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## Betting on the strong: Local government resource allocation in China's poverty counties



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### ABSTRACT

China's primary approach to addressing poverty in its rural areas has been geographic, through the targeting of loans, grants and public works at designated 'poverty counties'. The efficacy of this approach is increasingly being called into question as China faces entrenched poverty and rising inequality despite decades of rapid economic growth. At the same time, evidence is growing that recent reforms to fiscal policy have disadvantaged poverty counties, leaving them with limited resources with which to achieve poverty alleviation and rural service provision. This article considers how these two processes interact by explaining the pattern of resource allocation in a national poverty county in Shanxi Province. Evidence suggests that the county government, operating in a highly constrained fiscal environment, is betting on the strong. It concentrates resources in villages with better existing conditions to the detriment of poorer villages who are in greater need. Such a pattern of resource allocation amplifies existing inequalities and does little to address remaining poverty in rural China.

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### 1. Introduction

It is now widely acknowledged that the benefits of China's rapid economic growth have not been evenly shared. Despite immense gains in poverty alleviation, poverty – a predominantly rural phenomenon – remains entrenched in parts of China (Naughton, 2007, 212). Analysis based on an internationally comparable standard, rather than the relatively low Chinese official poverty line, suggests that rural poverty is still a serious and persistent problem<sup>1</sup> (Naughton, 2007; Ravallion and Chen, 2007). Indeed, the elasticity of poverty alleviation to economic growth has been decreasing, while aggregate growth is coming from sources that bring few gains to the poorest, suggesting that continued progress against poverty in rural China rests on addressing rising inequality in income, assets and opportunities (Ravallion and Chen, 2007; World Bank 2009, Wang, 2013). This inequality persists at many levels. The separate human development indices calculated by the United Nations Development Programme (UNDP) for China's urban and

rural areas (0.81 and 0.67) give a sense of widening urban–rural gaps in not just income, but education levels, life expectancy and other health indicators, reflecting a much larger problem of rural service provision (UNDP, 2005, 9). But inequality *amongst* rural residents is also increasing, and is evident not just at broad regional scales (i.e. inland versus coast), but at the county and even village levels (Wang and Hu, 1999, 200; UNDP, 2005, 27–28; Alm and Liu, 2013; Sun et al., 2014).

Unfortunately there is some disagreement in the literature as to the location and nature of poverty in rural China and therefore how it may best be addressed. It is typically argued that the remaining poverty in China exists in remote and marginal geographic “poverty traps” or “dead corners”, typically mountainous areas which suffer from poor natural resources and underinvestment (Jalan and Ravallion, 2002; Zhang et al., 2003; Sanders et al., 2007; Meng, 2013; Xue et al., 2013). It is argued that poverty alleviation and rural development funding is therefore best targeted at certain localities or administrative divisions (Yu et al., 2007). A contrary view is that the nature of poverty in China is more complex: that the poor are not necessarily confined to such poverty areas and that many residents in designated poor counties are not in fact poor (Riskin, 1994; Park et al., 2002). Indeed, growing income inequality between households living in the same village, province or region calls into question such a geographic focus (Benjamin et al., 2005).

Nonetheless, at the policy level, a kind of environmental determinism persists. Since 1986, China has pursued a ‘poor-area’

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<sup>1</sup> Ravallion and Chen's (2007) calculations, based on US\$1 PPP in 2002 (approximately 850 RMB per capita), show that 12.5 per cent of China's rural population are living in poverty, or 114 million people. Their estimates also suggest that while rapid progress was made between 1991 and 1996, poverty alleviation since 1996 has been very slow.

development strategy, targeting particular localities, namely counties, predominantly in inland provinces (Rozelle et al., 1998; Ravallion and Jalan, 1999; Merkle, 2003). This strategy focuses on promoting economic development through public investments rather than direct consumption subsidies (Park et al., 2002). Hence it is primarily the county, not the household or individual, that is identified as the unit requiring assistance, with 592 counties (out of a total of 2000) currently identified as nationally designated poverty counties (*guojia fupin kaifa zhongdian xian* 国家扶贫开发重点县) (Huang, 1999; Yu et al., 2007). Since the 1980s, these counties have been the beneficiaries of a number of poverty investment programs, including a subsidised loan program (the majority of loans go to industry), a public works program (infrastructure), and a budgetary grant program (development capital for agriculture, industry, education and health) (Park et al., 2002).

There is certainly evidence that poor counties have benefited over time from such targeted investment in terms of economic and income growth (see for instance Zhang et al., 2003; Meng, 2013). However, scholars raise three key concerns that suggest caution in using these results as a basis for continuing a poor-area strategy. First, much of this additional growth has been attributed to early direct investment in households for agricultural activities, investment that was later diverted in favour of local enterprises and came to lose its effectiveness (Rozelle et al., 1998). Second, very little evidence is available on the distribution of benefits *within* counties, hence, it remains unclear whether this kind of targeting has actually reached the poor within poor counties (Park et al., 2002). Third, there are problems in terms of political factors influencing the initial selection of poor counties in the 1980s, such that explicit criteria for designation were not strictly enforced, as well as strong resistance to removing poor county status, even if counties are no longer poor (Park et al., 2002, 125; Meng, 2013). Some argue that the entire poor-area strategy requires rethinking as it fails to capture the new forms, dynamics and severity of inequality and poverty in rural areas (Perkins, 2002; Christiansen and Zhang, 2009, 6; World Bank, 2009).

A further complication in this debate about the efficacy of a poor-area development strategy is the likely effect of recent fiscal reforms in China. These reforms have (once again) fundamentally changed the way revenue is collected and shared amongst different levels of government, and are shaping the ways in which the state invests in poverty alleviation. These changes are explained in the following section. Their effect on the process of allocating resources consistent with a poor-area strategy demands attention. Under earlier fiscal arrangements, studies drew the link between local government resource constraints and development prospects in poor counties (Park et al., 1996), but more up-to-date analysis is lacking.

This article engages with literature on fiscal policy, poverty alleviation and local governance in rural China to revisit the efficacy of China's poor-area development strategy in the current fiscal environment. It aims to explain the pattern of resource allocation in terms of poverty alleviation and rural development in one of China's poverty counties. Evidence is drawn from fieldwork conducted in Ji County, a national poverty county on the Loess Plateau in Shanxi Province.

More broadly, this article points to the ongoing importance of doing in-depth research in rural localities. While China is urbanising at a rapid pace and its place in the global economy is changing, its rural localities are equally undergoing transformation. These processes demand the attention of rural scholars, not just China scholars. The experience of Ji County raises questions about how the Chinese state's development 'project' translates to marginal, peripheral, and typically rural locations. Ji County is a site where uneven relations of wealth and power within the Chinese economy and across space are negotiated and reconfigured (Massey, 1994),

and where the increasing polarisation of Chinese society in terms of wealth, opportunities and access to resources is evident. These processes are certainly not unique to China, but they are occurring there on a very large scale.

The article proceeds as follows. The first section explains the recent changes in fiscal policy and implications for county governments in rural areas. The second section describes Ji County and the reasons for its selection, as well as the fiscal position of the county government and the characteristics of the four villages that are the focus of this research. The Results section describes the distribution of poverty and rural development-related initiatives in the county, compares these to the basis of need in two wealthier and two poorer villages, and explores the process of selecting villages for investment. The Discussion reflects on the behaviour of local officials in Ji County in terms of their fiscal and institutional environment, and draws attention to a number of problems related to China's current poverty strategy.

## 2. The changing nature of fiscal policy and its effects in rural China

China's fiscal policy has passed through various cycles of decentralisation and recentralisation as the central government has sought to negotiate its revenue and expenditure relationship with that of lower-level governments (provincial, city/prefecture, county and township) amid changing economic conditions. These cycles have been described in great detail elsewhere (see for instance Wong, 1991; Zhang, 1999; Naughton, 2007; Shen et al., 2012); only a brief summary is provided here.

From the early days of China's economic reform in the late 1970s until 1994, the fiscal autonomy of local governments was expanded through a system of particularised contracts with the centre, or "eating in separate kitchens" (*fenzao chifan* 分灶吃饭); an arrangement which aimed to promote local economic development (Shirk, 1993, 151; Wang, 1995). Over time, the extractive capacity of the central state went into decline and it came to rely on transfers from local governments which took control of an explosion in extra-budgetary revenue drawn from local enterprises (Wang, 1995). A period of centralisation followed, when in 1994 the central government introduced sweeping reforms that reassigned rights to various taxes and enabled it to collect the bulk of revenue and share it with the provinces (Naughton, 2007). Faced with increased revenue shortfalls, local governments came to rely on a proliferation of fees, levies and fines raised from farmers and local enterprises (Oi and Zhao, 2007; Liu et al., 2011). This additional taxation was one source of growing tension in rural areas: in response, beginning in 2000, "tax-for-fee" reforms (*shuifei gaige* 税费改革) were implemented to relieve farmers of their tax burdens by streamlining local revenue collection into a single agricultural tax and surcharge (Kennedy, 2007; Oi and Zhao, 2007). Then in 2004–2006 the agricultural tax and surcharge were completely eliminated (Kennedy, 2007; Li, 2007), thereby further recentralising central government control over revenue. To compensate local governments for loss of revenue following the tax-for-fee reforms, the central government introduced a system of fiscal transfers to provincial governments, which funnel funds to county governments and eventually to township governments (Yep, 2004; Oi and Zhao, 2007, 84). The outcome of these recent reforms is that the central government has further consolidated its control over revenue collection and distribution, but left local governments with increasing expenditure responsibilities (Naughton, 2007; Wu and Wang, 2013).

Given the tremendous variation in the wealth and resources of China's local governments, reflecting a still uneven spatial distribution of rural industry (Shen, 1999; Oi and Zhao, 2007), it is

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