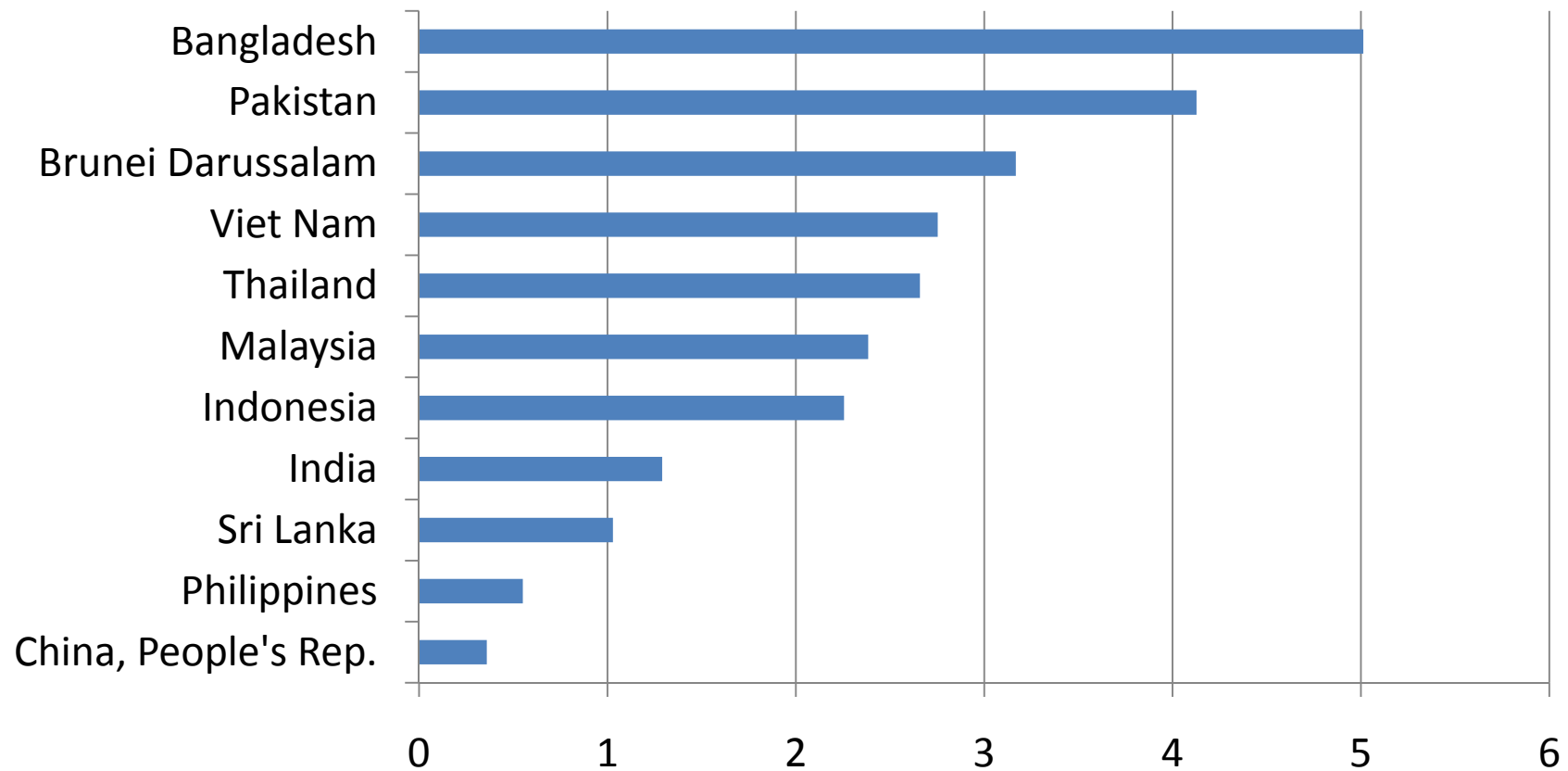
Social protection expenditure, 2010 or latest year available (% of GDP)



Efficient fiscal measures

- Switch from inefficient general subsidies to targeted transfers

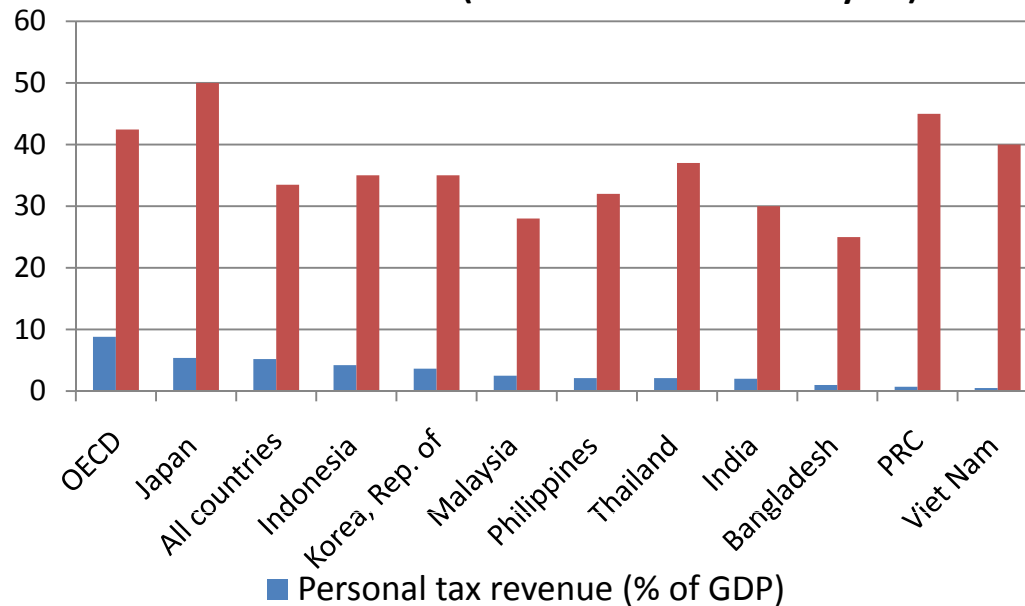
Fossil-fuel consumption subsidy (% of current GDP), 2010



Efficient fiscal measures

- Greater and more equitable revenue mobilization: Level of personal income tax is low in Asia due to narrow tax base and weakness in tax administration

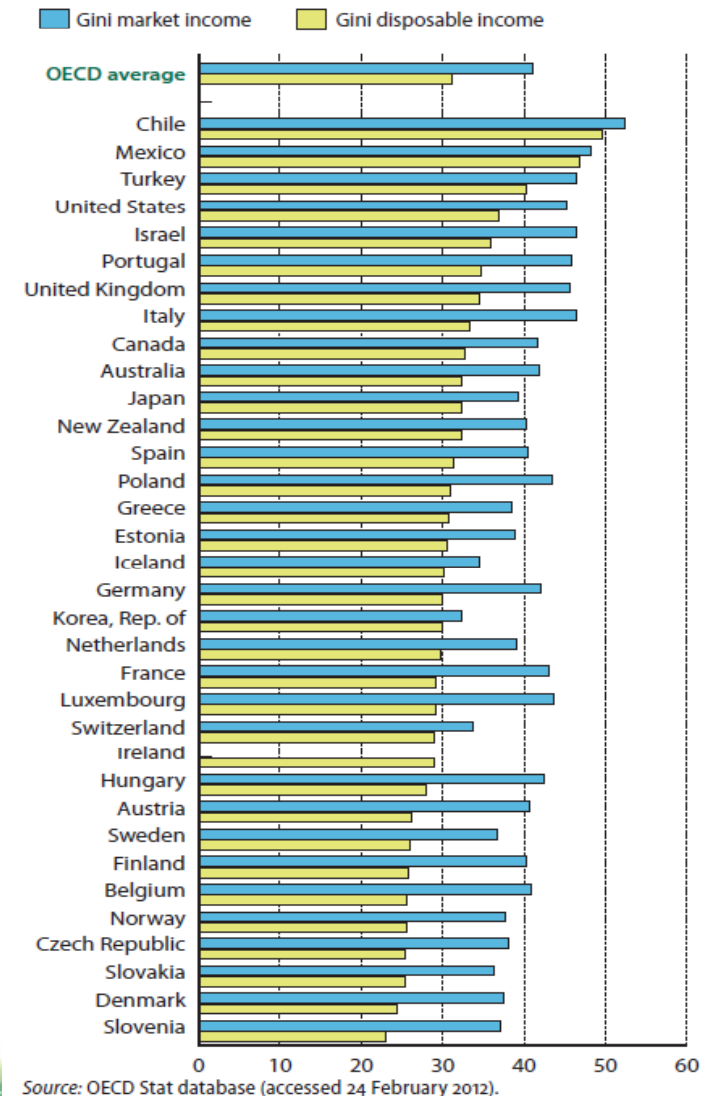
Personal income tax (% of GDP) and top marginal income tax rate (2009 or latest available year)



Redistribution effect of personal income tax in urban PRC

Year	Pre-tax Gini	After-tax Gini
1997	30.1	29.6
2005	35.2	34.2
2009	34.7	33.5

2.2.9 Gini coefficients of OECD countries, 2000s



Source: OECD Stat database (accessed 24 February 2012).

Move towards inclusive growth

- Inclusive growth means everyone can participate in and benefit from the growth process on an equitable basis.
- Inclusive growth makes a distinction between
 - Inequality due to differences in individual efforts, and
 - Inequality due to differences in individual circumstance, or inequality in opportunity.
- Reducing or eliminating inequality in opportunity is at the heart of an inclusive growth strategy.
- So inclusive growth can also be defined as “growth coupled with equality of opportunities”.

Figure 1 Policy Pillars of Inclusive Growth



Source: Adapted from Zhuang (2010).

Key messages

- Asia faces the challenge of rising inequality:
 - Rapid growth has favored capital over labor, skilled over unskilled workers, and coastal regions/cities over inland/rural areas
- Asian countries need to confront rising inequality through
 - Efficient fiscal measures, interventions to reduce regional disparity, and growth that is more employment-friendly, and
 - Move toward an inclusive growth strategy that is based on equality of opportunity

Thank you!

The presentation is based on Asian Development Outlook 2012.

For the full report, please visit

ADB web site at

www.adb.org

For more details on the concept of inclusive growth, please read the book *Poverty, Inequality, and Inclusive Growth in Asia: Measurement, Policy Issues and Country Studies*, edited by J. Zhuang, published by Anthem Press in 2010

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