CHAPTER 10

Wage Increase, Wage Convergence, and the Lewis Turning Point in China

Cai Fang and Du Yang

1 Introduction

In recent years, there have been multiple empirical studies arguing whether or not the Chinese economy has reached its Lewis Turning Point (for example, Minami and Ma, 2010; Yao and Zhang, 2010; Zhang and Wang, 2009; Cai, 2010a). Although those studies provide both supporting and contradicting evidence and disagreements remain, there remains room for further investigation. First of all, defining a Lewis Turning Point would help clarify the argument. Secondly, investigating the empirical results based on certain criteria of the Lewis Turning Point would help correctly interpret the data, which might otherwise lead to dissent. This paper is intended to provide more evidence on the arrival of the Lewis Turning Point based on a clearer definition of its more-or-less agreed-upon criteria.

According to Lewis (1972) and Ranis and Fei (1961), a Lewis Turning Point can be referred to as the period of time at which expansion of labor demand exceeds that of labor supply and, as a result, the wage rate of ordinary workers starts to rise while the wage of the agricultural sector is not yet determined by its marginal productivity of labor, and the difference in marginal productivity of labor between agricultural and non-agricultural sectors remains. The time when the wage rates in agricultural and non-agricultural sectors are both determined by their marginal productivity of labor while the gap in productivities disappears can be called the commercial point. Only at this time will dual economic systems end. This paper is intended only to discuss the Lewis Turning Point by examining the trends in wage changes.

Based on the Japanese experiences of achieving a turning point, Minami (2010) suggests five characteristics of wage-related changes as criteria to test the advent of the Lewis Turning Point. That is, if the Lewis Turning Point arrives, one can empirically observe that (1) wage in the subsistence sector equals the marginal product of labor, (2) wage in the subsistence sector becomes determined by marginal product of labor, (3) wages in the subsistence sector jump from a constant (or slowly increasing trend) to a rapidly increasing trend,
(4) wage differentials between unskilled and skilled workers tend to decrease, and (5) there is a trend that the elasticity of the labor supply shifts from being indefinite to be between zero and infinite.

It is obvious that Minami set those criteria to test the commercial turning point rather than the Lewis Turning Point. He himself agrees that the first criterion is too strict to directly test, and that empirical works should be devoted more to other criteria, instead. Since this paper aims to define the Lewis Turning Point in a different way, we will focus on discussing the third and fourth criteria—namely, the increase of ordinary workers' wages and the wage convergence between unskilled and skilled workers.

In the development of a dual economy characterized by an unlimited supply of labor, the wage rate of ordinary workers typically remains at a constant subsistence level above marginal productivity of labor in agriculture. The reallocation of an agricultural surplus labor force to non-agricultural sectors begins with the introduction of a household responsibility system in the farming sector, which in China has made extraordinary progress as the institutional barriers deterring labor mobility were eliminated in the urban labor market. In the country's 30-year period of reform, rural surplus laborers have experienced a shift from agricultural to rural non-agricultural sectors, a mass migration from rural to urban sectors, and from the central and western regions to the coastal regions. As the labor policies adjust to be more tolerant and friendlier towards labor mobility across regions and sectors, migrant workers have become a significant component of employees and residents in urban areas. In 2009, the stock of rural laborers having migrated beyond township boundaries reached 145 million, a figure which significantly mitigated the extent of the labor surplus in China's agricultural sector. Meanwhile, China's demographic transition has reached the phase at which the increase in the working age population is diminishing. Given the continuously increasing demand of the overall economic growth for a labor force, a scenario is appearing in which the growth of labor demand exceeds the growth of labor supply.

Accordingly, a shortage of labor, especially a shortage of migrant workers, appeared in the coastal areas in 2003 and then became widespread throughout the country. As can be expected from the turning point theory, wages of migrant workers substantially increased with an annual growth rate of 10.2 percent in the period of 2003 to 2009. In addition, the wage rates of hired workers in agricultural sectors have also increased, indicating a consistency among the

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1 The wage constancy is only an abstract expression in theory. Because the subsistence standard changes over time, subsistence wage rates change as well, which has, however, no nexus with marginal productivity of labor.