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## Urbanisation in China: The impact of the tax-sharing system and the definitions of new strategies

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**Urbanisation in China:**

**The impact of the tax-sharing system and the  
definitions of new strategies**

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## Abstract

This working paper examines the evolution of Chinese cities and the challenges they are currently facing. It aims to identify possible patterns of urbanisation in the next forty years.

The first part analyses the transformation of Chinese cities as a consequence of the economic policies implemented within the country. The authors argue that the economic reform has accelerated China's urbanisation. Other factors of this massive urbanisation include the improvement of transport infrastructures and the transformation of China's industries.

The reform of the tax system between central and local authorities in 1994 is also examined, and its consequences on urbanisation, and its limitations.

Based on this analysis, the second part introduces the possible strategies China may adopt for the development of its cities. The objective of these policies will be mainly to control the path of urbanisation to prevent the emergence of super large city and encourage the creation of city networks. Future urban policies will also need to tackle such issues as rural flight and environment protection.

**Keywords:** urbanisation, China, tax-sharing system, super large cities

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# Urbanisation in China: The impact of the tax-sharing system and the definitions of new strategies

By Miguel Elosua, François Gipouloux, Sébastien Goulard, Li Shantong and Ni Pengfei

## Introduction

Chinese cities have been through many changes since 1949. China's population has evolved from rural to urban; for the first time, in 2011, city dwellers exceeded rural populations. China's urban strategies have also evolved, consequently. The economic models adopted by the central government have had a strong impact on the development of Chinese cities. China's open policy and subsequent marketisation have led to massive urbanisation. This phenomenon has created new opportunities for development, but new urban issues have emerged as well. It has been noted that Chinese cities have experienced rapid territorial expansion. Today, China is searching for a new model that would associate economic growth and social stability to urbanisation. In a first part, this paper will look at the link between the 1994 tax reform and the expansion of Chinese cities, and will analyse the central-local relations in terms of fiscal resources and expenditures. These relations have favoured the creation of super large cities. Local governments have actively pursued land development as a means of financing this urbanisation. Is this model sustainable? What urban planning strategy will be adopted to regulate and control future urbanisation? In a second part, the paper will focus on new patterns of urbanisation of Chinese cities. Several topics have been identified as the main issues that will shape China's future urban strategies, including increasing urbanisation, rebalancing urban development and protecting the environment.

## I. Evolution of China's urbanisation

Over the past 60 years, China has experienced rapid urban development. In 1949, China's urban population was about 40 million, accounting for 7.3% of the total population. The approximate urbanisation rate at the time was 10.64%, but by 2011 it had reached 51.27%, culminating in an urban population of approximately 690 million<sup>1</sup>, exceeding the rural population for the first time.

From 1949 to today, the progress of urbanisation in China can be divided into three stages:

- During the first stage (1949-1961) the Chinese government chose to develop heavy industry as its primary strategy. Consequently, the urbanisation rate rose from 15.4% in 1957 to 19.4% in 1960<sup>2</sup>.

<sup>1</sup> 2011 Zhongguo chengshi fazhan baogao fabu: Chengzhen hua lu da 51.27% 2011中国城市发展报告发布：城镇化率达51.27% <http://www.nbd.com.cn/articles/2012-05-21/655098.html>, (accessed 20 February 2013).

<sup>2</sup> Xiao xiang肖翔 (2011) « Zhongguo chengshi hua yu chanye jiegou yanbian de lishi fenxi (1949 nian-2010 nian) 中国城市化与产业结构演变的历史分析(1949—2010), Research in teaching. Vol.6, pp. 18-25

- During the second stage (1961-1978) the government worked to decentralise the urban residents and relocate them to rural areas, due to a food shortage that resulted from the excessive focus on the development of heavy industry in the first stage of urbanisation. The government also set about reducing the proportion of industrial workers in the labour force. This strategy, in turn, triggered a separate phenomenon: industrialisation was not accompanied by a corresponding increase in urbanisation. Thus, even though the urban population increased from 127 million in 1961 to 167 million in 1977<sup>3</sup>, the rate of urbanisation declined from 19.3% to 17.6% during the second stage.
- During the third stage (1978 to today), the Chinese authorities implemented a policy of industrialisation. In contrast with the second stage, this was accompanied by significant progress in urbanisation. China's urbanisation rate increased from less than 19% in 1979 to 23% in 1984. With the implementation of the "Provisional Regulations for Private Sector of the People's Republic of China" in 1988<sup>4</sup>, the registration of the private sector began all around the nation. The development of the private economy was then mostly concentrated on light industry and the service sector. These sectors are labour-intensive and have been important contributors to the third stage of urbanisation in China. With growing industrialisation, the marketisation of the economy, and the contribution of private and state-owned businesses, the pace of China's urbanisation has accelerated. In other words, the economic reforms in China since 1978 have been instrumental in setting the highly dynamic pace and pattern of urbanisation throughout the country right up to the present.

Several factors have contributed to China's urbanisation, including, among others, economic development, transportation, population growth, and industrial upgrading.

- After three decades of reform and rapid development, China's economic performance has greatly improved. According to common international patterns, when the per capita disposable income of residents is over \$3000, in the middle-low development stage, the per capita consumption will increase quickly. At present, China is in the middle stage of its industrialisation and urbanisation acceleration period. The huge domestic demand provides a big market for economic development across China.
- With regards to the distribution of land resources, Chinese agricultural land area per capita is small and its distribution is uneven; its value increases gradually from south-east to north-west. Cultivated land area totalled 1.826 billion *mu* (a traditional unit of area equal to 1/15 ha) in 2008, but this will decrease to 1.805 billion *mu* by 2020. In other words, 20.74 million *mu* of cultivated land will be turned into construction land over the next 11 years, or 1.9 million *mu* annually. At present, the land required for construction appropriates some 3 million *mu* of cultivated land every year. This is more than the available land supply. Land users are forced to cultivate wastelands, abandoned mines, industry sites and other low efficiency sites in accordance with land regulations, which state: "use one unit and make up one unit". In total, an area of 4 million *mu* is developed every year to make sure that the minimum of 1.8 billion *mu* required for cultivated land in China is protected.
- When it comes to transportation, urban rail planning and construction has been a prominent part of development in urban and rural areas, in such a way that urban central zones have become larger and larger. Initially, the investment in high-speed urban rail focused on the development of large urban clusters. The construction of information infrastructure has also improved inland inter-urban communication and has provided an important boost to the recent development of inland urban areas.
- The 2010 Census data shows that the population of China is now 1.34 billion, about 20% of the world's population. It also shows that population structure has changed recently. In 1987, the neonatal population reached its historical peak of 25.5 million, and then decreased by 480,000 per annum until 2004. In 2003, the

<sup>3</sup> National Bureau of Statistics of China. China Statistical Yearbook, 1984. Beijing: China Statistics Press, 1984.

<sup>4</sup> Zhonghua renmin gongheguo siying qiye zhanxing tiaoli 中华人民共和国私营企业暂行条例  
<http://law.lawtime.cn/d673517678611.html>, (accessed 20 February 2013).

Chinese mortality rate was at its lowest since the 1980s at 6.4%. It then began to increase at 0.13‰ annually (220,000 per annum). As a consequence, an ageing society is becoming an immediate problem. Another change is the rising quality of the labour force as education continues to be improved. Due to all these changes, the urbanisation process faces a variety of major challenges such as developing a comprehensive social security system and increasing job creation. In addition, the population remains concentrated in the eastern part of China and this uneven geographical development continues to present problems.

- In the industrial sector, due to the intensification of global competition and the deepening of the international division of labour, developed countries are transferring and outsourcing low-end manufacturing, other parts of manufacturing and some elements of service production to countries and regions that have open markets and low production costs. Recently, the internationalisation of service activities has proved a significant new feature of global industrial regulation and organisation. While coastal areas have completed the industrialisation phase and are actively moving towards a larger service industry, the western areas of China remain poorly industrialised although it has more advantages than the Eastern seaboard in attracting activities such as low quantity transportation and electronic service industries.
- The increase in the level of domestic economic development and industrial upgrading in the Eastern provinces will cause the price of the factors of production, such as labour, to go up gradually and will force Chinese businesses to continually upgrade their industrial structure. The first to do so will be Eastern and Central cities, such as Shanghai, Beijing, Guangzhou and Shenzhen, and this will include a shift towards services just as has already taken place in Europe.

This review of China's urbanisation so far will help with the task of anticipating the possible urbanisation trends going forward to 2050. It is likely that the patterns, trends and challenges that are already apparent in the progress of urbanisation since 1949 will, to varying degrees and in different economic, social and political contexts, shape the on-going changes in the future, such as the urban-rural balance, the geographical distribution of cities, the changing structure of economic activities in cities, and so on.

It is also necessary to review the influences of fiscal policy on urbanisation. Land acquisition, compensation, and urban infrastructure are all related to the government's tax system, thus playing an important role in shaping urbanisation. In the following section, we look over the fiscal system of China before 1994, and then turn to the present tax-sharing system that was implemented after 1994.

## **II. The 1994 tax-sharing system: background and its impact on urban policies**

### **1. The tax system before the 1994 reform**

The tax-sharing system was established in 1994 in the context of an adjustment by the Chinese government to the pre-existing finance and tax system.

Before 1980, under the "unified income and expenditure" fiscal system, almost all of local government revenue and profits were submitted to the central government, and were then redistributed to the provinces according to an expenditure plan. This was because the new state power was not strong and the task of post-war reconstruction was very demanding. The central implementation of concentrated fiscal system control over income and expenditure quickly made prices stable and improved the country's economic conditions.

Thanks to this fiscal system, a large number of state-owned businesses were created, which gave strong support to the reform and development of agriculture, handicraft industries, industries and commerce. Furthermore, the public ownership of the social economic system was finally established. However, a system of this kind also has some very obvious flaws.

- Firstly, the allocation of social resources is not efficient. In this system, the extreme financial control of the central government means the distribution of social resources must comply completely with the tenets of central planning. This leads to one-sided management of information, as well as failure of supervision, which then leads to financial and economic development decision-making errors and operational failures. This means that economic efficiency and social welfare are compromised, and resource allocation and utilisation cannot achieve Pareto optimality.
- Secondly, this system has an adverse effect on the mobilisation of initiatives taken by local government. Due to the excessive concentration of power, local government lacks autonomy and is subordinate to the central plan. This suppresses the enthusiasm and creativity of all the provinces, departments and businesses, and is not favourable to social productivity and long-term sustainable development. After the reform and opening up, the system was not able to adapt to the needs of the new development trajectory. Therefore, in 1980 the Chinese government reformed the system.

From 1980 to 1994, China used a divided budget system whereby central and local governments had their own independent financial interests. This system had many features:

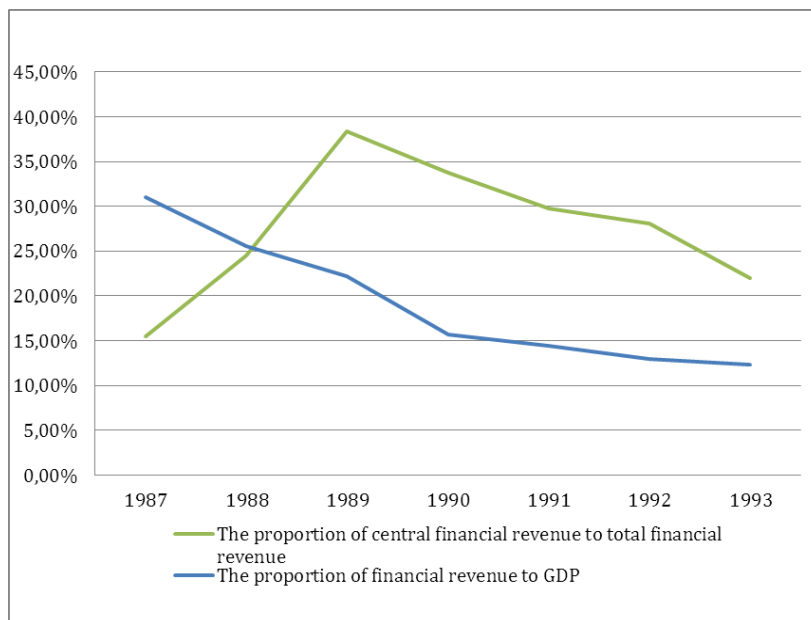
- Firstly, according to the relationship of subordination in the system of economic management provisions, central and local fiscal income range was clearly divided, so that the local fiscal system became a combination of responsibility, power and benefit. Local government was able to independently control its finances. This system encouraged local authorities to expand production so that they could increase their tax revenues.
- Secondly, in line with this economic management system, the fiscal income was divided into four parts: the central fixed income, which included central subordinate business income, tariff income and other income; the local fixed income, which included local subordinate business income, salt tax, farming and animal husbandry tax, industry and commerce income tax, local tax and other local income; 80% of the income of State-owned business, which belonged to the direct management of the centre, was sent to central government; and 20% was kept by local authorities.

Although this tax system was a great improvement on the long-established fiscal system, there were still numerous limitations:

- The government controlled businesses according to a relationship of administrative subordination. This policy limited the vitality of businesses, ensuring that the disadvantages of a planned economy continued. Although the state adopted a "profit share and tax reduction" policy, as a result of too much local government intervention, businesses had no real autonomy. Most of the state-owned business' development faced serious energy shortage; the central government had to make up for business losses. Crucially, there was no standard mechanism of 'survival of the fittest' in the market.
- The reinforcement of the local "fiefdom economy" led to a "reverse adjustment" of the system. At the same time, local government lacked the necessary tax power and stable sources of revenue. Local government liked to support local business and production projects that generated high tax and large revenues. So-called "inverse control" happened frequently. For example, high rates of regulation on cigarettes, liquor and other products limited both production and consumption, but this new tax system also encouraged the creation of more small cigarette factories and distilleries in order to increase the fiscal revenue of local governments. The policy also strengthened market segmentation, and promoted local blockades between regions, including blockades on the flow of high quality raw materials between regions. It also encouraged arranged sales of "own business" products in the local market, and prevented high quality products made in one province entering the market in a different province. This had an adverse influence on the development of a unified market, on the promotion of fair competition between businesses, and on national economic development.
- The country's financial allocation was not rational, and the "two proportions" (the proportion of financial income in GDP and the proportion of the central fiscal revenue in the national fiscal revenue) decreased (Fig. 1).



The central fiscal revenue could not meet the needs of their own spending, and relied on local fiscal income to balance out public spending. Moreover, it could not guarantee the necessary concentration of the government financial resources; the financial control of the central government was limited, and largely contributed to weakening the ability of central government to regulate and reducing central finance to a passive role. In this role, implementing macroeconomic policy was difficult because, for one thing, the central government was unable to use tax policy as a tool for stable and balanced economic development.



**Figure 1: The ‘two proportions’ before 1994**

In the light of these developments and the demand for a more practical system, the Chinese government worked to put in place a reform of the tax system in 1994.

## 2. Implementation of the tax-sharing system since 1994

In 1994, China cancelled the contract system for taxation and began to implement the tax-sharing system. The main goal of this new policy was: to strengthen the control of central government over sources of tax revenue; to raise the proportion of the central fiscal revenue in the national fiscal revenue and the proportion of fiscal revenue in GDP; and to resolve the conflict of interest between the central and local authorities.

Therefore, taxes were divided into a central fixed tax, a local fixed tax, and a shared tax between the central and local authorities with a view to stabilising the financial relationship between the two.

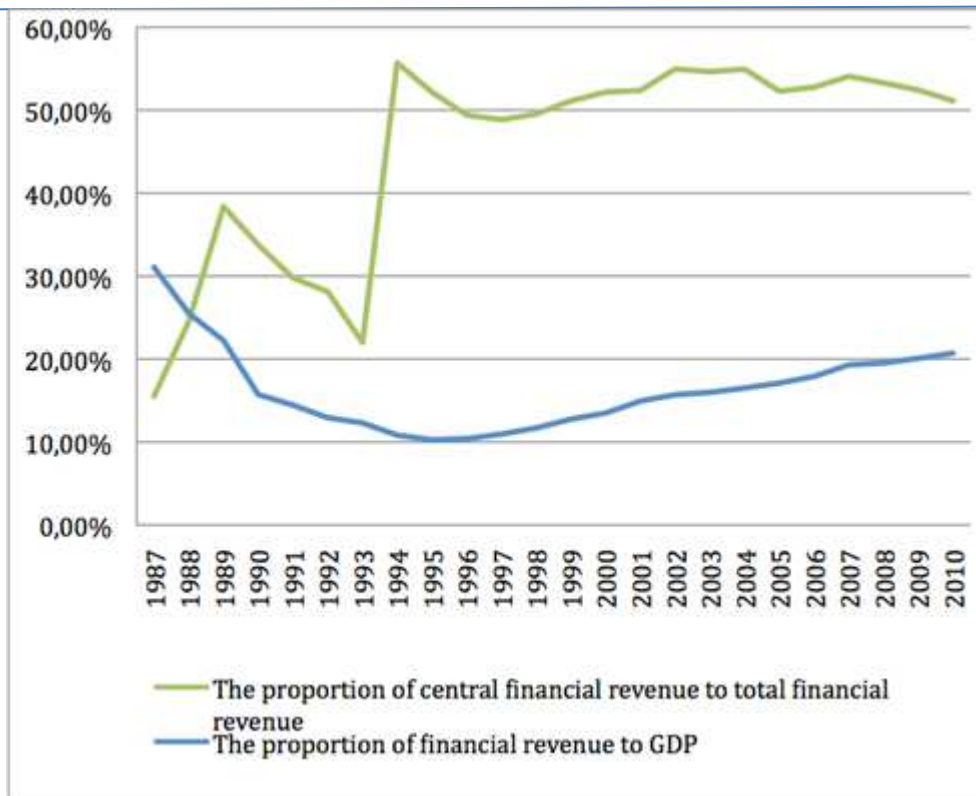


Figure 2. The 'two proportions' after 1994

In addition, the corresponding fiscal expenditure range is determined according to the powers of the central and local governments. The expenditure of central government includes mainly: the basic construction investment of central management; the expenses associated with technological transformation, new product development and geological exploration in state-owned businesses directly under the central government; the cost of national defence; funding the police; diplomatic services and foreign aid; the central administrative costs arising from culture, education, health and other expenditures; as well as the costs of servicing the domestic and foreign debt borne by the central government. The local fiscal expenditure mainly includes: the basic construction investment of local co-ordination; the costs of technological transformation, new product development and agriculture support for local state-owned enterprises; urban maintenance and construction; local culture, education, health fees and administrative expenses; price subsidies; and other expenditures.

The implementation of the new tax system has achieved good operating results, as illustrated by the "two proportions" increase, and in the enhancement of central macro-control capacity (Fig. 2). The new system has promoted the formation of a unified market, curtailing the problems of regional blockade and local protectionism. Simultaneously, it has promoted the adjustment and the optimisation of the economic structure.

The objective of the tax-sharing system has not only been to improve the fiscal system but also to raise the proportion of the tax revenue that the Chinese central government would collect. The tax-sharing system has generated a great increase in central fiscal revenue. However, it has also caused some problems, such as unclear responsibilities for financial expenditure, and inequity to the tax levy items.

### III. New strategies adopted by Chinese cities

What strategy will be adopted regarding the development of Chinese cities? Will urban China consist of a few super large cities or will we see the emergence of a network of middle size cities?

#### 1. Increasing urbanisation

In 2011, for the first time, China's urban population exceeded its rural one. A least 10 cities now have more than 5 million inhabitants, and cities with more than 1 million inhabitants are widely spread across the country.

There are several different estimates on the speed and level of urbanisation in China predicted for the next few decades up to 2050 among research communities. The National Development and Reform Commission (2000) believed that the speed of urbanisation in future would not exceed one per cent per year<sup>5</sup>. Chen Shurong (2000) thought that if we consider the reality of China, the defined target about 60% would be more accurate. However, the reality of the development of urbanisation shows that such estimates are too low<sup>6</sup>. The Development Research Centre of the State Council (2000) argued that the true level of urbanisation in China may reach 70%, which is higher than the statistic for migrant workers who participate in the economic activity of the city but are not calculated in the city population<sup>7</sup>. Zhang Yan (2010) also predicted about 70% in 2050 by using a logistic pattern<sup>8</sup>. Some estimate even higher. Chen Jiaojun and Jing Puqiu (2008) estimated that by 2050 the ideal urbanisation rate will be 74.03%<sup>9</sup>. Li Shantong (2001) proposed that urbanisation rate will increase by 1.5 per cent per year, and it will therefore reach more than 70%<sup>10</sup>. Similarly, Lu Xueyi (2011) held that the urbanisation rate will exceed 70% or even 80% in 2050<sup>11</sup>.

The World Bank (2013) calculated that China's urban population would increase by about 500-600 million between today and 2050<sup>12</sup>. McKinsey Global Research Centre (2009) pointed out that the level of urbanisation in China will reach 70% and the urban population will be more than one billion in 2050.

The economic reforms implemented since the '80s have led to an intense urbanisation, which has been controlled by authorities thanks to several tools such as the *hukou*.

This trend will continue as urbanisation is considered a way of reducing regional inequalities. Even with the residence permit limitation, a labourer can improve his overall revenue and living conditions by becoming an urban resident. At the same time, through remittance, he is contributing to the economic and social development of his local village. Urbanisation does contribute to reduce the economic and social gaps existing between rural and urban areas. As a result, the urbanisation rate will continue to increase, and may even catch up with Western countries.

#### 2. Rebalancing urban development

<sup>5</sup> Macroeconomic Research Institute of the State Development Planning Commission Task Force. 2000. Several issues of the implementation of the urbanisation strategy during the Tenth Five-Year Plan period. *Journal of Macroeconomic management*. 4, pp.4-7

<sup>6</sup> Chen Shurong (2000) The current situation, issues and development prospects of China's urbanisation. *Journal of Urban problems*. 1, pp.3-5

<sup>7</sup> Development Research Center of the State Council. (2000) The Tenth Five-Year Plan Research Group: Orientation of macroeconomic reforms during the Tenth Five-year Plan. *Journal of Economic worker learning materials*, 41:53-56

<sup>8</sup> Zhang Yan and Huang Zhilong (2010). Re-examine the level and pace of urbanisation in China. *Journal of Urban Development Studies*. 11, pp.1-6

<sup>9</sup> Chen Jiaojun and Jing Puqiu (2008). The new urbanisation theory and the development target prediction. *Journal of Economic Perspective*. 9, pp.4-15

<sup>10</sup> Li Shantong (2001) Further understanding of urbanisation. *Journal of China's Soft science*. 5, pp.25-28

<sup>11</sup> Sina (2011) Social sciences researcher predict China's urbanisation will be more than 70%, quoted from Sina <http://news.sina.com.cn/c/2011-12-21/075923667870.shtml>, 2011 December 21th.

<sup>12</sup> Securities Times (2013) Path dependence: Unique urbanisation in China, quoted from Securities Times [http://epaper.stcn.com/paper/zqsb/html/epaper/index/content\\_435480.shtml](http://epaper.stcn.com/paper/zqsb/html/epaper/index/content_435480.shtml), 2013 January 12th.

The national policy is to encourage the expansion of small and medium size cities and limit the sprawl of megalopolises. The *hukou* system, which was recently made more flexible, approved at the 11<sup>th</sup> National People Congress (2011), illustrates this trend:

*“In super large cities, the population should be controlled rationally. In large and middle-sized cities, the population management should be strengthened and improved, so as to keep on exerting the important role of absorbing migrant population. In middle and small cities as well as small towns, the conditions of population transformation should be broadened according to the real situation. Encouraging different areas or districts to explore related policies and measures, so as to define the scale of the population being transformed.”<sup>13</sup>*

This policy aims at rebalancing development in China and filling the gap between an urban developed area in coastal regions and a rural hinterland.

Three main measures will need to be carried out in order to get this balanced urbanisation: the prevention of super large cities’ expansion, the creation of satellite cities and the integration of urban villages.

### ***Preventing the expansion of super large cities***

Central authorities are willing to control the expansion of large cities and develop second tier cities. However, they may face resistance from local governments. To some extent, city creation and urban expansion led to an increased bargaining power for local governments with the central government. The fiscal system put in place in 1994 has weakened the financial stability of local governments. In this context, urban development seems to be the easiest and safest source of revenue for local authorities. Land and property prices have been increasing as a consequence – such an increase suits the financial interest of the local government, but not necessarily the central government’s. Local government tax represents a fairly high proportion of total real estate costs. Some developers assess that local government tax revenue represents 50% of the direct cost of the real estate sector (or 40%)<sup>14</sup>, 10% represents financial costs, 30-40% building/production cost. They argue that the best way to reduce real estate costs and prices would be to reduce the share of local government taxes. However, as local government cannot survive without these taxes, it is unlikely that such a reduction will occur, especially if the central government does not modify the current tax system.

Conflicting interests between local and central government are growing because the central government does not support the local government, in favour of concentrating on national urbanisation priorities. Our interviews reveal that the decision-making process on urban development lacks coordination between the central and local authorities. In fact, interviews with local urbanisation planners revealed no compliance with state-level set priorities. Autonomous cities, such as Shanghai, seem to have advantage on the policy-making side, especially in term of efficiency and consistency, as there is less need for coordination.

### ***Planning satellite cities, the case of Shanghai***

Because large cities need to limit their expansion to meet sustainable development, new cities have been planned in the fringes of large cities to alleviate city centres from demographic and economic pressure.

The concept of satellite cities has already been used in Europe, but its execution in China differs from the European model because of scale. The municipality of Shanghai is a good example of how satellite cities are managed in China and illustrates the challenges city authorities face as regards planning activities and transportations.

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<sup>13</sup> Chapter 20: *Actively and steadily promote urbanisation*; The Twelfth Five-Year Plan for National Economic and Social Development of The People's Republic of China, Approved at the fourth session of the 11<sup>th</sup> National People's Congress, March 14, 2011, (Unofficial summary translation)

<sup>14</sup> Interview, Shanghai, March 2012.

In the case of Shanghai, satellite cities were planned as economic hubs where residents could work, but it appears that most satellite cities' residents still work in Shanghai downtown. The last Shanghai Master Plan (1999-2020) introduced the "1-9-6-6 Model". This new concept of urban structure redefines the hierarchy of the Shanghai area with a three-layered structure: one city centre oriented towards the service sector; nine decentralised "key cities" that serve as administrative centres (300,000 to 1,000,000 residents) and sixty small towns (50,000 to 150,000 residents). Six hundred villages (2,000 residents) are also included, completing the "1-9-6-6 Model". The main impetus behind this plan was to re-house one million people from the city centre to the surrounding areas. It also aims to better control Shanghai's urban sprawl.

Improvements to the public transportation system (such as the creation of a fast and reliable subway network in Shanghai) are an answer to this issue. However, in the long run, new policies should be put in place to develop activities in these satellite cities. Otherwise, satellite cities would remain "bedroom communities".

To make these projects feasible, satellite cities need to foster better coordination in order to limit competition among them.



Map of Shanghai districts

Regarding the categories of residences offered by satellite cities, two trends are worth noting. Many land development programmes target the new upper middle class. Their projects consist of large villas, mostly located in gated communities. Their residents can enjoy a typical Western suburban way of life. Most of them use their cars to go working in the city centre. Satellite cities are planned to host the lower middle class that previously lived in the city centre but whose housing has been redeveloped by local authorities. For them, living in satellite cities was not their decision. They need more transport options to work within the city centre, and more businesses need to be created in satellite-cities, so that inhabitants do not need to commute.

The lowest class, rural migrants, are excluded from living in these new satellite cities since they do not have the necessary *hukou* to be able to buy apartments in these new towns. Because of this policy, satellite cities fail to host the poorest residents. Rural migrants are excluded because they usually lack a formal job and do not paid taxes or

social security in Shanghai. Even if they were allowed to buy property, they would be restricted in terms of financing for the same reason; they would not be able to get a bank loan, for example.

### ***Integrating “urban villages”***

In China, the concept of urban villages is not the same as in Western countries, where it refers to an urban planning project promoting pedestrian facilities and mixed use zoning. In China, urban villages (*chéng zhōngcūn*, 城中村: villages surrounded by city) are the unplanned result of an intensive urban sprawl. Chinese cities have been spreading into their rural surrounding for the last twenty years. Most of the farmland has been requisitioned by city governments; however in most cases, villagers have kept their housing lots. In the absence of farmland, villagers have become landlords: they use their original dwellings or construct buildings themselves on their housing lots catering to the large number of migrant workers arriving in the city, as well as to low income urban residents in search of affordable housing.

Contrary to satellite cities, residents of urban villages are mostly rural migrants who find cheap housing next to the centre. Because of urban sprawl, working activities for local villagers have changed. Without farmland, they can no longer work in the fields. By renting apartments or rooms to migrants on their housing lots, local villagers can expect a comfortable source of income, and thus gain a higher social status.

Living conditions are hazardous, and most of the constructions lack basic facilities. Interaction between migrant workers and original villagers is minimal, demonstrating the imperfections of the double citizenship system, where only some achieve first class citizenship, while others remain marginalized on the fringes of urban life.

City authorities are absent within China’s urban villages. While regulations are set by local villagers, city governments do not wish to be responsible for taking on the redevelopment, management and social welfare of urban villages, as this would require large investments. In the absence of city regulations, urban villages have kept their traditional forms of governance. Because they are located in urban villages, rural settlements remain collective and the community still plays an important role. Although urban villages are convenient for both villagers, who profit from the system’s imperfections, and city authorities, who do not need to provide social services, their existence reflects the inadequacy of the *hukou* and the double property system, and the need to champion social housing and the rental market in the city. Efforts should be pursued to better integrate urban village within cities.

### **3. Urbanisation and the environment**

Urbanisation is often regarded as harmful to the environment, because of issues related to water shortage and waste management. The recent low air quality level in Beijing illustrates the important challenge China needs to tackle regarding urbanisation. The causes of pollution are many: the continuing use of coal as a major source of energy, the increasing car traffic, the presence of factories near cities and insufficient pollution regulations and enforcement. Pollution affects inhabitants’ health, of course, but it also holds China’s large cities back from becoming global. Polluted cities will not attract the emerging knowledge workers class. These workers will prefer to move to smaller, cleaner cities to enjoy a better environment.

Although stricter environmental regulations may reduce economic growth in the short term and increase discontent among the new consumer classes, green policies would help China’s leading cities to develop their service sector and thus increase their competitiveness as global cities. However, it would be a mistake to link pollution to urbanisation. Some of our interviews rightly pointed out that urbanisation may also have a positive effect on the environment. Respondents argued that urbanisation might help the government to better manage farming lands, improve agricultural modernisation and reduce agricultural pollution.

Furthermore, in Western countries, urban citizens seem more responsive to environmental issues. A similar trend may be adopted in China. This is illustrated by the emergence of new pro-environmental grassroots organizations in Chinese cities.



## Conclusion

Since China's reform and opening up, rapid urbanisation has accompanied high economic growth. By 2011, the rate of China's urbanisation had exceeded 50% (0.67 billion) in 655 cities and 2,000 small towns. The hierarchy of cities and towns comprises large cities at the top, and middle-sized and smaller cities forming the backbone at intermediate and lower levels. Currently, Chinese urbanisation is at the middle stage of the traditional urbanisation model. Economic development is the central objective, driven by export-oriented industrialisation, with local government performing a key role. Land consumption for large scale and extensive urban expansion is the principal method of development helped by a significant amount of financial investment. This model is not sustainable in the long run. It is plagued by many problems, not least the fact that a significant proportion of the population remain disengaged from urbanisation. Although more than 50% of China's population now live in urban areas, just 35% of residents enjoy equal access to the full range of urban public services. Land has been overdeveloped; construction has progressed at four times the rate of population growth over the past 30 years. The cities at the top of the urban hierarchy have attracted the lion's share of high level administrative functions (both public and private sector) and jobs. Medium-sized cities have developed more slowly, while the role and function of small cities and towns is not well defined. The traditional model of urbanisation also causes other problems, such as concentration of infrastructure investment, unbalanced economic structure, environmental pollution, and aggravation of social divisions.

The 1994 tax reform has favoured land over-consumption, but also helped the construction of a unified market. Chinese cities and their expansion are still influenced by this reform. The problems linked with urban expansion and the development of super large cities will lead to more reforms and policies.

In the case of Shanghai, satellite cities have not solved the issue related to urban sprawl because of inter-district competition, and the "integration of urban villages" is still not accomplished. New policies need to be implemented to solve these issues in order to limit urban sprawl.

Environment protection in urban strategy making is an undeniably important issue, and needs to be addressed systematically. To solve the environmental issues, the service industry needs to be developed intensively within Chinese cities, but in order to make this policy work central-local fiscal relations need to be reformed first.

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