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The State, the Market, Economic Growth and Poverty in China

John Donaldson

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Socialism means eliminating poverty. Pauperism is not socialism.

Deng Xiaoping, Building Socialism with Chinese Characteristics

Introduction

The People's Republic of China is often cited as an unprecedented success story as far as rural poverty is concerned. Despite recent reports of sometimes violent protests in rural areas over illicit land seizures and pollution, since implementing reforms in 1978, China has seen rural poverty rates fall from xxx to yyy, as economic growth increased zzz on average each year, according to World Bank estimates. Some have ascribed liberal policy prescriptions based on open markets and pro-market government policies as are largely responsible, even as they forwent expensive, large-scale mass welfare programs. Starting with their initial round of fundamental reform of China's land policy, based since the mid-1960s on collective agriculture and an all-encompassing communal system, China's leadership enhanced the role of the market in order to spur agriculture production and growth in China's economy. They accomplished this through market reforms centered on a "Household Responsibility System," under which local governments reallocated land to China's peasant families through long-term leases, allowing them to sell agriculture production over set quotas on a free market based on gradually reformed prices. This reform, completed over the next few years, not only dramatically increased rural incomes, reducing poverty in many rural areas, but also helped to jump start China's economy by

providing additional incentives – in the form of more plentiful food – to urban workers. This, combined with subsequent primarily urban-based reforms, though gradual, spurred development that fueled China's impressive economic growth that produced history's most dramatic reduction of rural poverty.

While the record of poverty reduction is indeed impressive, two other elements of the above argument concerning the process through which poverty reduction occurred are more controversial. First, advocates of this argument emphasize the close and crucial role that economic growth played in reducing rural poverty. Economic growth provided new opportunities for farmers, stimulated markets for agriculture products, filled government coffers used to fund infrastructure and other projects, and sparked industrialization which provided new job opportunities for migrants. This is a commonly-held view. For instance, the World Bank, in a comprehensive survey of rural poverty in China during the 1980s and 90s, found that for each one point of GDP growth in China, rural poverty declined 0.8 percent. Scott Roselle and his colleagues similarly found a .98 correlation between economic growth and poverty reduction in the country. In emphasizing the importance of economic growth for poverty reduction, this research echoes a common theoretical hypothesis linking growth with poverty (e.g., Dollar and Kraay 2002). A conclusion limited to the linkage between economic growth and poverty reduction, however, would not be controversial, for most theories of development and poverty reduction – from Smith to Marx – emphasize growth and industrialization. However, observing this link leaves unexplored the mechanisms through which economic growth was achieved, as well as how it reduced poverty. On this question, many analysts posit a second argument, contending that market-oriented liberalization sparked both economic growth and, both directly indirectly (through economic growth), helped to reduce poverty. Though gradual, the reforms,

because market-based, allowed China's farmers the freedom needed to profit from individual initiative, motivating farmers to farm more actively, to make better decisions on planting and to seek to learn how to make farming more effective. Responding to higher market prices, and allowed for the first time in decades to keep the rewards for their own labor, most farmers increased their workload, reallocated labor within the household and made crucial investments in the land. A reduction in state interference provided freedom for peasants to choose among more alternatives, not only within farming itself, but outside agriculture.

Among those arguing for the linkage between a reduction in state 'interference' and subsequent economic growth and poverty reduction, sociologist Victor Nee is typical, writing,

The role of markets in China has steadily increased since 1978 and the agricultural sector has undergone the most dramatic shift in reliance on market coordination. In 1980, the state instituted the household responsibility system which is in many ways similar to private farming in a market economy, with the household leasing its land and paying delivery quota as rent... This change in ownership structure returned to peasants incentives in line with their traditional preferences for household production and eliminated the 'free rider dilemma' that had plagued collectivist agriculture. This shift resulted in dramatic increases in per capita income in the 1980s ... The correlation between increases in per capita income and the transition from redistributive/collective agriculture to household commodity production is striking. (Nee 1989, p. 664)

Many prominent China experts share Victor Nee's view, including political economist Dwight Perkins (1991) and political scientist Kate Zhou (1996). These arguments present China as a major – because it is a large and reforming communist state – example supporting the 'pro-market' side of the debate on whether state or market forces are superior for reducing poverty (e.g., Kohli 2002, Kanbur 2001).

This article tries to balance this view, arguing that the actual story is less straightforward. In this article, I first trace the explanatory power of economic growth, comparing it to patterns of poverty reduction. While economic growth certainly played no small role in many periods during the reform era (1978-present), during other periods, the linkage between economic growth and

poverty reduction appears to be less direct, as poverty rates responded to forces (often policy) other than economic growth. Second, I focus on the initial reform period to the mid-1980s, especially the Household Responsibility System to examine the assumption that it was primarily market-based. While the state did apply market forces to enhance incentives for China's farmers by providing tangible rewards for household effort, the role of the state in setting high quota prices, providing important agriculture inputs and improving infrastructure, also played a crucial role. The opportunities to access the market under the household responsibility system proved critical in helping farmers emerge from poverty by the mid-1980s. However, by that time, the pace of poverty reduction slowed, and in some areas reversed for a time, despite a continuously growing economy. Only when the state increased quota prices to encourage more grain growing did agricultural production rise again. In the third section, I outline the programs and policies that have made a difference in reducing rural poverty in China, including examples of central, provincial and local initiatives that were indispensable to that effort. As early as 1986, the state, hoping to maintain the pace of poverty reduction, asserted itself more fully in the poverty reduction effort, not only in building roads and bridges, establishing and regulating markets in towns and villages, and promoting opportunities for rural non-skilled and semi-skilled workers in manufacturing, mining and services, but also through larger projects and proactive central and local initiatives for rural development. In sum, in contrast to a view of economic growth and market forces as the major impetus behind the impressive rate of poverty reduction in China and the view of the state as an often predatory actor impeding poverty reduction, the role of the state in poverty reduction was of critical importance, even as the role of economic growth – though important – is more circumscribed.

Section 1: Trends in Poverty Reduction in China

Poverty declined radically in China since Deng Xiaoping took the helm in 1978 (Figure 1).

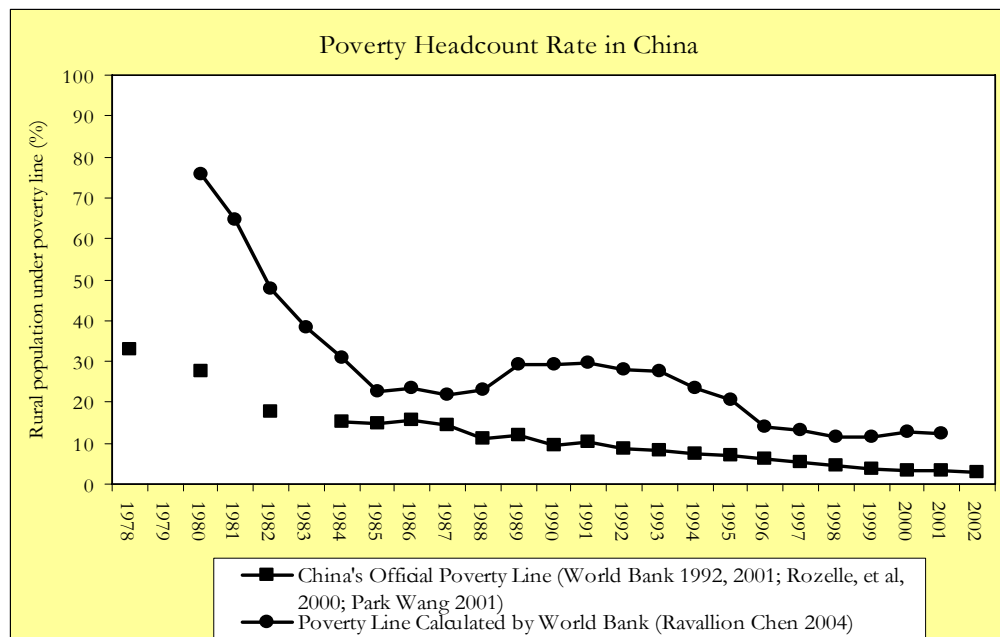


Figure 1: Poverty headcount rate in China. Sources: World Bank 1992, 2001, Rozelle 2001, Park Wang 2001, Ravallion Chen 2004

Various scholars have attempted to measure China's poverty by applying a variety of poverty standards, including the international poverty line of US\$1/person/day, China's poverty line, or some other cut-off line. Despite the differing results, each of these studies concludes that, overall, China's poverty rate has declined rapidly since 1978. A cursory comparison of China's declining poverty rates with the country's rising gross domestic product (GDP) per capita (Figure 2)

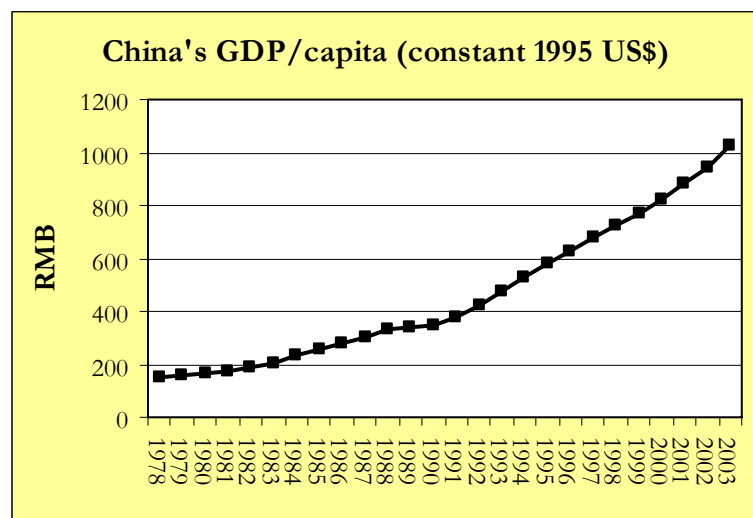


Figure 2: China's GDP/capita. Source: World Development Indicators

suggests that China's poverty is closely and inversely linked with China's growth. However, careful scrutiny of the data reveals two trends that cast doubt on the direct link between growth and poverty.

First, examining poverty rates reveals not uniform decline, but several time periods with

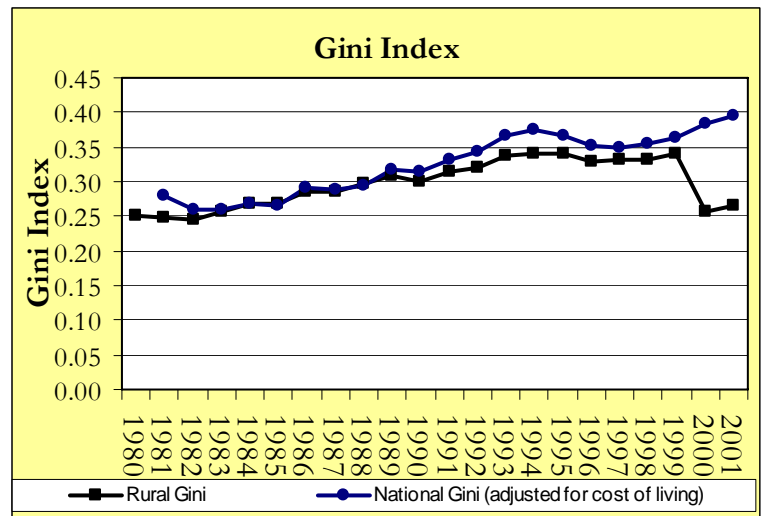


Figure 3: China's rural and national Gini index. Source: Ravallion and Chen 2005

contrasting trends. Based on nearly any measure, China's headcount poverty rate declined most rapidly from 1978 to 1984, from 260 million to 128 million people according to China's official statistics, before flattening out between 1984 and 1989, when the official statistics place the poverty headcount rate at 106 million. In the 1990s, poverty rates declined steadily once again, especially after 1993.¹ Thus, though China's poverty rate declined between 1978 and the present, it did so more rapidly in some periods and less rapidly in others. Second, economic growth benefited some socioeconomic groupings more than it did others, as evidenced by China's precipitously expanding rich-poor gap (Figure 3), although again, in different patterns during different periods. This is true not only in China as a whole, but also in China's rural areas.

Starting from a low level in 1980 of .25, the Gini index (a commonly-used measure of

¹ After comparing several Western and Chinese measures of China's poverty rate over time, two economists conclude, "All estimates agree that there was a spectacular reduction in poverty in the early 1980s. All estimates other than the official poverty count show little or no progress in poverty reduction in the late 1980s. Reductions in the official count are almost certainly due to insufficient inflation of the poverty line in 1988 and 1989. In the early 1990s, Khan and the World Bank show little decline until after 1993. The official poverty count falls steadily throughout the 1990s," (Park and Wang 2001).

inequality) for China's rural areas declined slightly to .24 in 1982, but then increased steadily to reach .34 in 1993, when it apparently leveled off, a pattern similar for China's overall Gini index (Ravallion and Chen 2004, p. 39).

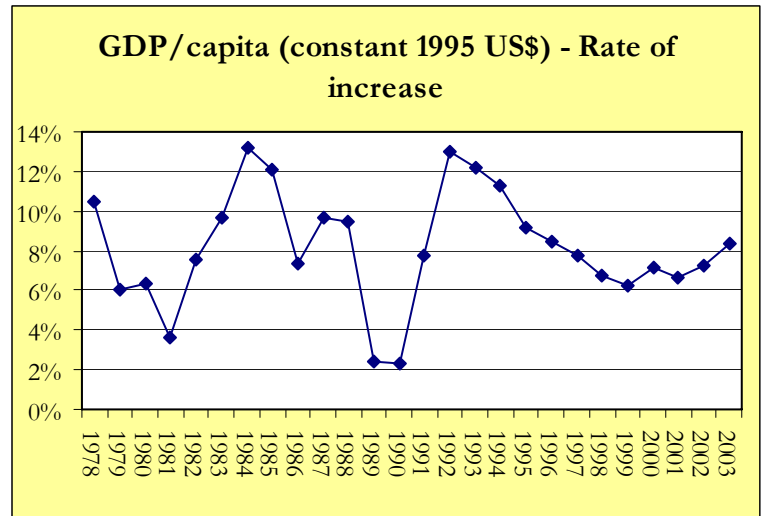


Figure 4: GDP/capita rate of increase. Source: Author's calculations

Looking more carefully at

economic growth and poverty reduction underscores were not linked in many periods.

Comparing all four indicators in Figures 1 through 4 (poverty rates, GDP, the rich-poor gap and growth rates in GDP/Capita), whereas poverty reduction slowed and the rich-poor gap increased starting in 1984, the rate of GDP growth that had begun in 1978 accelerated in 1982, reaching its height in 1984 and 1985, when GDP per capita grew 13.2 and 12.1 percent, respectively. The economic growth experienced during this period (1983-1985) primarily benefited wealthier people, as the slowing rate of poverty reduction and increasing rich-poor gap indicate. Moreover, as poverty began to decline again in the early 1990s (especially 1993), the rate of increase for per capita GDP had already slowed. Thus while it is true that growth consistently expanded and poverty consistently declined during most periods between 1978 and the present, neither are the two factors as systematically related as some argue, but also economic growth does not appear to

have helped the poor of China as much as it did everyone else.² Other factors, in addition to growth, must have been at work.

Section 2: The State and the Household Responsibility System

One time period in which the growth and poverty rates do vary together is 1978-1984. During the entire nearly thirty-year-long reform period, the breakup of the communes and the decollectivization of farms was the one change in government policy with the most extensive impact on the lives and livelihoods of farmers, both poor and non-poor. Between 1979 and 1984, the Chinese government, which was under some political pressure from farmers and local governments, gradually but steadily broke up the old communal system that has been in place since the 1950s, divided the land relatively equitably among rural residents, and signed long-term leases with them.³ For the first time in decades, the government devolved planting and other major decisions to the most local of units, the household (Chung 2000, Zweig 1997). However, although market forces and market-set prices increase in importance, even as the role of the state in making micro-level planting and distribution decisions waned, the role of the state was far greater than that prescribed by liberal economists. Under this system, the government assigned each family responsibility for producing government-established quotas, which the state then

² Throughout the 1990s, the rich and poor gained from growth at different rates. As one World Bank report concludes, the income of China's richest one percent grew four times as fast as everyone else's; the income of the richest 20 percent increased by 6.9 percent per year, while the income of the bottom half grew at 4.9 percent each year (Chen and Wang 2001).

³ Studies independently undertaken by Unger (2002a) and Cheng (1998) confirm that plot size or quality distributed to local officials did not significantly differ from the average, indicating a relatively equitable distribution process. However, Cheng finds that officials command greater access to agricultural inputs, such as seeds and fertilizers, which affects their income.

purchased at set prices that increased steadily over the first few years.⁴ The government also allowed any production above the quotas to be sold on the newly reopened private markets.

The change was extraordinary. In 1978, nearly all planting decisions were made by commune authorities. By 1984, 96 percent of all farms were held by private producers. The number of agricultural products subject to government procurement declined from 113 in 1978 to 38 by 1984, although procurement of major products such as grain continued (Fan, et al. 2002, p. 53). With the combination of newly endowed rights to land, individual incentives linking work to reward, increases in government procurement prices and good weather, agricultural production rose 6.6 percent on average each year between 1978 and 1984 (Yao 1999). Farmers, no longer obligated to produce grain first, reverted to producing traditional and more profitable crops, such as cotton in Shandong. While some bemoaned the reduction in scale of Chinese farms (e.g., Hinton 1991), the stimulus to the agricultural sector was such that it grew faster than the industrial sector and narrowed for a time the urban-rural rich-poor gap (Whyte 1986, pp. 113-4), reducing poverty quickly in many areas of the country. By the mid-1980s, the government was faced with unmanageably ballooning costs. As a result, the central government slashed agricultural procurement prices paid for grain and other agricultural goods over the years of the mid-1980s and early 1990s, while simultaneously phasing out grain subsidies in urban areas, primary factors behind the decline in grain production from 1984 until the early 1990s. These declines sparked the government to reverse course and increase procurement prices several times: by 40 percent in 1994 (when procurement prices exceeded international prices) and 42 percent in 1995 (Fan, et al. 2002)(Findlay 1997).

⁴ In 1979 alone, procurement prices for above-quota sales on 18 agricultural products increased 50 percent.

Therefore, though the agricultural reforms were based on increasing the range of market choices for peasants, enhancing the efficient selection of agriculture production and allocation of key inputs, the government role was also significant, a critical determinant of the subsequent levels of grain production. Most advocates of pro-market reforms willingly concede the importance of government involvement in establishing institutions and enforcing laws. In this case, the implementation of the household responsibility system for agriculture in China placed heavy demand on local governments for reasonably fair reallocation of collectively owned land to households, including the resolution of disputes. Central governments had extensive work in ensuring compliance with the policy and ensuring its systematic implementation in all parts of the country. However, the importance of the state went far beyond the implementation and enforcement of a fundamentally pro-market policy. Indeed, grain production during this time period closely followed the levels of pricing the government established for quotas of agriculture produce, with higher prices producing higher grain yields. When the government's procurement price increased, as during the 1978-1984 period, the lot of farmers improved, but when procurement prices were cut, poverty reduction stagnated or even reversed itself. While Perkins (1991) and Lardy (1983) specifically deny a place for procurement prices in explaining rising farm incomes, research by Claude Aubert (1990), Albert Park and his co-authors (1994) and (even while recommending scrapping agricultural quotas) Terry Sicular (1995), each find the state's quotas and procurement system during the 1978-1984 period to be progressive on incomes.⁵ Moreover, the costs of this program were significant, and could rival many costly

⁵ Perkins, in writing about China's rural economy of the early 1980s, discusses the role of state subsidies for grain prices. However, he argues that the market was the primary driver behind rural growth, but notes directly afterwards the problem of massive state deficits that accumulated as prices paid by the state to farmers exceeded those paid to the state by urban residents. He

direct benefits programs. Thus, the role of the state – a far more proactive state than most pro-market theorists would advocate – was important to understanding the extent of poverty reduction in China.

Section 3: Government Responses after Reform (1978-2005)

Finally, in addition to the effect of growth on poverty, we should also consider government policy changes implemented during different time periods. To underscore the primary role played by the state in reducing poverty, this necessarily brief survey mainly highlights some of the key poverty-reduction policies implemented during the post-1976 reform era. When Perkins (1991), among others, asserts that no formal rural anti-poverty programs were established before the mid-1980s, he is no doubt referring accurately to the relative absence of direct development programs in poor areas. This gives the incorrect impression that rural reform was the sole driver of poverty reduction during this period. As the government implemented the Household Responsibility System, China's anti-poverty policies were not nearly as extensive as those adopted later. Nevertheless, the government responded directly to rural poverty during these years in a number of ways, both old and new. Since the mid-1950s the government had been implementing rural relief programs to guarantee subsistence in-kind income to destitute residents, even though responsibility for that task was borne, in order, by the family, the workplace and the state. For households with the "three lacks" (those families that lack financial support, a source of livelihood and labor power), China's central government had by the 1956 adopted Model Regulations for Advanced Agriculture Producers' Cooperatives, a program of

apparently does not give any credit for rural poverty reduction to an expensive, government-managed system that created incentives for farmers to grow and sell grain and for urban residents to purchase more grain surpluses than they otherwise could afford (Perkins 2001, pp. 526-7).

“five guarantees” of vital goods and services: food, clothing, burial expenses, children’s education and medical care (Dixon 1981). In practice, only the childless elderly (83 percent of recipients), orphans and the disabled received these funds, which were usually quite modest, as many poor areas were able to provide the needy little more than grain rations (World Bank 1992).⁶ Moreover, the precondition that the state seizure recipient assets provided strong disincentives for cheating (Hussain 1990). Nevertheless, for decade, this program this represented the primary direct anti-poverty program that specifically targeted the non-working poor. In addition to this program, the Ministry of Civil Affairs (MCA) also managed programs in disaster relief by providing clothing and grain to areas affected by earthquake, floods and drought, with the objective of ensuring survival and not necessarily of compensating damages (World Bank 1992, p. 109).

In addition to these programs, central government ministries implemented programs specifically targeted to poor areas. The government made nine years of formal education compulsory in 1978, an unrealistic ideal that has yet to be made universal throughout China even today (Unger 2002a).⁷ Nevertheless, according to official statistics, illiteracy rates declined from 48 percent in the 1970s to less than 10 percent by 1997 (Fan, et al. 2002, pp. 22-3). The Ministry of Public Health also implemented programs that focused on improving education and healthcare in poor areas, although some argue that these programs only partially compensated for the end of the “barefoot doctor” system that provided healthcare to rural areas before 1978 (Piazza and

⁶ The program’s reach is modest. One 1957 survey found only 12 people in one Shanghai commune of 3,432, were receiving “five guarantees” support. Overall, throughout China, less than one percent of rural residents were receiving such benefits (Dixon 1981, p. 193). Hussain (1990), while critical of the system, notes that three percent of rural residents over 65 receive *wubao* aid, which he calls “exceptional” for a developing country.

⁷ For instance, a campaign to wipe out illiteracy and provide nine years of education was being implemented in remote rural areas in Guizhou and Yunnan in 2004.

Liang 1998)(Hussain 1990). Moreover, the government focused on electrifying the countryside, which increased most rapidly during this period, as well as subsidizing grain to support poor rural areas (Fan, et al. 2002)(Park and Rozelle 1994). Finally, in 1982 the State Council implemented the Sanxi Agricultural Construction Fund provided development aid grants to 47 counties in Gansu and Ningxia as part of a special Ministry of Finance (MOF)-administered Development Fund for Underdeveloped Areas (Kuchler 1990).

By the mid-1980s, China's central government, seeking to deepen its focus on poverty reduction, established an extensive array of formal anti-poverty initiatives for poor rural areas. This effort required an extensive network of new institutions. In May 1986, the State Council established the Leading Group for Economic Development in Poor Areas (LGPAD)⁸ to oversee and coordinate anti-poverty programs, in part through its executive agency, the Poor Area Development Office (PADO), with branches in provinces, prefectures, and counties throughout China. In addition, many township-level governments also assigned a point person to work with county-led PADOs on poverty reduction (World Bank 2001). That year, the central government also designated 331 counties (about 12 percent of the country's total) as poor based on a poverty line of RMB 150 (for most counties), RMB 200 (for selected minority or old revolutionary base areas), or RMB 300 (for special cases, including pastoral and semi-pastoral counties).⁹ Supplementing this monetary income standard, the central government also considered those counties with per capita grain production under 200 kg per capita as poor counties (World Bank 1992, p. 117). For designated poor counties, the central government earmarked special funds. Provincial governments supplemented this central list with an additional 368 counties based on

⁸ In 1993, the name of this organization changed to the "Development-Oriented Poverty Alleviation Leading Group" (State Council LGPAD 2003).

⁹ For much of the 1990s, RMB was trading at approximately 8.2 to the US dollar.

their own poverty lines (Fan, et al. 2002). Therefore, between the national and provincial lists, counties designated as poor approached 700, about a quarter of China's counties, each of which received central and local support through three key programs, described below.

How well did this list actually cover the poor? Most counties included in the initial list were indeed poor, living in areas with severe geographic and environmental problems, below average levels of irrigation, fertilizer use and poor infrastructure. However, for political reasons, counties designated poor on the national level were spread throughout the country, a decision that benefited many relatively well-off provinces, while forcing some poorer provinces to add to their provincial lists some counties that under objective standards should have qualified for inclusion on the national list (Piazza and Liang 1998, p. 264). This problem was partially addressed when government officials adjusted county lists in 1993 and 2001. Nevertheless, experts estimate that a minority of the people within poor counties were poor (i.e., below China's poverty line), and more than half of China's poor people lived outside these designated poor areas, scattered among China's other counties (Park, et al. 2002, Riskin and Li 2001). For these reasons, World Bank researchers suggest that China shift its focus to townships, one administrative level below the counties (World Bank 2001). Many provinces during this period, in search of quick successes, directed funding to the wealthier of the poor counties (Park, et al. 2002, p. 134), thereby mitigating the overall impact on poverty.

In spite of these challenges related to targeting and leakage of funds, this program did apparently benefit targeted poor counties. One study concluded that economic growth in designated counties exceeded growth in non-designated poor counties by 2.3 percent in 1985-1992 and by 0.9 percent in 1992-1995 (Park, et al. 2002). Another found a 1.1 percentage point increase per year in consumption between 1985 and 1990, and a marginal return on investment

of 12 percent for money spent on projects in these areas (Jalan and Ravallion 1998), while a subsequent study found a 12.5 percent return for 1985-1992 compared to 11.6 percent for 1992-1995 (Park, et al. 2002).

To support poor counties, the central government implemented three core poverty-alleviation programs, which included subsidized loans through the Agricultural Bank of China, the Food-for-Work program (*Yigong-Daizhen*) through the State Development Planning Commission, and development grants through the Ministry of Finance (World Bank 2001). These programs were funded

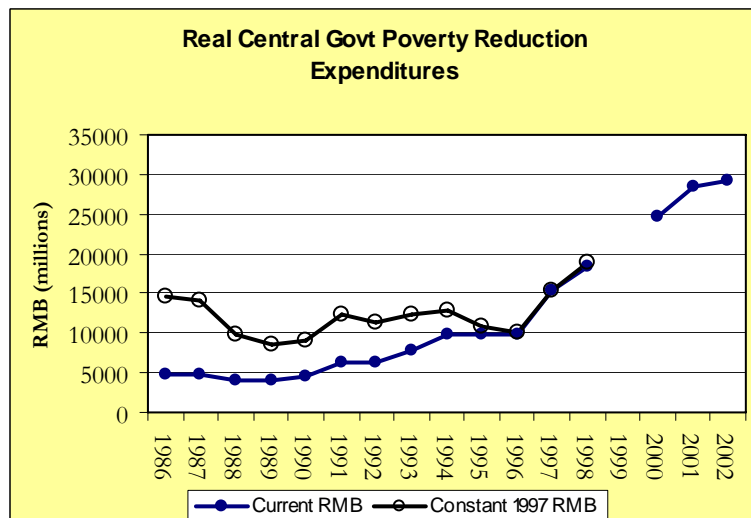


Figure 5: Real central government poverty reduction expenditures. Source: World Bank 2001, LGPAD 2003

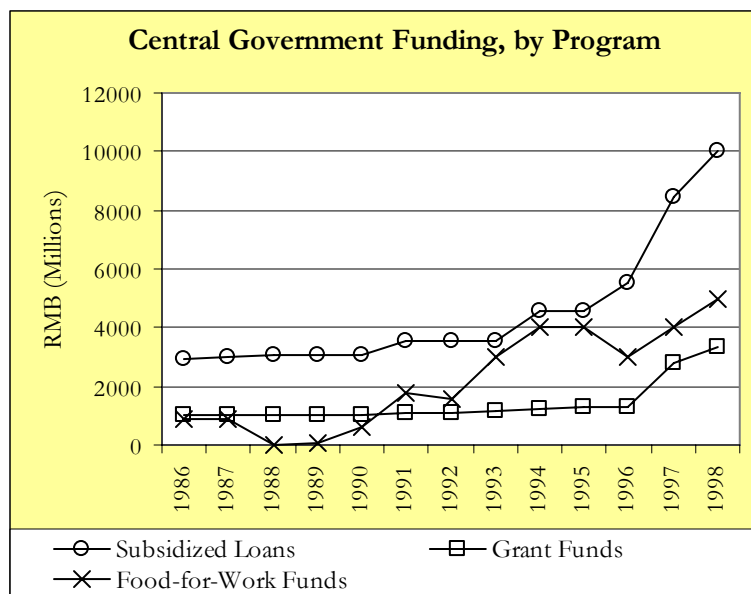


Figure 6: Central government funding by major anti-poverty program. Source: World Bank 2001, p. 43

centrally, with matching funds expected from provincial and local governments. In real terms, overall funding levels fell over time, and did not achieve their previous levels until 1996 (Figure 5).¹⁰ Moreover, the funding levels of these three programs varied a great deal (see Figure 6).

- Subsidized loans

Viewed as the flagship of China's poverty reduction efforts, China's subsidized loan program was intended to provide inexpensive loans to poor families with which they can invest in productive agricultural assets. While program did benefit many Chinese families, it is difficult to find an expert with an overall positive evaluation of the program (World Bank 2001). Originally oriented toward direct lending for household agricultural production, in 1989 governments at all levels refocused the program on promoting TVEs, before reverting in 1996 to its original focus on households (Rozelle, et al. 2000, p. 10). Surveys do suggest that most loans were directed to poor rural households. However, while the program was intended to target agricultural production of poor rural households, many loans either subsidized primarily direct, unsustainable household consumption or were diverted to middle-income farmers, dampening their long-term effect on poverty (Park, et al. 2002). Moreover, some local governments, which consider most poor people risky, because they are incapable of managing agriculture projects successfully, channeled loans away from them to wealthier people or to businesses. In the late 1990s, poverty-alleviation loans were systematically diverted to capital-intensive enterprises of the kind that hired few poor people (World Bank 2001, pp. 47-8). Though losses to this program are difficult to calculate, researchers estimate that total losses from this program are substantial

¹⁰ The data for this chart has two sources, one (World Bank 2001) for the years 1986 to 1998, and the other (State Council LGPAD 2003) for 2000 to 2002, leaving a gap.

(Rozelle, et al. 2000, pp. 7-8). Still, these have to be weighed against the significant number of families that program has been able to pull out of poverty.

- Food-for-work

Much clearly successful is the Food-for-Work program, implemented by the State Planning Commission, which was designed to provide rural employment to poor people, hiring them to work on labor-intensive projects to promote drinking water, land improvements and local road construction. By the early 1990s, the government diversified the program to include water conservation, education and health. A World Bank (2001) study concluded that, although many poor villages could not participate in Food-for-Work opportunities, the program did predominantly reach poor rural residents in those areas in which it was implemented in part because remunerations were modest enough to support self-selection. The Food-for-Work program is also praised for successfully constructing rural infrastructure, including 131,000 km of rural roads and 7,900 bridges, and for providing 20 million people with drinking water between 1985 and 1991 (Zhu and Jiang 1996). Thus, the effect of the food-for-work program on poverty is two-fold: it provided needed support for the working poor and, through the completed projects, provided vital services for poor areas.

Despite this success, China's Food-for-Work program faced several problems. Most provinces and counties provided insufficient matching funds, often far less than the program required. As a result, program officials were sometimes forced to purchase inputs with central funds, reducing the amount of funds available to compensate rural labor. Thus, estimated 40 percent of the participating labor force was obtained for free or on a non-cash basis, as local governments in rural areas maintained the "work day contribution system," a throwback to the communal era in which each household was given quotas for labor contributions (World Bank

2001, p. 50). In addition, the program was implemented in a top-down fashion, and community needs were sometimes not addressed (for instance, work focused on terracing instead of an alternative, expressed community need such as road construction), and some projects (such as the construction of rural post offices) had little direct effect on poverty (Zhu and Jiang 1996). Finally, the expansion of the program in the mid-1990s made the program more difficult to administer and monitor (World Bank 2001, p. 51). Nevertheless, even when rural labor was unpaid, many poor rural communities benefited significantly from drinking water and rural infrastructure created through this program, and rural families obtained transferable skills.

- Development grants

The development grant program, administered by the Ministry of Finance, is the most poorly studied of the three programs, although one report noted that development grants are “highly progressive” and have effectively reduced poverty (Park, et al. 2002, p. 139). Nevertheless, the value of grant funding has declined in real terms from the late 1980s and did not again reach its 1986 value until 1998 (World Bank 2001, p. 51).

By 1993, the central government, facing widening gaps between rich and poor, redoubled its efforts, designing the “Seven-Year Priority Poverty Alleviation Program” designed to eliminate poverty among China’s remaining 80 million poor people (calculated based on China’s poverty line) over the subsequent seven years (i.e., by 2000). The plan, nicknamed “8-7” (*ba-qi*), focused on several priorities, including land improvement, strengthening poverty-related institutions, establishment of establishing a new monitoring system, improving access to migration opportunities, continuing investments in agriculture, TVEs and infrastructure (including roads, drinking water and electricity), and increasing investments in human capital, education and disaster relief (Piazza and Liang 1998, pp. 262-3, World Bank 2001, p. 41). The plan focused

specifically on the problems facing the agriculture sector in mountainous regions by providing land development, small-scale water conservation projects, and improved techniques in food production, animal husbandry, forestry as well as raising cash crops (World Bank 2001 p. xxv). Poor provinces adopted similar plans for this period.

The 8-7 Plan (the first sentence of which, “Socialism will abolish poverty,” echoes Deng Xiaoping’s quote that begins this paper) supported its ambitious list of priorities with additional funding. It was not until the 1996 National Poverty Reduction Conference that that State Council significantly increased funding under the 8-7 Plan in an effort to achieve poverty reduction targets before the 2000 deadline (World Bank 2001, pp. 41-2). The plan also linked government and party organizations with poor areas, charging most such organs with supporting a specific poor area by, for example, posting cadres temporarily to the areas to act as advisors and raising money from government employees for support and development of those areas. Similarly, wealthier provinces and cities were and charged them with supporting an assigned poor province, helping to with funds, personnel training, and other forms of assistance. According to government statistics, by 2000, the 8-7 Plan involved 138 government units, which posted more than 3,000 officials to poor areas and were responsible for some RMB 14.9 billion in funding (State Council 2003). The province-to-province linkages also provided financial support, estimated at RMB 2.14 billion in in-kind and direct financial support, as well as RMB 28 billion in investment.

In May 2001, after the deadline for the 8-7 Plan had passed, China’s government convened a working conference to evaluate program success and develop the next stage in China’s poverty reduction efforts, from which emerged the “Outline of China’s Development-oriented Poverty Alleviation in Rural Areas (2001-2010).” By the end of 2001, the conference had concluded that

the total number of people living under China's poverty line – which is far lower than international standards – totaled 30 million, or less than three percent of the population. These people were characterized as living in inhospitable geographic areas dispersed primarily throughout the western provinces, where 61 percent of the poor people remained. The program also classified a further 60 million people as “low-income” (under RMB 865 per capita). Three main foci for the poverty alleviation effort included ensuring that the remaining poor have sufficient food and clothing, improving further the living conditions of poor people who have recently emerged from poverty and intensifying infrastructure construction.

Development of Western China

Despite the impressive pace of poverty reduction, China's economic growth during the reform period benefited primarily the wealthier and better positioned coastal areas first. This result was not unexpected by China's central leaders: when Deng Xiaoping discussed the reform era that he had started decades earlier, he noted that some areas will “get rich first,” but that by the turn of the century, the central government would have to ensure that other areas catch up. To respond the widening gaps in regional development, China's central government shifted its focus away from wealthier coastal provinces, which had received special policies to attract foreign investment, toward China's western interior, inaugurating in late 1999 and early 2000 the central government plan to “Open Up the West.” Although this wide ranging plan involves six goals (ensuring equity, attracting foreign investment, constructing infrastructure, promoting sustainable development and staving off nationalist sentiments among China's ethnic minorities), the plan is vague and its progress has been mixed. Moreover, the amount of financing for most items, save infrastructure development, that is forthcoming from the central government is relatively modest. According to scholars, the bulk of support was intended to be sourced from

private and foreign investment, which has so far been limited (Goodman 2004, Holbig 2004). The government for its part claims it has invested US\$ 72.6 billion in dozens of reforestation, infrastructure development and other projects between 2000 to April 2003, with US\$16 billion invested in 14 new “key projects” in 2003 alone (Ash 2004, pp. 869-70).¹¹ Despite some obvious accomplishments, judging the overall effect of this policy – which has been extended in modified form to the industrial rust-belt in Northeastern China – is premature (citation).

Other government poverty reduction initiatives including training and placement of migrant workers, supporting rural-based town-and-village enterprises, massive infrastructure construction project and so forth. In addition to these centrally-administered projects, China’s provincial and local governments have also been active in poverty reduction. Starting in 1984, governments at all levels shifted from cautious regulation to active encouragement of TVEs (Fan, et al. 2002). Local leaders in China’s coastal and inland provinces, responding to new incentives from a reformed economic system, established town-and-village enterprises, local industries. The number of TVEs exploded during this period, increasing from 1.4 million firms in 1980 to six million firms in 1984 to 12.2 million firms in 1985. Employment in TVEs also rose sharply and the number of small family firms, which are best suited to small niche markets in local areas, also increased. The role of the local official in these industries was central, with many local leaders acting as high-level managers and CEOs of these industries, using their political power to obtain key inputs and to protect the nascent industries (Oi 1995). This provided many farmers employment opportunities outside the farm providing an essential source of cash income.

¹¹ With rising urban poverty, the program has also been applied to the three northeastern provinces in China. With economies based on inefficient heavy industry, industrial restructuring have cost many workers in this region their jobs.

Although this was important in reducing poverty with sufficiently favorable conditions for developing industries, many areas did not receive much benefit from such enterprises (Byrd and Gelb 1990, World Bank 1992, p. 65). For instance, by 1990, TVEs in 120 of China's poorest counties employed only four percent of local rural labor (Piazza and Liang 1998, pp. 257-8).

In addition to establishing these industries, many local governments also implemented more traditional anti-poverty programs. Long before provincial governors were help personally responsible for reducing poverty in their constituencies in 1996, every province implemented strategies for reducing rural poverty. These have taken a variety of forms, including development-based initiatives (such as spurring rural tourism or building roadway), or more direct anti-poverty programs, such as microcredit programs. Moreover, many local governments have taken innovative steps toward poverty reduction, by taking advantage of local attributes. In one dry county of the northwestern province of Gansu province, the government encouraged farmers to pave their backyards with cement inlaid with a receptacle that would catch rainwater that ran off the farmers' slanted roofs. This helped farmers address one of their most urgent problems – access to sufficient water. The ground of one township in the remote, mountainous southwestern province of Guizhou, for instance, is so rocky that most agricultural production is not viable. Instead of more traditional anti-poverty programs, encouraged farmers to abandon efforts to plant grain, and instead plant grass that can grow between the rocks in the soil. A micro-credit program was then instituted under which farmers could buy and raise cattle, which fed off the grasses, and complemented this strategy by building a market where cattle could be bought and sold. Even as the news is dominated by reports of local abuses from local government officials, there are many less-well-known stories of these sorts of programs, –

implemented by a pro-active and sometimes quite innovative government, that have proven effective in reducing poverty.

Naturally, the state often adopts policies that have been detrimental to poverty reduction. China's household registration (*hukou*) system ties peasants administratively to their home areas, restricting their freedom of movement. Although this system has relaxed somewhat in recent years, with rural migrants able to obtain work permits and even local experiments allowing more rural migrants to obtain urban *hukou*, this population control policy has impeded the ability of some rural residents from benefiting from growth in the coastal areas through voluntary migration. Moreover, the tax burden on the peasant remains quite high, with some of the highest tax rates throughout the 1990s paid by residents of some of the poorest provinces. Moreover, few programs of poverty alleviation have been unqualified successes, as reports of systematic diversion of funds for various purposes, ranging from the legitimate to the illegitimate, are not uncommon. Nevertheless, the overall role of the government in ensuring poverty reduction has been a positive one, with central and local authorities playing a role in reducing rural poverty, both in areas where economic growth is rapid, as well as in areas far removed from coastal areas that has powered China's impressive industrialization.

Section 4: Conclusions

In the reform era, pro-market theorists find much support for their prescriptions for development and poverty reduction. Many such theorists argue that the withdrawal of the state allowed Chinese farmers to produce crops primarily for their own benefit, making planning decisions based not on the mandates of state bureaucrats and party cadres, but on what would maximize profits for the farmer and his or her household. China's GNP per capita between 1978

and 1985 increased more than 70 percent, rural incomes increased, poverty declined, and in defiance of Kuznet's inverted "U," China's growth, far from stratifying China, narrowed inequality between rich and poor, urban and rural, at least until the mid-1980s (Whyte 1986).

However, a closer look provides more support for the idea that the role of the state – rather than lessening – has instead shifted to other vital roles. First, despite the indispensable role that economic growth has played in reducing rural poverty in China, the linkage between such growth and poverty reduction is not direct during all periods. Economic growth had to be complemented with factors other than growth that reduced poverty. Second, we know from the lessons of the state-market debate that simple sentiment in favor of the market misses the critical role of the state. In China's case, "Marketizing the countryside" did not merely involve the total withdrawal of the state, but the active contribution of the government at all levels even to set up the Household Responsibility System (Chung 2000, Unger 2002a, Zweig 1997). The Household Responsibility System, although not formally transferring property rights to the formerly collectivized peasantry, nonetheless amounts to comprehensive reform of land ownership since it granted the ability of rural households to control their own small plots of land. Whereas other reforming states have privatized their land by selling it land to the highest bidder or merely handing it off to the wealthy, a strong state was required for China to ensure that land was allocated relatively equitably, not based on price or wealth, but on citizenship. Finally, the government has implemented numerous anti-poverty programs through an extensive administrative network that reaches down to the local areas. True, the main role has shifted from one of making most marketing decisions to one that more complementary to market forces. Nevertheless, this is a proactive and powerful role nonetheless. As David Goodman argues,

While two decades of economic reform had certainly seen an emphasis on the importance of market forces, this had not been an exclusive demand of the central

leadership ... As with the introduction of economic liberalism in Britain during the 19th century, a balance has been established between state and market with specific roles ascribed to each, rather than the replacement of all state economic activity by the market. (Goodman 2004, p. 319)

Growth in GDP, though not determinative, remained important to reducing poverty. Market forces also played a crucial role. Despite their central importance, the most important factor for China was the relationship between the state and the market. China's government supported, shaped and influenced market forces as its primary – and overall successful – approach to poverty reduction.