

Research Note

Fiscal Reform, Fiscal Decentralization and Poverty Reduction in China: Some Observations

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Abstract

China has been said to be one of the world's most economically decentralized countries. While the claim that decentralization had much to do with the success of China's reforms has been controversial and it has been argued that China's approach to administrative decentralization might over time threaten the success of the reform process, the highly remarkable extent of fiscal decentralization could have the potential to aid the effort at poverty alleviation, especially in the context of the ethnoregional dimension of the country's poverty problem. This research note presents various observations on the dimensions of decentralization in China and briefly explores its potential implications on poverty reduction.

Keywords: *fiscal decentralization, administrative decentralization, government expenditure, government revenue, poverty reduction*

JEL classification: *H52, H71, H77, I38*

1. Introduction

The analyses on spatial dimension of politics in terms of decentralization in China have so far invariably utilized the typology of administrative versus economic decentralization.¹ This preference is not difficult to understand given the fact that the core dimension of such decentralization – that of political power – has the problem of applicability in the light of the centralism of the present political power configuration.

The following comment by a former Chinese vice-premier, cited in Li (2003: 1), reflects the reformers' feeling towards the lessons of the multiple cycles of administrative decentralization and recentralization in China: "A [more] important and fundamental lesson of the [1958] attempt to improve the economic management system is: We only saw the vices of overcentralization

of power, and sought to remedy the situation by decentralizing powers to the lower levels. When we felt too much power had been decentralized, we recentralized them. We did not then recognize the inadequacies of putting sole emphasis on central planning (and in particular a system dominated by mandatory planning) and totally neglecting and denying the role of the market [...] As a result over a long period of time (after the 1958 decentralization) we were trapped within the planned economy model. Adjustments and improvements could only work around the cycles of decentralization and recentralization. Moreover the recipients of more powers are invariably the local governments, rather than enterprises.”²

Cai and Treisman (2006) noted that China’s administrative decentralization only increased considerably during the 1980s, while before that the country had been administratively and politically highly centralized, and

As for appointments, from the late 1980s village officials have been locally elected. In practice, all other subnational appointments have been made by higher authorities, with the center exercising ultimate control. If fiscal decentralization means the subnational share of budget spending, this increased from about 53 percent in 1978 to 73 percent in 1996, before falling back to 70 percent in 2003. The subnational share of revenues fell from 85 percent in 1978 to 62 percent in 1985, then rose to 78 percent in 1993, before falling to 45 percent in 2003. Tax system design has remained a prerogative of the central authorities.

(Cai and Treisman, 2006: 4)

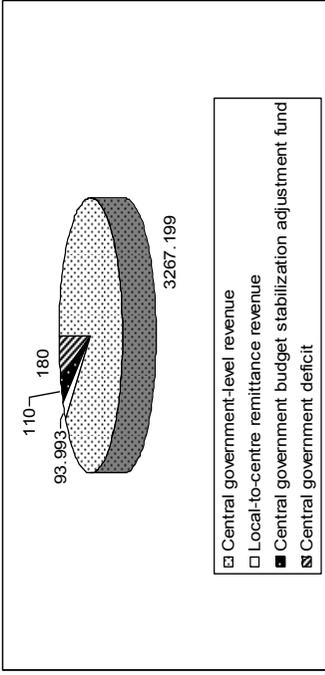
Political realities aside, the measurement of the degree of decentralization also suffers from the fact that it is very difficult to get complete information on government revenues and expenditures as the budget is incomplete and many government revenues and expenditures are not included in the budget and hence reliable figures for overall government revenues and expenditures are never available (Yeoh, 2009: 241).

2. The Administrative Dimension: Subnational Autonomy

The 2008 central and local budget implementation report and 2009 central and local budget draft³ presented on the 11th National People’s Congress, second meeting, on 5th March 2009 reported for year 2008 a national total revenue of 6.13169 trillion yuan⁴, comprising central revenue of 3.267199 trillion yuan and local revenue of 2.864491 trillion yuan. From the perspective of fiscal IGR (intergovernmental relations), for year 2008, central-to-local tax revenue rebate and transfers amounted to 2.294561 trillion yuan – with an increase of 26.5 per cent over the previous year – comprising central-to-local tax revenue rebate of 0.428219 trillion yuan (with an increase of 3.9 per cent over the previous year), financial (including general) transfers of 0.869649 trillion yuan

Figure 1 China: Central Government's Fiscal Balance, 2008 (billion yuan)

Central Government Revenue 3741.192 billion yuan and Deficit 180 billion yuan



Central Government Expenditure 3651.192 billion yuan

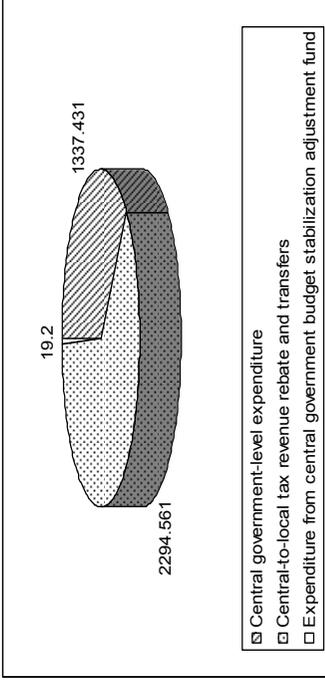
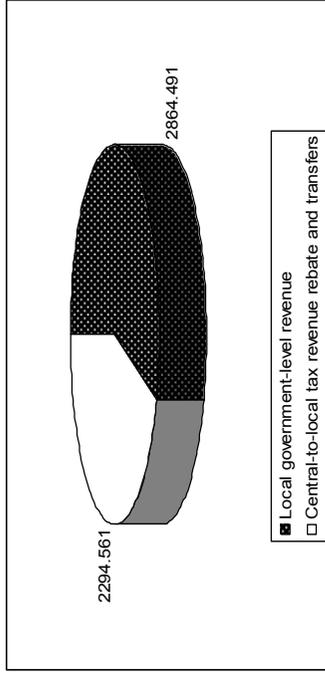
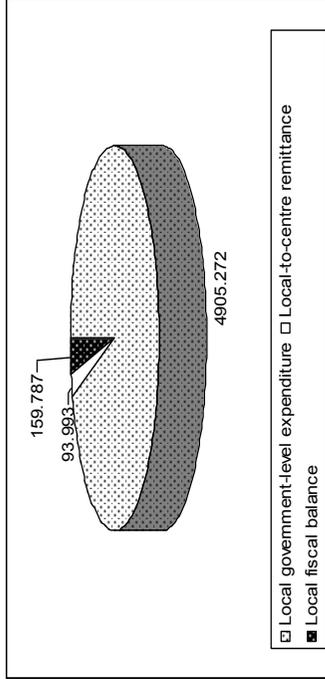


Figure 2 China: Local Governments' Fiscal Balance, 2008 (billion yuan)

Local Government Revenue 5159.052 billion yuan



Local Government Expenditure 4999.265 billion yuan and Fiscal Balance 159.787 billion yuan



Source: Data for Figures 1 and 2 from 关于 2008 年中央和地方预算执行情况与 2009 年中央和地方预算草案的报告.htm <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengxinwen/200903/t20090316_122544.html>.

Table 1 China: Central Government Expenditure, 2008 and 2009 (billion yuan)

Item	2008 (Actual)	2009 (Estimate)	2009 Estimate as % of 2008 Actual
<i>General Public Service</i>	121.665	131.361	108.0
including: Central government-level expenditure	106.015	101.386	95.6
Transfer payments to local governments	15.650	29.975	191.5
<i>Foreign Affairs</i>	23.924	26.893	112.4
including: Central government-level expenditure	23.916	26.893	112.4
Transfer payments to local governments	0.008		
<i>Defense</i>	410.141	472.867	115.3
including: Central government-level expenditure	410.093	472.251	115.2
Transfer payments to local governments	0.048	0.616	1283.3
<i>Public Security</i>	87.577	116.131	132.6
including: Central government-level expenditure	64.862	73.26	112.9
Transfer payments to local governments	22.715	42.871	188.7
<i>Education</i>	159.854	198.062	123.9
including: Central government-level expenditure	49.165	62.327	126.8
Transfer payments to local governments	110.689	135.735	122.6
<i>Science and Technology</i>	116.329	146.103	125.6
including: Central government-level expenditure	107.741	142.824	132.6
Transfer payments to local governments	8.588	3.279	38.2
<i>Culture, Sport and Media</i>	25.281	27.975	110.7
including: Central government-level expenditure	14.061	14.228	101.19
Transfer payments to local governments	11.22	13.747	122.5
<i>Social Security and Employment</i>	274.359	335.069	122.1
including: Central government-level expenditure	34.428	30.048	87.3
Transfer payments to local governments	239.931	305.021	127.1
<i>Low-income Housing</i>	18.19	49.301	271
including: Central government-level expenditure	0.711	3.138	441.4
Transfer payments to local governments	17.479	46.163	264.1
<i>Healthcare and Hygiene</i>	85.445	118.056	138.2
including: Central government-level expenditure	5.396	5.628	104.3
Transfer payments to local governments	80.049	112.428	140.4
<i>Environmental Protection</i>	104.03	123.662	118.9
including: Central government-level expenditure	6.621	3.735	56.4
Transfer payments to local governments	97.409	119.927	123.1
<i>Township and Village Community Affairs</i>	6.316	0.395	6.3
including: Central government-level expenditure	0.722	0.365	50.6
Transfer payments to local governments	5.594	0.03	0.5

Table 1 (continued)

Item	2008 (Actual)	2009 (Estimate)	2009 Estimate as % of 2008 Actual
<i>Agriculture, Forestry and Water</i>	270.22	344.659	127.5
including: Central government-level expenditure	31.439	30.34	96.5
Transfer payments to local governments	238.781	314.319	131.6
<i>Transport</i>	160.029	188.72	117.9
including: Central government-level expenditure	103.759	93.475	90.1
Transfer payments to local governments	56.27	95.245	169.3
<i>Extraction, Electricity and Information, etc.</i>	60.076	75.75	126.1
including: Central government-level expenditure	45.596	48.936	107.3
Transfer payments to local governments	14.48	26.814	185.2
<i>Food, Oil, Material Reserve, etc.</i>	110.51	178.045	161.1
including: Central government-level expenditure	60.063	83.843	139.6
Transfer payments to local governments	50.447	94.202	186.7
<i>Financial Affairs</i>	97.551	31.558	32.4
including: Central government-level expenditure	97.551	31.558	32.4
Transfer payments to local governments			
<i>Expenditure for Recovery and Reconstruction after Earthquake</i>	60	97	161.7
including: Central government-level expenditure	6.246	13.061	209.1
Transfer payments to local governments	53.754	83.939	156.2
<i>Expenditure for Interest Payment on National Debt</i>	127.869	137.185	107.3
including: Central government-level expenditure	127.869	137.185	107.3
Transfer payments to local governments			
<i>Contingency</i>	40		
<i>Other Expenditures</i>	56.694	168.839	297.8
including: Central government-level expenditure	41.177	83.119	201.9
Transfer payments to local governments	15.517	85.72	552.4
<i>Tax Revenue Rebate to Local Governments</i>	334.226	493.419	147.6
<i>General Transfer Payments to Local Governments</i>	827.713	885.45	107
Central Government Expenditure	3538	4386.5	124
Central Budget Stabilization Adjustment Fund	19.2		

Source: <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengshuju/200903/t20090319_124155.html>.

Table 2 China: Transfers from Central Government and Sub-total Revenue (i.e. Revenue which Are Not Transfers from Central Government) of Local Governments, 1999-2008, and General and Earmarked Transfers and Tax Revenue Rebate, 2008 (billion yuan)

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
A) Central-to-Local Governments' Transfer Payments										1866.342
1) General Transfers										869.649
2) Earmarked Transfers										996.693
B) Central-to-Local Governments' Tax Revenue Rebate										428.219
Central-to-Local Governments' Tax Revenue Rebate and Transfers (A+B)	408.661	466.531	600.195	735.177	826.141	1040.796	1148.402	1350.145	1811.245	2294.561
Sub-total Revenue of Local Governments	559.487	640.606	780.33	851.5	984.998	1189.337	1510.076	1830.358	2356.504	2864.491
Total Revenue of Local Governments	968.148	1107.137	1380.525	1586.677	1811.139	2230.133	2658.478	3180.503	4167.749	5159.052

Sources: Zhongguo Caizheng Nianjian 中国财政年鉴, various years;

<http://www.mof.gov.cn/mof/hengwuxinxi/caizhengshujij/200807/t20080728_59019.html>;
<http://www.mof.gov.cn/mof/hengwuxinxi/caizhengxinwen/200903/t20090316_122544.html>.

(with an increase of 22 per cent), earmarked transfers of 0.996693 trillion yuan (with a substantial increase of 44.6 per cent mainly due to the increase in subsidizing local education, healthcare and other major development items). Central-to-local tax revenue rebate and transfers thus form local revenue and spent by local arrangement. An average 38 per cent of local government expenditure was funded by central government transfers, and in the case of the central and western regions an average 54.4 per cent of local government expenditure was funded by such central government transfers.

On the part of local government finance, revenue totaled 5.159052 trillion yuan – an increase of 23.7 per cent over the previous year – comprising a) local own revenue of 2.864491 trillion yuan and b) central-to-local tax revenue rebate and transfers totaling 2.294561 trillion yuan.

Placed within the framework of the trichotomy of fiscal, administrative and political dimensions of decentralization (see, for example, UNDP, 2002, and Schneider, 2003), the above figures could show the extent of decentralization, in particular in the administrative dimension.

Schneider (2003: 33) hypothesizes three core dimensions of the decentralization concept:

Fiscal decentralization refers to how much central governments cede fiscal impact to non-central government entities. Administrative decentralization refers to how much autonomy non-central government entities possess relative to central control. Finally, political decentralization refers to the degree to which central governments allow noncentral government entities to undertake the political functions of governance, such as representation.

One of the ways to gauge the degree of administrative decentralization or “local administrative autonomy” is by examining the control exercised over local revenue:

The percentage of local revenues from taxes provides an indicator of the degree of subnational control over resources. Taxes are different from the total amount of resources, which is more a measure of wealth rather than control [...] subnational revenues are a combination of taxes, transfers, grants, and loans. Taxes offer the greatest degree of autonomy, grants, and loans offer somewhat less, and discretionary transfers probably the least. Transfers, even supposedly automatic ones, can be withheld, and grants and loans generally arrive with conditions or with expenditures earmarked.

(*ibid.*: 38-39)

Besides this, according to Schneider, subnational autonomy can also be measured by looking at the percentage of total grants and revenues not accounted for by transfers, which

[...] could conceivably include taxes, loans, fees, sales of assets, or informal contributions. There are some drawbacks to excluding all transfers, which

do not distinguish for example between transfers over which lower levels of government have total control, such as block grants, and transfers that are tied to central government priorities, such as earmarked transfers, or transfers that require certain behaviors by subnational governments, such as matching or fiscal balance. Still, the treatment of all revenues aside from transfers gives an indication of the degree to which subnational governments raise their own funds through taxes, loans, fees, or sales of assets.

(*ibid.*: 39)

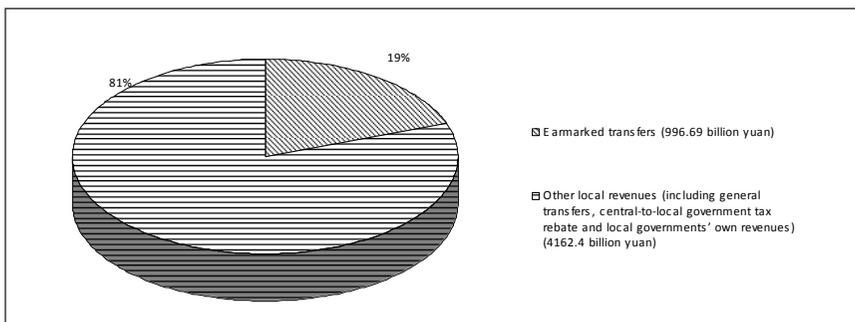
Figures from the above report for 2008 show a central-to-local tax revenue rebate to all transfer ratio of 0.428 : 1.866 or the former as about 23 per cent of the latter amount. On the other hand, non-earmarked transfers were 46.6 per cent of total transfers.

Figure 3 shows a comparison of earmarked transfers and other local revenues including general transfers, central-to-local tax revenue rebate and local governments' own revenue. It could be seen that for year 2008 local revenues which are not earmarked transfers constituted 81 per cent of total local revenues.

From the time-series perspective, it can be seen in Figures 4 and 5 that from 1999 to 2008 local government revenues which were not transfers from the central government always constituted slightly above half of the total local government revenues.

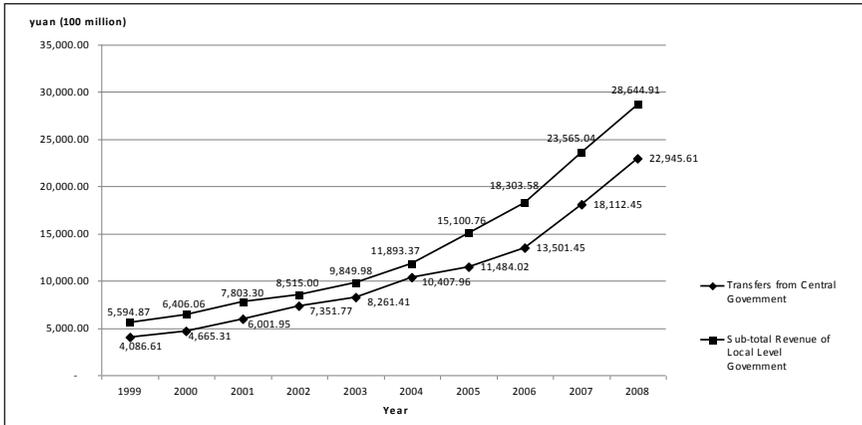
Figure 6 shows central-to-local transfers for year 2008 (actual) and 2009 (estimate). It can be seen that earmarked transfers are slightly larger than general transfers. Details of the general transfers by items in 2008 are shown in Figure 7, and details of earmarked transfers by item in 2008 are shown in Figure 8.

Figure 3 China: Central-to-Local Governments' Earmarked Transfers and Other Local Government Revenues, 2008



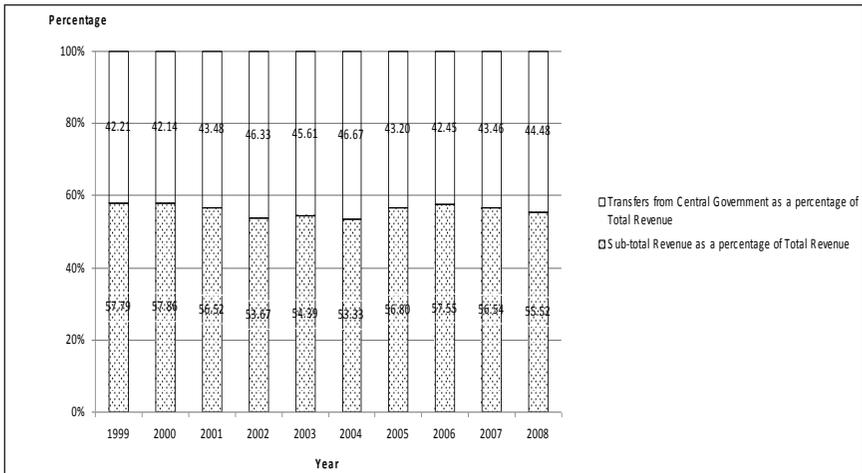
Source: Data from <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengxinwen/200903/t20090316_122544.html>.

Figure 4 China: Transfers from Central Government and Sub-total Revenue (i.e. Revenue which Are Not Transfers from Central Government) of Local Governments, 1999-2008



Sources: Data from Zhongguo Caizheng Nianjian 中国财政年鉴, various years; <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengshuju/200807/t20080728_59019.html>; <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengxinwen/200903/t20090316_122544.html>.

Figure 5 China: Transfers from Central Government and Sub-total Revenue (i.e. Revenue which Are Not Transfers from Central Government) as Percentages of Total Revenue of Local Governments, 1999-2008



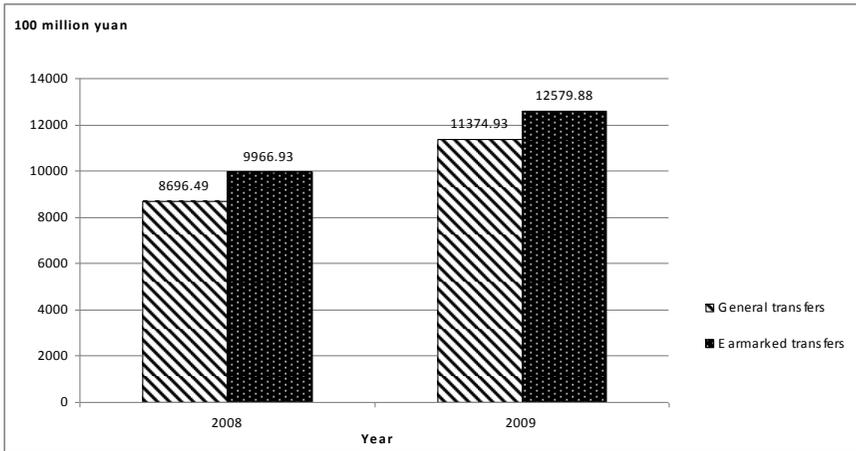
Sources: Data from Zhongguo Caizheng Nianjian 中国财政年鉴, various years; <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengshuju/200807/t20080728_59019.html>; <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengxinwen/200903/t20090316_122544.html>.

Table 3 China: Central-to-Local Governments' Transfer Payments and Tax Revenue Rebate, 2008-2009 (billion yuan)

Item	2008 (Actual)	2009 (Estimate)	2009 Estimate as % of 2008 Actual
I. Central-to-Local Governments' Transfer Payments	1866.342	2395.481	128.4
(1) <i>General Transfers</i>	869.649	1137.493	130.8
1. Equalization transfers	351.052	391.8	111.6
2. Nationality areas transfers	27.579	28	101.5
3. Basic fiscal security subsidy for counties and villages	43.818	55	125.5
4. Wage adjustment transfers	239.23	236.563	98.9
5. Transfers for rural tax and fee reform	76.254	77.022	101
6. Fiscal transfers for urban resource depletion	2.5	5	200
7. Fixed-amount subsidies (original institutional subsidies)	13.614	13.814	101.5
8. Enterprise unit subsidies	33.5	34.8	103.9
9. Fiscal balance subsidies	35.466	34.451	97.1
10. Transfers for industrial and commercial departments after abolition of "two fees"	4.7	8	170.2
11. Village-Level Social Welfare "One-Event-One-Suggestion" Award Fund		1	
12. General Public Service Transfers		4.5	
13. Public Security Transfers		33.29	
14. Education transfers	41.936	90.849	216.6
15. Social Security and Employment Transfers		123.404	
(2) <i>Earmarked Transfers</i>	996.693	1257.988	126.2
Including: Education	68.753	44.886	65.3
Science and technology	8.588	3.279	38.2
Social security and employment	239.931	181.617	75.7
Healthcare and hygiene	80.049	112.428	140.4
Environmental protection	97.409	119.927	123.1
Agriculture, forestry and water	238.781	314.319	131.6
II. Central-to-Local Governments' Tax Revenue Rebate	334.226	493.419	147.6
Rebate of "Two Taxes"	337.2	347.6	103.1
Income Tax Base Return	91.019	91.019	100
Product and Oil Price and Tax-Fee Reform Tax Revenue Rebate		153	
Revenue from submitting of local government	-93.993	-98.2	104.5
Central-to-Local Governments' Tax Revenue Rebate and Transfer Payments	2200.568	2888.9	131.3

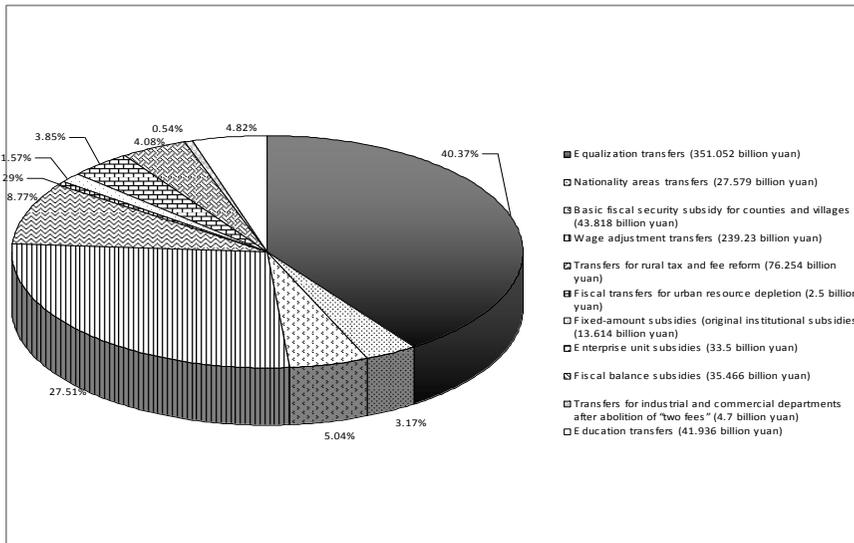
Source: <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengshuju/200903/t20090319_124155.html>.

Figure 6 China: Central-to Local Governments' Transfer Payments, 2008-2009



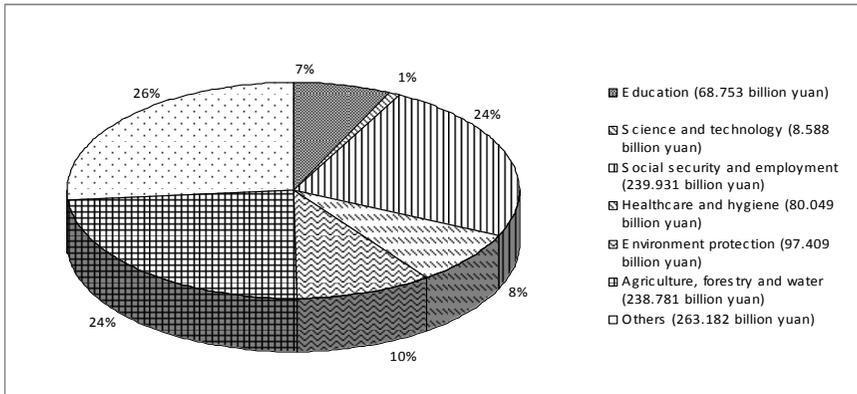
Source: Data from <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengshuju/200903/t20090319_124155.html>.

Figure 7 China: Central-to-Local Governments' General Transfers by Item, 2008 (Actual)



Source: Data from <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengshuju/200903/t20090319_124155.html>.

Figure 8 China: Central-to-Local Governments' Earmarked Transfers by Item, 2008 (Actual)



Source: Data from <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengshuju/200903/t20090319_124155.html>.

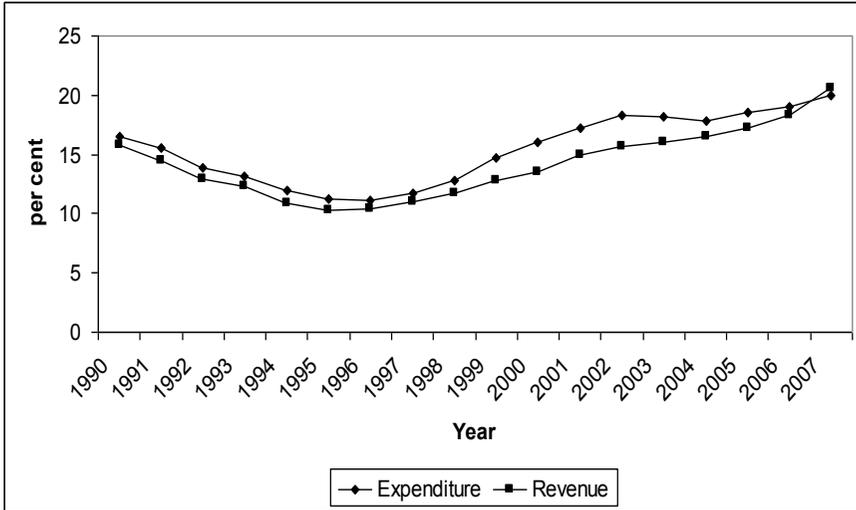
3. Fiscal Decentralization

Hypothesizing that the best indicator for the level of fiscal centralization or decentralization is the share of subnational expenditures and revenues, Schneider (2003: 36) explained that

The choice of focusing on fiscal instruments rather than regulatory or financial policies is partly methodological and partly substantive. Governments use various instruments to influence the amount and distribution of wealth in society. Because regulatory instruments are built into the formal and informal institutions that govern civil society and private sector, they are extremely complex and context-specific. Financial instruments are similarly difficult to measure with statistics, and their impact on distribution is not as direct as fiscal policy. Fiscal policy offers the best window into levels of fiscal decentralization. Decentralization of regulatory or financial mechanisms will thus have to be taken up in individual country studies.

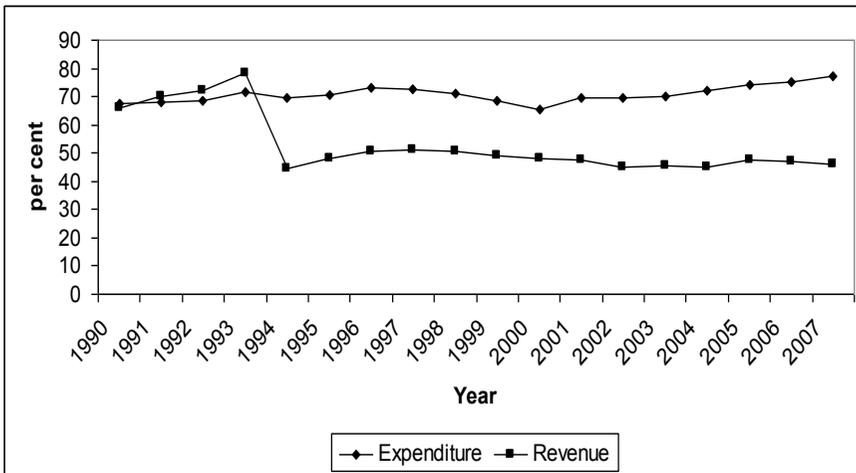
The degree of Chinese fiscal decentralization can be seen in Figures 9, 10 and 11. Figure 9 shows, among others, that revenue collection had been falling rapidly as the traditional tax base of the command economy eroded with the onslaught of market reform and this fiscal decline continued well into the early 1990. It was in this climate that the 1994 fiscal reform was introduced as an effort by the central government to regain control and recoup lost revenues via a new system of dual taxation (tax sharing) that redefined central government's and regional governments' revenues. The comprehensive reform in effect redefined the whole intergovernmental fiscal relations (fiscal IGR) by

Figure 9 China: Government Expenditure and Revenue as Percentages of GDP, 1990-2007



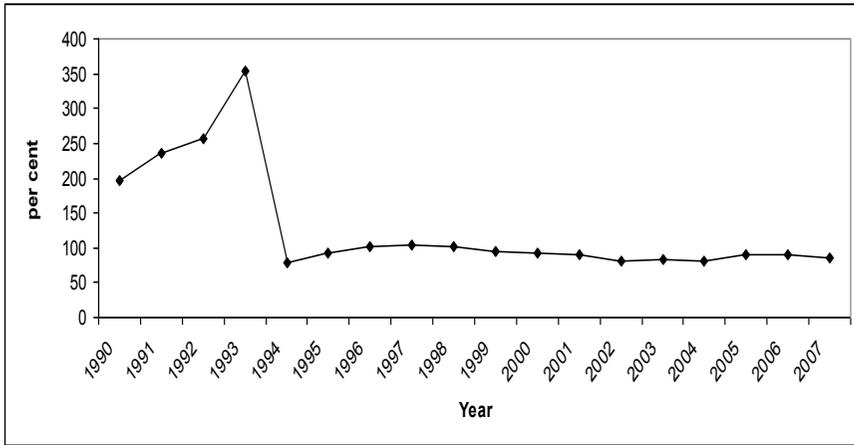
Source: Computed with data from *China Statistical Yearbook*, various years.

Figure 10 China: Local Government Expenditure and Revenue Respectively as Percentages of Total Government Expenditure and Revenue, 1990-2007



Source: Computed with data from *China Statistical Yearbook*, various years.

Figure 11 China: Ratio of Local to Central Government Revenue, 1990-2007



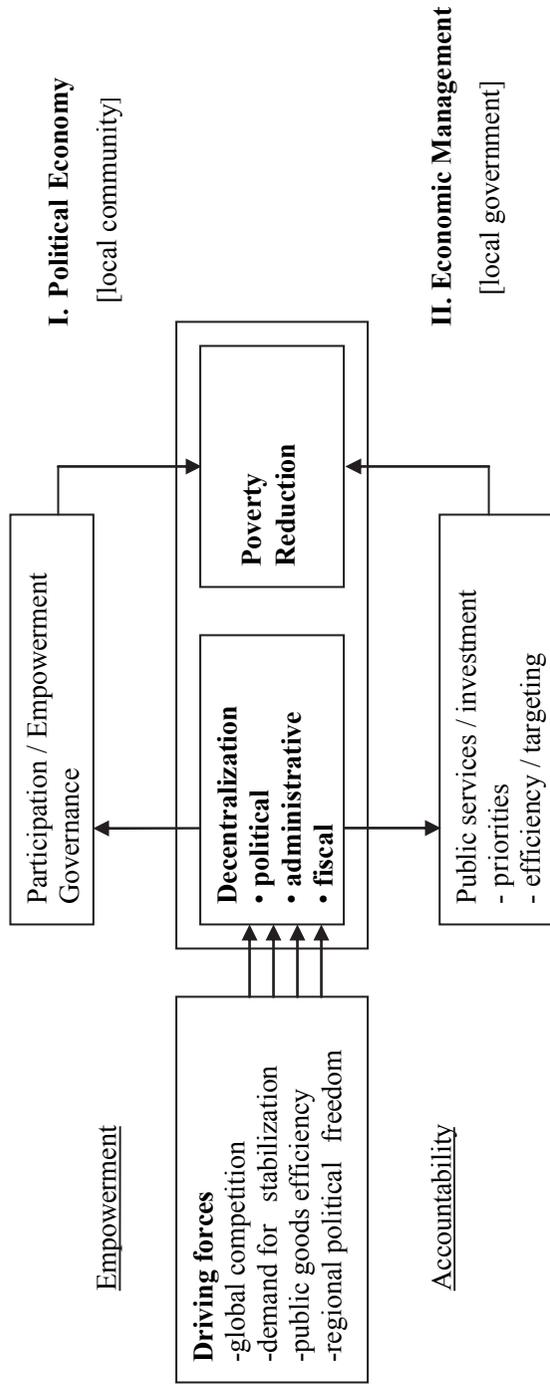
Source: Computed with data from *China Statistical Yearbook*, various years.

changing the structure of the main taxes, responsibilities in tax administration, revenue-sharing arrangements, and weakened the ability of the regional governments to employ surreptitious approaches for revenue mobilization. China's proportion of local public spending in total national public spending is actually much higher than those of the major federal countries in the world. China's local public spending has since the mid- and late 1980s been steady at about 70 per cent of her total national public spending (Figure 10), whereas in federal countries such as the US, Germany and Russia, the proportions of local public spending in total national public spending are only respectively 46 per cent, 40 per cent and 38 per cent (Yeoh, 2009: 246). Furthermore, the scope of China's economic decentralization goes far beyond decentralization in public finance, but even measured solely by the latter, China has been said to be one of the world's most economically decentralized countries.

4. Poverty and Decentralization

While Cai and Treisman challenged the claim that decentralization had much to do with the success of China's reforms and her subsequent economic miracle, von Braun and Grote (2000: 15) warned that China's approach to administrative decentralization which relies on negotiations rather than rules to define relations between the central government and the four sub-national tiers (provinces, prefectures/cities, counties and villages/townships) might over time threaten the success of the reform process.⁵

Figure 12 Von Braun and Grote's Conceptual Framework on Decentralization and Poverty Reduction



Source: von Braun and Grote (2000: 7), Figure 1.

Pursuing the second link outlined in their conceptual framework delineated in Figure 12 – whether public services for the poor are fostered by decentralization, and by fiscal decentralization in particular – von Braun and Grote (2000) commented that the 1994 tax reform seemed to have failed to arrest the trend towards worsening interregional inequality, as the loyalty of the local governments shifted away from the national government to the subnational level⁶ since taxes belonged to the central government unless specifically assigned to the localities. As the local rural governments began to impose a host of fees and levies since the higher-level governments were not able to subsidize existing services due to fiscal strain, the poorer regions hence might be victimized as they were less able to do the same (*ibid.*: 20). In fact, in order to end the wanton charging of fees by schools and to further regulate and strengthen the fee management system of schools to reduce the economic burden of families with school-age children especially the rural poor, the government began implementing the one-fee system (*yi fei zhi* 一费制) in the poor areas. One-fee reform was remarkably effective in stopping education cost from rising too fast and in reducing peasant families' liabilities, as well as to a certain extent increasing the rate of enrolment. However, *Zhongguo Fazhan Baogao 2007 – Zai Fazhan zhong Xiaochu Pinkun* [China Development Report 2007 – Eliminating Poverty through Development in China] warns that the fee reduction also has the tendency to compromise the quality of education, due to schools' financial difficulties and debts. On the other hand, as one of the seven prongs of the western regional 2004-2007 plan to achieve comprehensive nine-year education and basically eliminate youth and adult illiteracy in the western region by 2007⁷, the “two exempts and one subsidy” (*liang mian yi bu* 两免一补) scheme aims at solving the problem of children of poor families in backward areas attending school. Under this scheme, the central government provided free textbooks, while the various tiers of the local governments took up the responsibility of exempting poor students from sundry fees and subsidizing boarding expenses. *Liang mian yi bu* specifically targets compulsory education stage students living in rural areas (with main source of family income being agriculture), studying in rural (including village, township and county town) primary and secondary schools, who are unable to pay for textbooks, sundry fees and boarding expenses due to economic difficulties of their families (also including county-level students with disabilities). The report indicates that central government expenditure for this purpose in 2004 amounted to 1.17 billion yuan, with 32 per cent of students from poor families in the central and western regions provided with free textbooks. The number of primary and secondary students from poor families in the rural compulsory education stage benefiting from free textbooks in the central and western regions reached about 30 million people. Nationwide government expenditure for

rural compulsory education amounted to 184 billion yuan in 2006, exempting all 52 million students at rural compulsory education stage in the western region and part of the central region from school and sundry fees, providing free textbooks for 37.3 million students from poor families, and subsidizing living expenses for 7.8 million boarding students. To further strengthen the development of rural foundational education, The report notes that the central government has also decided to extend the *liang mian yi bu* scheme to all rural areas nationwide to provide educational opportunity for more children from poor families.

Besides such schemes targeting at education, whole-village development (*zheng cun tuijin* 整村推进) – one of the three foci⁸ of China's current rural developmental poverty assistance – on the other hand aims at using relatively large-scale capital and other resources to greatly enhance in a relatively short time the assisted village in terms of foundational and social services and amenities, living and production conditions as well as industrial development, leading to better coordination of various items to achieve greater integrated benefits, hence enabling the poor population to get out from poverty, and at the same time enhancing the integrated productive capability of the poverty community and population and their ability to withstand risks. *Zhongguo Fazhan Baogao 2007* cited government statistics on 70 thousand poverty villages in 16 provinces/zizhiqu (including Hebei, Jilin, Heilongjiang, Jiangxi, Anhui, Henan, Hubei, Hunan, Guangxi, Hainan, Sichuan, Yunnan, Shaanxi, Qinghai, Ningxia and Xinjiang) which gave the average poverty assistance fund for each poverty village at 2.28 million yuan. Of the 16 provinces/zizhiqu, 12 have average fund planned at between 1 million and 3 million yuan, only Guangxi and Heilongjiang have more than 3 million yuan planned, with Guangxi having more than 13 million yuan. On the other hand, two provinces i.e. Hunan and Yunnan, have lower than 1 million yuan. According to the statistics, till mid-2005, the average poverty assistance investment for each poverty village was 0.34 million yuan, which met only 15 per cent of the demand. The report emphasized that even with the assumption that all these investments were used on poverty villages that have already implemented the whole-village development programme (only 32 per cent of the poverty villages have implemented the whole-village development programme), the average fund for each of such villages was merely 960000 yuan. Hence, the actual poverty assistance investment and planned investment were seriously inadequate to meet the actual demand. Only Jilin, Jiangxi, Henan, Guangxi, Ningxia and Xinjiang have average poverty assistance investment exceeding 50 thousand yuan, while Hubei, Hunan, Hainan and Qinghai have average investment of each poverty village less than 20 thousand yuan. The findings also showed that except for a minority of poverty villages where the provincial/zizhiqu/zhixiashi units⁹ and leadership were directly responsible in

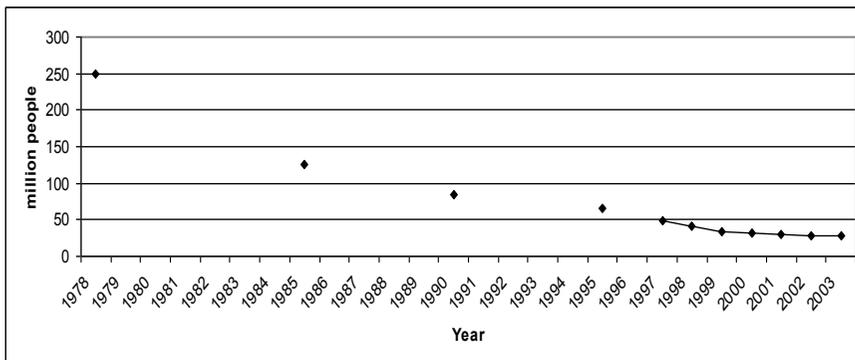
supporting the programme, most poverty villages were either not getting any poverty assistance investment at all or only very limited funds. Besides, the report's findings also showed great discrepancy in the income growth among different rural families in the same village under the programme, and the main beneficiaries from poverty assistance investment are the relatively richer rural families in the poverty villages, due mainly to the need for the rural families themselves to provide a part of the capital (matching fund) which is beyond the capability of those in absolute poverty.

5. Concluding Remarks

This research note has presented various observations on the dimensions of decentralization in China which has been said to exhibit the rather unusual combination of high political centralism and high fiscal/economic decentralization, and given the still grave situation of overall Chinese poverty even after the remarkable poverty reduction achievements over the last few decades (see Figures 13 and 14), it is indeed pertinent to include the implications on poverty reduction and interregional disparity in further research on fiscal reform and dimensions of decentralization.

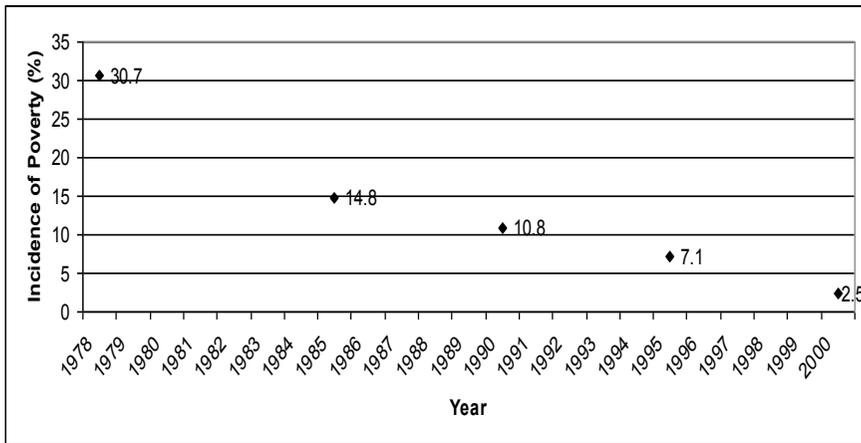
As poverty and inequality constitute one of the most, if not *the* most, critical challenges China faces in her next phase of politico-socioeconomic development, and poverty in China has the properties of being concentrated in the western region and in the ethnic minority areas, ethnoregionalization of poverty inevitably ensues (Yeoh, 2009: 269-272), presenting China not only with economic challenges but also long-term sociopolitical security risks. The solving of the remaining problems of poverty and inequality, still daunting despite the impressive achievements in the last few decades, in this vast nation

Figure 13 China: Rural Population in Poverty



Source: Chen (2006: 174), Figure 7-1.

Figure 14 China: Rural Incidence of Poverty



Source: *Zhongguo Diqu Jingji Fazhan Zhanlüe Yanjiu*, 2003, p. 47, Table 3-6.

has duly been the focus of researchers and policymakers, whether the policy suggestions, to give a few examples, be in the form of Woo's four points of implementing programmes that strengthen the three mechanisms of income convergence (i.e. free movement of goods, people and capital), that provide infrastructure, that focus on rural poverty and that mobilize the universities for growth (Woo, 2004), or Fan *et al.*'s seven points of increasing overall public investment in rural areas, increasing public investment in agricultural R&D, in rural education, in rural infrastructure, in improving the efficiency of existing public irrigation systems, as well as improving the targeting of funds to the poor and increasing fiscal transfers from the richer coastal region to the poorer western regions, in view of the country's decentralized fiscal system and the western region's small tax base (Fan *et al.*, 2002: 50-51), or *Zhongguo Fazhan Baogao 2007*'s nine points of establishing the "developmental poverty line" standard to readjust long-term poverty alleviation policy, establishing a poverty alleviation credit system and ways for private finance institutions to participate in poverty alleviation, establishing a sound social security system both urban and rural, advancing the progress of urbanization and the provision of social security and public services to rural-to-urban migrants, providing more equitable educational opportunity, expanding human resource development (including skill training and re-training) for rural labour, improving rural medical services, establishing a rational public finance system and strengthening public governance for poverty alleviation, and enhancing the role of non-governmental organizations in poverty alleviation (*Zhongguo Fazhan Baogao 2007*, pp. 174-182).

The highly remarkable extent of fiscal decentralization that exists in China should be further enhanced to aid the effort at poverty alleviation, especially in the context of the ethnoregional dimension of the poverty problem. In recent years, local and international organizations around the world are increasingly advocating decentralization to bring about more effective poverty reduction, with both the direct effects on the regional targeting of transfers and the indirect effects of overcoming the inefficiency in local public services and hampered economic growth related to sub-optimal decentralization (von Braun and Grote, 2000: 2). Although theoretically there may not be a clear-cut functioning relationship between decentralization and poverty reduction, most research findings in recent years definitely pointed to the positive. Von Braun and Grote (2000) pointed out that political, administrative and fiscal decentralizations need to be considered simultaneously, and the sequencing and pace of these three aspects of decentralization seem to play an important role in impacting poverty reduction. While fiscal decentralization shows ambivalent effects for poverty reduction and administrative decentralization alone does not add power and voice to the poor, “political decentralization often benefits the poor, because involving civil society in planning, monitoring and evaluating public programs and policies is crucial to ensure steady progress and that is facilitated in a decentralized system” (*ibid.*: 25-26), or, as Boex *et al.* pointed out in their research report “Fighting Poverty through Fiscal Decentralization” (January 2006: 2), “if the increasingly accepted wisdom that ‘all poverty is local’ is correct, then decentralization policy and poverty reduction strategies could be closely intertwined and have synergetic positive effects on each other”¹⁰. Kyei (2000), in his study on the case of Ghana, concluded that the rural poor in Ghana could only benefit with a much stronger commitment from the central government to decentralization, especially in terms of powersharing and financial provision. Vijayanand (2001), in his paper on the Kerala state of India, noted various advantages of decentralization in terms of poverty reduction including the greater reach of resources with earmarking of funds for the disadvantaged groups, less sectoralism in decentralized programmes with greater convergence contributing to the reduction in the ratchet effect of poverty, greater emphasis on locally appropriate and affordable solutions, greater realism in tackling problems of poverty, improved accountability, etc. while decentralization “affords opportunities to the poor to grow in strength by continuous participation (learning by doing), constant observation of the exercise of power (learning by seeing) and accessing more information (learning by knowing)” (p. 23). Hence, given the crucial ethnoregional dimension of China’s poverty problem, it is pertinent that the poverty alleviation effort of the country should benefit from any possible progress in decentralization – fiscal, administrative, and most importantly, political – since decentralized

governments, due to their closeness both institutionally (e.g. ethnically) and spatially to citizens in the regional/rural areas, could be more responsive to the needs of the poor than the central government and hence are more likely to successfully formulate and implement pro-poor policies and programmes in these regions and areas.

Notes

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1. See Li (2003) which cited the 1968 work of Franz Schurmann (who called these type 2 and type 1 decentralization) and that of James Townsend and Brantly Womack (1986).
 2. Bo Yibo 薄一波 (1993), *Ruogan Zhongda Juece yu Shijian de Huigu* 若干重大决策与事件的回顾 [Looking back at some important decisions and events], p. 804, cited in Li (2003).
 3. 关于2008年中央和地方预算执行情况与2009年中央和地方预算草案的报告.htm <http://www.mof.gov.cn/mof/zhengwuxinxi/caizhengxinwen/200903/t20090316_122544.html>.
 4. “Yuan 元” is the largest denomination of China’s currency “renminbi 人民币” (“people’s currency”, Rmb), equivalent to about US\$0.146. Following the US (rather than British) convention, billion = 1000,000,000 and trillion = 1000,000,000,000.

5. Braun and Grote (2000: 15) noted that in China “the allocation of responsibilities across tiers of government remains unclear, except for health and education which are controlled by the provinces [...] While administrative discretion has helped preserve the momentum for growth and reform, it has also created opportunities for corruption.”
6. As von Braun and Grote (2000: 20) noted, provincial tax officers, aiming to establish some tax autonomy, “entered into direct negotiations with enterprises for payments and transferred tax funds that would otherwise have been shared with the central government into local extra budgetary accounts.”
7. The seven prongs are 1) implementation of the rural boarding school system; 2) implementation of the “two exempts and one subsidy” system to assist schoolchildren of rural families with economic difficulties in the western region; 3) long-term modernization of the rural primary and secondary schools; 4) greatly strengthening the teaching team in the rural areas of the western region; 5) deepening the reform in teaching and learning, and enhancing quality of education; 6) expanding and strengthening direct assistance in education; 7) clear demarcation of the responsibilities of various levels of government in implementing this plan.
8. That also include labour retraining and loans. Poverty reduction through loans, including microcredits, has in general not met with much success.
9. Referring to the 31 *sheng* (i.e. provinces of Anhui 安徽, Fujian 福建, Gansu 甘肃, Guangdong 广东, Guizhou 贵州, Hainan 海南, Hebei 河北, Heilongjiang 黑龙江, Henan 河南, Hubei 湖北, Hunan 湖南, Jiangsu 江苏, Jiangxi 江西, Jilin 吉林, Liaoning 辽宁, Qinghai 青海, Shaanxi 陕西, Shandong 山东, Shanxi 山西, Sichuan 四川, Yunnan 云南 and Zhejiang 浙江), *zizhiqu* (i.e. “autonomous regions” – each a first-level administrative subdivision having its own local government, and a minority entity that has a higher population of a particular minority ethnic group – of Guangxi 广西 of the Zhuang, Nei Monggol/Inner Mongolia 内蒙古 of the Mongols, Ningxia 宁夏 of the Hui, Xizang/Tibet 西藏 of the Tibetans and Xinjiang 新疆 of the Uyghurs) and *zhixiashi* (municipalities under the central government – Beijing 北京, Chongqing 重庆, Shanghai 上海 and Tianjin 天津).
10. “Poverty is local and it can only be fought at the local level” (UNCHR, 1999).

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