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## Labor Migration and Wage Inequality

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**Labor immigration in China seems to have positive effects on wage growth for both labor migrants and local workers**

**Xiaohan Zhong**

Since the beginning of China's reforms and especially after the late 1980s, the system of permanent residence registration (Hukou) and related government policies, which had been preventing people from migrating for several decades and had thus resulted in the segmentation of the labor market, gradually but persistently became less strict. Labor from less-developed rural areas in mid and west China flocked into developed urban areas along the eastern coast.

The impact of this so-called "tide of rural labor" has seen rural migrants taking jobs unoccupied by urban workers and thus coming to dominate in all kinds of unskilled occupations, such as construction workers, repairers, waiters, cleaners or nannies. Related to (but probably not resulting from) such an occupational segmentation, rural migrants have been earning much lower salaries than their urban counterparts. Additionally, labor flows have not led to wage convergence across regions. On the contrary, in the past two decades the trend has been divergence between urban and rural labor, and east and west regions.

The theoretical model proposed in our research paper is based on Kremer and Maskin (1996). The model gives a specific production function, where a typical production process can be accomplished only through the cooperation of workers playing different roles, e.g. "white-collar" and "blue-collar" workers. There are two assumptions: first, there are imperfect substitutions of skills in these two roles, and second, the relative importance of these skills differs. Under some conditions, our theoretical model shows that:

- After entering urban labor markets, the less-skilled rural migrants will do blue-collar work only, and urban workers will do white-collar work only, thus, these groups exist alongside each other with no crossover or mixing.
- Real wages of rural migrants in urban labor markets will remain unchanged, and those of urban workers will rise.

### Labor Migration Benefits All Workers

The implications of the model are quite striking: labor migration, through cross-match, benefits both rural and urban workers. However, the wage gap between rural migrants and urban workers increases. Finally, occupational segregation and wage differentials are both outcomes of skill differentials, no causality exists between them. East-west regional divergence can also be explained by using a variation on this model.

How does labor immigration affect local wage growth? In our analysis, which uses provincial cross-sectional data in various periods after the reform and averaged across years, we find that throughout the reform era, labor immigration was increasing local workers' wage growth rate. In a typical year, 1% labor immigration (as a share of the local population) raises local wage growth rate by roughly 1% (see Graph).

From the above theoretical and empirical analyses several important implications follow: first, skill differences seem to be root causes of both wage inequality and occupational segregation. Thus, education might be the single most important approach to eliminating the 'dual labor market' and related inequalities. Second, labor migration has really been a reform without losers. The theory explains why there are hardly any tensions between rural migrants and urban workers, at least from the urban side. Third, wage inequality may be a natural result of resource re-allocation by markets, and not by policy discriminations. Regional divergence may not be a bad thing at all—wage differentials and occupational segregation are at least better than market segmentations, for everyone involved.

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