

Poverty

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1. China's record on poverty

Since the start of economic reforms, China has successfully lifted hundreds of millions of its citizens out of poverty, an achievement of historical and global importance. Using the World Bank's preferred \$1.25/day consumption poverty line, as seen in Figure 1 China reduced poverty from 835.1 million (84.0%) to 173.0 million (13.1%) from 1981 to 2008 (World Bank, 2012). During this same period of time, poverty in the rest of the world actually increased by 13.2 million even as the poverty rate fell from 40.5% to 25.2% as the population increased. Without China, the world fell well short of the pace required to meet the Millennium Development goal to halve the 1990 poverty rate by 2015. With China, the world is on track to meet this objective (Chen and Ravallion, 2010).

The dramatic reduction of poverty in China is robust to using different poverty lines and poverty measures (World Bank, 2009; Chen and Ravallion, 2010). The Chinese government uses a poverty criteria that incorporates both consumption and income data. For many years, China adopted a poverty line well below the World Bank's \$1.25/day line (World Bank, 2001 and 2009). Using this austere poverty line, China's official poverty count still fell dramatically from 250 million in 1978 to 14.8 million in 2007 (Figure 2). In 2000, the government established a higher "low income" line very near to \$1/day in order to identify additional near-poor populations to be targeted by policy; in that year 94.2 million people fell below the low income line compared to 32.1 million people who were below the official poverty line. In 2008 the low income line was adopted as the official poverty line. In 2011, the Chinese government nearly doubled the poverty line again to reach \$1.8/day, which raised China's official poverty headcount to 122.4 million in 2011 from 26.9 million in 2010 (Figure 2). Thus, China has raised its poverty threshold twice to reflect rising incomes and aspirations.

2. Sources of poverty reduction

What factors contributed to China's remarkable record of poverty reduction? Although the Chinese government has invested significant resources in combatting poverty through a variety of targeted programs, rapid economic growth and reforms that produced broad-based increases in

rural incomes can explain most of China's reduction in poverty. Growth would have had an even greater anti-poverty impact if inequality had not increased so substantially (Ravallion, 2010).

China's flagship anti-poverty program is a regionally targeted public investment program initiated in 1986 under the direction of national, provincial, and county Leading Group Offices for Poverty Alleviation and Development (LGOPAD). The goal of the program has been to increase the income-generating potential of households living in poor regions. Initially, the government targeted 328 nationally designated poor counties, which increased to 592 poor counties by 1993, accounting for 23.5% of China's rural population (LGOPAD, 2003; Park et al, 2002). The 592 poor county designations were revised in 2001 and 2011. Starting in 2001, partly in response to criticism that nearly half of the poor did not live in official poor counties (World Bank, 2001; Park et al, 2002), China shifted from county-level to village level targeting, focusing targeted public investments in 148,131 officially designated poor villages covering about 15 percent of China's rural population (Park and Wang, 2010). Unfortunately, the shift to lower-level targeting actually worsened targeting accuracy due to political, institutional, and informational factors (Park and Wang, 2012). According to China's poverty reduction plan for 2011-2020, China will concentrate public investments in 14 key poor areas located in remote, mountainous areas (State Council News Office, 2011).

The main targeted investment programs have been budgetary grants administered by the Ministry of Finance, a public works program administered by the State Planning Commission and Development and Reform Commission, and a subsidized loan program administered by the Agricultural Bank and Agricultural Development Bank. Funding amounts have increased over time, reaching 5% of the national budget (including loan principal) during 2001-2007 (World Bank, 2009). Rigorous evaluations find that the programs have had a positive impact on consumption and incomes. Analysis of household panel data from 4 southern provinces in the late 1980s finds that living in a poor county increased growth of consumption per capita by 1.1% per year with a rate of return of 12% (Jalan and Ravallion, 1998). A study using panel data for all counties in China estimates that poor county designation increased rural income per capita by 2.3% per year during 1985-92 and

0.9% during 1992-95 with rates of return of 15.5% and 11.6%, respectively (Park et al, 2002). An evaluation of poor village targeting using nationally representative rural household panel data finds no statistically significant average impacts on income or consumption from 2001 to 2004; however, the program did increase the consumption and income of richer households (above the median) by 6.1% (Park and Wang, 2010). Overall, the programs appear to have made a difference in targeted areas, but there remains doubt about the extent to which the programs actually have helped the poor living in those areas (Wang, 2005) and many poor live outside officially targeted areas and so do not realize any benefits (Park and Wang, 2012).

Broad-based rural income growth associated with market reforms and rapid economic development can explain most of the reductions in poverty. The introduction of the Household Responsibility System in the early 1980s returned authority over farm decisions to households, significantly increasing incentives and productivity. In combination with large agricultural price increases, this led to dramatic increases in rural incomes and a halving of the official poverty count from 250 million in 1978 to 125 million in 1985, the year *before* government poverty programs were set up. Poverty reduction actually slowed in the late 1980s after the poverty programs were in place. In general, poverty reduction in China has been strongly associated with agricultural growth, both across time and across regions (Ravallion and Chen, 2007; Montalvo and Ravallion, 2010). The importance of agricultural growth contrasts with Brazil and India where growth in the service sector is much more strongly associated with poverty reduction (Ravallion, 2010). This difference likely reflects China's relatively equitable land distribution. All rural households in China have access to land unlike in India where there is a large landless class or Brazil where land is very unequally distributed. Agriculture is also important because many of the poor live in remote areas with few local off-farm wage opportunities and find it difficult to migrate out due to limited labor, poor human capital, or the need to care for children or the elderly (Du et al, 2005; World Bank, 2009). Nonetheless, over time the share of agricultural income in total rural household income has fallen steadily while the share of wage income has increased to over 40% by 2011 thanks to robust growth

in the demand for (and wages of) migrant workers. In many poor villages, young adults have nearly all out-migrated. For this reason, nonagricultural growth is likely to play an increasingly prominent role in poverty reduction in the future.

3. Identifying and helping China's remaining poor

China's official poverty headcount rate is calculated as a share of the population with rural residential registration (*hukou*) and so excludes entirely the urban poor. This omission reflects China's large urban-rural divide dating from the socialist period. Urban residents were provided with wages, housing, education, and health care that were far superior to those available to rural residents. However, with massive layoffs of state enterprise workers in the late 1990s and a massive surge in rural-to-urban migration, it has become more likely for those living in urban areas to be poor. Still, efforts to quantify the extent of rural and urban poverty have generally found that rural poverty accounts for over 97% of total poverty (Ravallion and Chen, 2007; World Bank, 2009). Poverty in China has always been and continues to be predominantly a rural phenomenon.

Poverty rates are much higher in western China, where the topography is mountainous, fertile land is scarce, and the distance to ports and China's major cities is great. In 2003, the consumption poverty headcount rates using the \$1/day line were 21% and 29% in the Southwest and Northwest compared to 6%, 7%, and 13% in the Coast, the Northeast, and central China (World Bank, 2009). Minority villages and mountainous villages are concentrated in the West and have higher poverty rates than non-minority and non-mountainous villages (World Bank, 2009). Because of the geographic concentration of poverty in Western China, the Chinese government has used regional targeting to guide its public investments for poverty alleviation.

However, given that most of China's population lives in the East, despite having a lower poverty rate non-Western regions account for nearly half of China's poor; these poor are much more dispersed spatially than in the West. A cluster analysis aimed at revealing different types of poor populations using 2003 rural household survey data identified six categories of the poor, the key features of which are living in a minority area (20.6%), low land productivity (19.6%), high

dependency ratio (18.6%), low work capacity (17.3%), land scarcity (13.9), and remote location (8.6%) (World Bank, 2009). The prevalence of these different poverty groups varies considerably across regions. Nearly all of China's poor can be characterized as working poor, with less than 0.5% of the poor living in households with no able-bodied workers (World Bank, 2009). This diversity in the nature of poverty provides justification for developing a multipronged approach to poverty alleviation efforts that shifts the focus "from poor areas to poor people" (World Bank, 2009).

Another important feature of poverty in China is that much of the poverty is transient in nature. An analysis of three years of household survey from the early 2000s found that on average 17.8% of the rural population was consumption poor, but 30.9% were poor in at least one of the three years and only 6.9% were poor in all three years (World Bank, 2009). A study using 6 years of rural panel data from southern China in the late 1980s found that 7% to 13% of the population were poor in a given year even though their mean consumption was above the poverty line (Jalan and Ravallion, 1998). Both studies found that nearly half of poverty as measured by the poverty squared index is attributable to consumption variability. These findings suggest that social insurance and social protection programs as well as improved access to insurance and credit services may be important for addressing the transient nature of poverty.

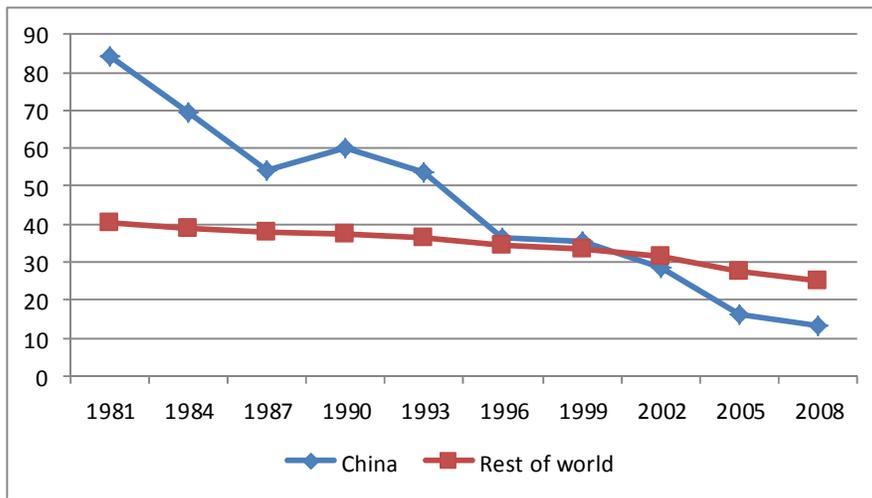
The Hu-Wen government has recognized this challenge and has made significant efforts to expand social protection and social insurance programs. Since the mid-2000s, China has aggressively expanded the rural minimum living standard (*dibao*) program, administered by the Ministry of Civil Affairs, to cover the entire country. The program in principle provides subsidies to bring household incomes up to the poverty line. However, the program is decentralized and benefits are often low and unevenly provided across regions and households. The government also runs other social assistance programs, including assistance to help pay medical fees, subsidies to support households lacking work capacity (*wubaohu* and *tekunhu*), and disaster relief. According to official statistics, rural health insurance now covers over 97% of the rural population, and a new rural pension program also is being scaled up nationally, with 326 million participants by year-end 2011.

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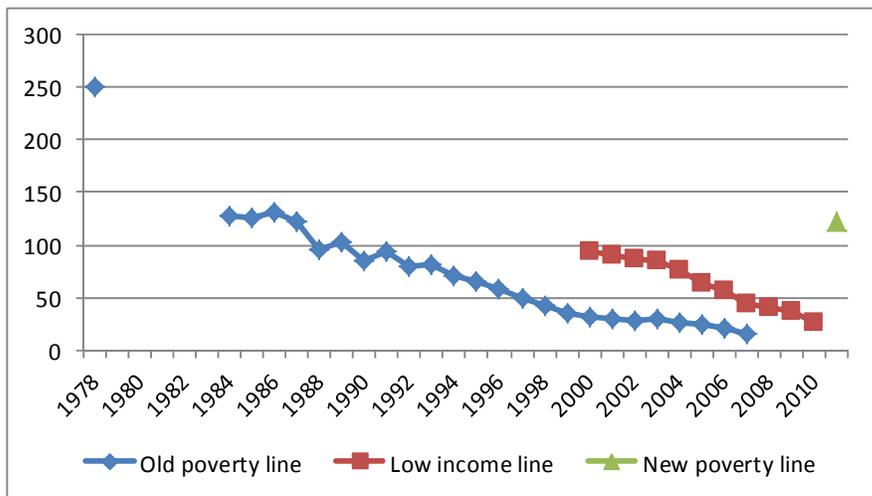
Figure 1: Poverty Headcount Rate (%) in China and the Rest of the World, 1981-2008.



Source: World Bank (2012).

Note: Based on consumption being below \$1.25 a day based on 2005 PPP.

Figure 2: China Official Poverty Count (millions), 1978-2011



Source: Leading Group Office for Poverty Alleviation and Development (LGOPAD)