PEOPLES REPUBLIC OF CHINA:

CASE STUDIES ON POVERTY EXIT

A Case Study from the 2006 Special Evaluation Study on Pathways Out of Poverty and the Effectiveness of Poverty Targeting

December 2006

Qiaolun Ye

Operations Evaluation Department

Asian Development Bank
## Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>IRR</td>
<td>internal rate of return</td>
</tr>
<tr>
<td>Kg</td>
<td>kilogram</td>
</tr>
<tr>
<td>Km</td>
<td>kilometer</td>
</tr>
<tr>
<td>OEM</td>
<td>operations evaluation mission</td>
</tr>
<tr>
<td>O&amp;M</td>
<td>operation and maintenance</td>
</tr>
<tr>
<td>PFI</td>
<td>participating financial institution</td>
</tr>
<tr>
<td>PRC</td>
<td>People’s Republic of China</td>
</tr>
<tr>
<td>RCC</td>
<td>rural credit cooperative</td>
</tr>
<tr>
<td>SES</td>
<td>special evaluation study</td>
</tr>
</tbody>
</table>

## Note

In this report, “$” refers to US dollars.
## Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Introduction</td>
<td>1</td>
</tr>
<tr>
<td>II. Results of Poverty Exit</td>
<td>2</td>
</tr>
<tr>
<td>III. Poverty Exit Strategies</td>
<td>4</td>
</tr>
<tr>
<td>IV. Household Resources</td>
<td>8</td>
</tr>
<tr>
<td>V. Context and Conditions</td>
<td>10</td>
</tr>
<tr>
<td>VI. Issues, Underlying Causes, and Alternatives</td>
<td>13</td>
</tr>
</tbody>
</table>
I. Introduction

1. Selection of the Projects for Case Studies

1. Two projects in People’s Republic of China (PRC) were included in the study: (i) the Chengdu–Nanchong Expressway Project, financed by Loan 1638-PRC for $250 million and approved in 1998, and (ii) the Southern Yunnan Road Development Project, financed by Loan 1691-PRC for $250 million and approved in 1999. Both projects had been completed. The former was located in Sichuan Province and rated highly successful by the project completion report prepared by the Asian Development Bank (ADB). The latter was located in Yunnan Province and rated successful by the project completion report prepared by ADB.

2. Fieldwork of the Operations Evaluation Mission

2. An operations evaluation mission (OEM) \(^1\) visited areas under these two projects from 20 July to 16 August 2005. In Sichuan Province, the OEM visited the 208 kilometer (km) project expressway as well as two of the five local roads upgraded under that project (supposedly to be financed by the ADB loan, see para. 64). For comparison, the OEM also visited local roads in two counties upgraded without assistance from the project, as well as National Highway G318, which was replaced by the project expressway. In project and non-project areas, the OEM conducted in-depth interviews with 42 rural households in eight villages that belonged to seven townships in six counties. In addition, the OEM briefly interviewed 14 shop owners in small towns and held lengthy discussions with four owners and/or managers from three private companies that invested in the project areas. In addition to meetings with the Sichuan Provincial Communication Bureau (the Executing Agency of the project) and the Chengdu–Nanchong Expressway Corporation, the OEM held discussions with county transportation bureaus, poverty reduction and development offices, business bureaus, and township and village leaders.

3. In Yunnan Province, the OEM visited the 147 km project expressway and National Highway G213, which it replaced. In addition, the OEM visited many local roads, including those connecting two counties and those running from countries to townships, from townships to administrative villages, and from administrative villages to sub-villages, or so-called “natural villages” under administrative villages. These roads were all developed without ADB financing, though some were included in the ADB project as add-on components. In project and non-project areas, the OEM conducted in-depth interviews with 51 rural households in eight villages that belonged to eight townships in five counties. In addition, the OEM briefly interviewed six migrants who had migrated from poor villages and were working in shops and restaurants in Simao City, which is located near an exit of the project expressway. In addition to meetings with the Yunnan Provincial Communication Bureau and the Yuangjiang–Mohei Expressway Corporation, the OEM held intensive discussions on rural poverty issues with various government agencies including the Provincial Poverty Alleviation and Development Office, Provincial Education Bureau, Provincial Health Bureau, Provincial Treasury Bureau, Labor and Social Protection Bureau, and Provincial Civil Affairs Bureau, which is in charge of welfare programs for the most needy in rural areas. In the five counties visited, the OEM held in-depth discussions with county heads and poverty reduction officials, as well as with village and township leaders and field staff who worked directly with farmers. Finally, the OEM interviewed

\(^1\) The OEM comprised a senior evaluation specialist from ADB as mission leader, one international consultant, and two interpreters. In addition, one local consultant participated for 15 days of the fieldwork.
11 managers or staff members of agricultural companies in project and non-project areas whose investments included tobacco, tea, sugarcane, coffee, and rubber.

4. Altogether, the OEM visited 16 villages and conducted 204 interviews during its fieldwork in the PRC, including (i) in-depth interviews with 93 rural households, (ii) individual discussions with 76 government officials (13 from provincial agencies, 30 from municipalities and counties, and 33 from townships and villages), (iii) individual discussions with 15 managers or staff members from commercial companies or financial institutions, and (iv) brief discussions with 14 shop owners and six migrants working in shops and restaurants. To understand the role of ADB projects in households’ rise out of poverty, the OEM visited areas both close to and far from expressways and local roads. The table below provides a list of areas visited.

### Project Areas Visited

<table>
<thead>
<tr>
<th>Municipality</th>
<th>District/County</th>
<th>Township</th>
<th>Village</th>
<th>Sub-village</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A. Sichuan Province</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Suining</td>
<td>Daying</td>
<td>Yufeng</td>
<td>Yuyin</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Shehong</td>
<td>Dayu</td>
<td>Wujiangqiao</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Pengxi</td>
<td>Mingfeng</td>
<td>Kuantai</td>
<td></td>
</tr>
<tr>
<td>Nanchong</td>
<td>Gaoping</td>
<td>Yong’an</td>
<td>Qianjin</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Nanbu</td>
<td>Shuangfeng</td>
<td>Caojiawo</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Jialing</td>
<td>Datong</td>
<td>Longtai</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Sufenba</td>
<td></td>
</tr>
<tr>
<td><strong>B. Yunnan Province</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yuxi</td>
<td>Yuanjiang</td>
<td>Mili</td>
<td>Mengpeng</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Wazhi</td>
<td>Nibai</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Lali</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Lushui</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Hapulu First</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Halou</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Duolongyi</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Kala</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Lushui</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Damiduo</td>
<td></td>
</tr>
<tr>
<td>Simao</td>
<td>Pu’er</td>
<td>Dehua</td>
<td>Pojiao</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cuyun</td>
<td>Yixiang</td>
<td>Yingpanshan</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Menglian</td>
<td>Mangxin</td>
<td>Bangshun</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Wotuo</td>
<td></td>
</tr>
</tbody>
</table>

Source: Operations Evaluation Mission.

## II. Results of Poverty Exit

### 1. Poverty Reduced

5. Poverty was reduced substantially in the areas visited. In Sichuan, poverty was estimated by some interviewees at less than 3% in the better-off areas and less than 10–20% in the poorer villages. The definition of the poor that they used was people with enough to eat but no cash in hand. The poorest households could not afford electricity and used oil lumps even
when electricity was available in their villages. Poverty incidence seemed to be higher in the villages visited in Yunnan, which was dominated by mountainous regions with 25 ethnic minorities. While hunger poverty was not observed, the OEM visited hardcore poor who lived on less than CNY668 per capita per year,\(^2\) and other poor who lived on less than CNY924 per year. In addition, there were many low-income or near-poor households in the poor regions visited in Yunnan who relied mainly on grain production without cash crops or off-farm incomes. These people reportedly could not afford to pay medical bills and had little capacity to cope with shocks, and so were at high risk of returning to poverty.

6. Non-income dimensions of poverty were also observed, including a shortage of drinking water, poor housing conditions, long distances to travel to primary schools and clinics, lack of all-season roads, and isolation from the dynamic growth of the outside world. Even where government clinics were available in all townships and counties, many poor households interviewed said that they could not afford the fees and used private village doctors who charged less.

2. Causes of Remaining Poverty

7. Rural poverty had various causes. Some of the hardcore poor interviewed lacked capacity to help themselves, such as the disabled, the aged in their 70s–80s, people lacking family labor, or households with at least one chronically or seriously sick member. For the poor able to work, the causes of poverty seemed to include the following: (i) a severe shortage of land, where farmland per capita was inadequate or merely sufficient for self-consumption, with little surplus for selling; (ii) a poor external environment in remote mountainous regions with small local markets and expensive access to outside markets; and (iii) low human capital due to limited education, difficulty in speaking Mandarin Chinese, lack of aggression or ease of contentment, or lack of courage to face exposure to the outside world. This last cause seemed to be common among the poor minority households visited in Yunnan.

3. Sustainability of Poverty Exit

8. While the majority of the rural households had risen from poverty in the areas visited, risks remained that may threaten the sustainability of that exit. The following risk factors seemed to be most relevant:

(i) First was serious sickness of family members, which led to high bills for medical services and related expenses, such as the cost of family members’ staying in the hospital to take care of the sick and, in some cases, the loss of family labor. While only a few interviewees actually suffered from serious sickness, it was one of the most common concerns of many.

(ii) Second was natural disasters such as droughts, floods, and epidemic outbreaks of animal or crop disease. Unlike in other parts of the PRC, this risk was relatively low in the areas visited in Sichuan and Yunnan, which are particularly suitable for agricultural production, with a mild climate and relatively good soil.

(iii) Last was the employment prospects of the rising generation. Even in areas currently with sufficient farmland per capita, if most of the young remained in the village and relied on agriculture, the labor-to-land ratio would deteriorate, and the shortage of farmland for the new labor might eventually lead to cultivating steep slopes and therefore threatening the sustainability of natural resources. This last risk was less a concern in the areas visited in Sichuan, where most of the young

\(^2\) After the OEM fieldwork, the official poverty line for hardcore poor was raised in 2006 to CNY683.
People's Republic of China: Case Studies on Poverty Exit

III. Poverty Exit Strategies

9. Farmers in the areas visited adopted various strategies to escape poverty. These varied among households and across regions, as discussed below.

1. Migration

10. In the villages visited in Sichuan, migration was the primary strategy to escape poverty used by the great majority of households in the past 10–15 years. In many villages, almost all families had at least one young member who had migrated. Most of the migrants went to coastal provinces, while the remaining worked in inland provinces or autonomous regions such as Xinjiang, Qinghai, and Guizhou. Almost all migrants worked in non-agriculture sectors such as manufacturing, construction, and services. Due to a long history of migration in Sichuan, most rural households had contacts in other provinces such as relatives, friends, or other fellow-villagers, who provided information about job opportunities for those still in the villages. Most migrants sent back remittances two or three times a year, averaging CNY1,000 per year in the cases studied, and brought additional cash with them when they visited home during holidays. They helped with additional cash when their families faced emergencies, especially the sickness of a family member. In Sichuan, the OEM interviewed some migrants who had returned to their hometowns and invested in agriculture or rural industries and/or services, using savings from wages accumulated when they worked as migrants.

11. The situation was rather different in areas visited in Yunnan, where migration was less common for several reasons. These included (i) limited education, with school dropout rates high among the minorities even in elementary schools; (ii) language barriers, as many minority people could not speak fluent Mandarin; (iii) lack of social connections in cities because very few people had migrated in the past; and (iv) a culture of being reluctant to go far from home and being less aggressive and easily contented. These factors combined to make young people reluctant to migrate, leaving households with few alternative strategies to rise from poverty. Nevertheless, seasonal migration within the county or in neighboring counties was observed, mostly during winter when there was no farm work.

12. The OEM observed the following positive impacts of migration:

(i) It enabled a rise from poverty for the migrants themselves, who had been surplus labor in their villages before migrating.

(ii) It reduced the financial burden on the migrants’ parents. Many parents interviewed said that at least they did not need to support their children after they migrated.

(iii) It reduced population pressure in villages.

(iv) Remittances from migrants became a main source of cash income for families that remained in the villages and were crucial to cover education fees, the construction of new houses, weddings and funerals, medical services, and
medicines, especially for households that relied on subsistence farming with little cash.

(v) Remittances increased the cash available in villages, enabling informal lending among villagers, as poor people were able to borrow more easily when periodic remittances increased their repayment capacity.

(vi) Savings from wage earning enabled some migrants to return home and start a new business, which generated employment for themselves and for others (para. 10).

2. Government Organized Migration and Resettlement

13. Cases were observed in the PRC in which government interventions aim to facilitate the migration of rural labor out of surplus areas. In a migration program in Menglian County, Yunnan, the county government had agreements with local governments in Shanghai and Guangdong Province to help its migrants to those destinations. Under that program, the Menglian government helped migrants by subsidizing transportation, while the Shanghai and Guangdong governments helped migrants make contact with potential employers. At the end, participating companies offered the first job for migrants, who received low wages as interns for their first year but gained experience. In Sichuan, some local governments offered training courses for potential migrants. In one village visited with 120 households, the county government provided training to 10 villagers willing to migrate to other provinces. With a view to providing new skills to facilitate job hunting, each month-long training course focused on a particular set of skills, such as electronics or wine making. Nine of the 10 participants migrated in 2004 or early 2005 and reportedly found jobs related to the training they received, and the last participant stayed in the county and got a job in a winery.

14. Though well intentioned, these government interventions were not free of problems. First, the interventions were costly for both participants and governments. In one village, the OEM was told that 15 people had applied for a migration program but eventually only one participated, because the other 14 could not afford the CNY480 fee required even after being partly subsidized by the county government. Second, some participants not seriously interested in migration were attracted to the program because it provided a free medical check up. These people returned home shortly after migrating. Third, some participants were interested in migrating but preferred destinations other than the ones arranged by the programs. The OEM interviewed a female participant who left her factory in Shenzhen, where she worked as a program participant, after only 6 months. After returning to her village, she planned to migrate again but at her own expense and to her choice of destination. Many other participants left the Guangdong factory jobs to which they were assigned under the program and later moved to Shanghai instead of returning to their villages. In spite of these problems, the migration programs seemed to have achieved the objective of facilitating surplus labor migration from poor regions, although not to the cities intended.

15. The OEM also observed resettlement programs organized by governments, frequently for an entire village that was displaced by government infrastructure projects. In Yunnan, a program organized by local governments imported settlers from a mountainous region with a harsh climate to areas with good farming conditions and a labor shortage. Under that program, land was given on concessionary terms to a private company for tea production, which hired the settlers who participated in the program. The program provided settlers with construction materials for building new houses as well as stipends to cover basic living expenses during the first few months, at a cost of about CNY10,000 per settler. The tea company provided each participant with an area of tea to manage and harvest, paying them CNY2 per kilogram (kg) of
tea surrendered. Most settlers ended up better off than they had been in their home villages. Later, other households migrated to the tea areas without government help, sometimes with help from earlier migrants. The OEM was told that about 20% of the government-sponsored settlers returned home after a while for various reasons, while all those who had migrated at their own expense remained.

16. In Menglian County, Yunnan, a coffee company supported by local governments hired migrants from poor regions as farm laborers, who were organized by the company into various specialized production teams, each with about 100 migrants. The company provided the new workers with construction materials to build houses, a stipend to cover living costs for the first 3 months, and a small parcel of land to grow grain for home consumption. In addition, each household received 5 mu (one-third of a hectare) of land for coffee production. The program reportedly worked well, and the migrants interviewed were better off than they had been. While government-organized migration and resettlement helped the settlers rise out of poverty, the programs’ cost per participant was high, and the number of households rising out of poverty was relatively small.

17. In the areas visited, agriculture provided an avenue out of poverty in the early stages when farmland per capita was sufficient. The household responsibility system, adopted in the late 1970s, distributed land-use rights to individual households and provided strong incentives for farmers to increase production. Nationwide, total agricultural net value increased by 55% from 1978 to 1985, and agricultural productivity increased by 40%.\(^3\) Substantially increased agricultural production resulted in the first large-scale poverty reduction in the PRC in the early 1980s. Many interviewees said that they rose from poverty during that period.

18. Higher grain production in the mid-1980s allowed the Government to relax controls on grain production and marketing. As it did so, while increasing farmgate prices, many farmers diversified away from grain production to cash crops, which brought better market prices. Agricultural diversification was therefore adopted as another avenue out of poverty.

19. As the production of cash crops, fruit, fish, and animal products burgeoned, their market prices have dropped significantly in many places in the PRC, especially since 2000. Typically, the first batch of farmers who adopted a new crop earned a sizable profit. Many of the latecomers, however, did not enjoy the same fortune. In particular, many of those who followed the new practice at a very late stage, when prices had fallen sharply, suffered significant losses.

20. Agricultural intensification and diversification continued in the 1980s and 1990s. In particular, hybrids of rice, maize, and potato substantially increased crop yields. However, input costs also increased as the use of purchased inputs such as fertilizer and other chemicals intensified and their prices rose. Further intensification of agricultural production over already high yields proved expansive. In spite of higher crop yields, agricultural intensification was not an effective strategy for poverty reduction in the later stage due to the high cost of inputs. Few farmers interviewed managed to rise from poverty through intensified agriculture at this stage.

---

4. Contract Farming

21. A more recent change in cropping patterns has occurred in Yunnan since the late 1990s and early 2000s, as contract farming with private or government-owned commercial firms played a lead role in introducing new crops and reorganizing the value chain from production to processing and marketing. Commercial firms signed contracts with individual small farmers, provided them with technical assistance and farm inputs, and purchased their production. This model became quite common in several counties visited in Yunnan for producing tobacco, tea, coffee, and sugarcane.

22. For tobacco production, the processing firm Yuxi Hongta Tobacco Group Limited, which is part of the larger Hongta Group conglomerate, decided to expand tobacco cultivation to mountainous regions in southern Yunnan Province, the biggest tobacco-producing province in the PRC. Until the early 2000s, tobacco was concentrated in the center of the province, close to the main processing facilities in Yuxi County. Partly as a result of expressway construction, which sharply reduced transportation time and cost for farmers selling fresh produce in Kunming, many tobacco producers decided to shift to growing flowers, which have much higher value. In addition, the tobacco company found that climate and soil conditions in the mountain regions in southern Yunnan were exceptionally good for tobacco.

23. The OEM visited commercial tea-producing companies in two counties. In Menglian County, a private company had contracts with individual households that had their own small tea plantations. The company provided farmers with technical assistance and farm inputs, purchased their production, and deducted the input costs from the crop payment after the harvest. In Cuiyun District, a commercial company obtained long-term concessions from the local government to invest in new tea plantations on public lands. It signed contracts with rural households for them to manage a small area of tea, about 2.5 mu per laborer, who received a management fee of CNY30 per mu per month during the first 2 years, when there was no harvest, and thereafter CNY1–CNY2 per kilogram of tea leaves harvested.

24. Sugarcane cultivation observed in a village in Menglian was somewhat different. A private processing firm was the main buyer for small farmers, and two private intermediaries, called “bosses,” became the major actors organizing small producers. The private firm signed a single contract with each boss, who then obtained loans to provide farmers with inputs, purchased sugarcane from them, and sent it to the firm’s processing facilities. Once the firm received the sugarcane, it paid the bosses, who then paid individual farmers. Many farmers relied on their bosses for other credit needs as well, including loans for emergencies.

25. In the cases above, commercial firms and private bosses played a key role in agricultural diversification and poverty exit. Compared with small individual farmers, commercial firms had better access to financial resources and agricultural technology and stronger capacity to operate in the changing commodity markets. In some cases, the OEM observed that prices paid to farmers for their crops were very low, in particular for tea, and the implied interest for the loans to farmers was too high in the case of sugarcane. The situation observed by the OEM is similar to what critics of contract farming have reported in several other studies. However, the OEM noted that almost all interviewees said that they were better off now than they had been before becoming contract farmers. Furthermore, the experience of contract farming in other countries shows that low prices paid to farmers was a common problem at the beginning of contract...
farming, because commercial firms tend to enjoy monopolies that leave farmers little negotiating power. However, experience also shows that high profits tend to attract more commercial firms, giving farmers more options and enhancing their capacity to negotiate better prices for their crops. As time passes, farmers may gain negotiating experience and form organizations for collective bargaining, which may help them get better prices.

5. Off-farm Employment in Rural Areas

Off-farm employment was rather limited in many poor villages visited. In Sichuan, township and village enterprises played a primary role in absorbing surplus rural labor in the 1980s and 1990s. This has largely ceased at the current stage, as these enterprises became uncompetitive with large manufacturing enterprises after the economic reforms improved efficiency in urban areas. In the areas visited in Sichuan, the local industries employed only a small number of nearby farmers. Many interviewees said that wages offered by the local industries were much lower than what migrants could earn in coastal provinces. Only in villages adjacent to cities did the OEM observe farm households engaged in services. In contrast, small towns and cities visited in Yunnan absorbed a relatively large number of migrants from villages within the same province, especially in the service sector. One factor underlying this observation was a culture in Yunnan in which farmers were reluctant to go far from home. Because of insufficient social connection in cities, rural households in Yunnan had fewer migration opportunities than their peers in Sichuan.

IV. Household Resources

Household resources include physical, financial, natural, human, and social capital. In the areas visited, the following household resources had the largest impacts on poverty reduction.

Farmland. While the quantity and quality of farmland per household was homogeneous within the same village, great variation was found across regions, depending on population density and land quality. In Sichuan, population density was high, so each household received only tiny plots of between 2 and 5 mu, or 1,300–3,300 square meters—barely sufficient for subsistence, with little or no surplus for marketing. Thus, if the rising generation stayed in the village, they would not find it possible to live by agriculture, as their parents would not be able to give them land without compromising their own welfare. In most cases, young people had no choice but to migrate in search for jobs. This is an important reason why migration to coastal provinces started as early as in the late 1980s in the villages visited in Sichuan.

In contrast, Yunnan had a much lower population density, with more land available per household. In the villages visited, each household had between 20 and 30 mu, and even 50–60 mu per household in some areas, where farmers were allowed to open new land on their own. In addition, the soil quality was good in Yunnan, and the altitude of 1,000–1,500 meters was ideal for such cash crops as tobacco, tea, sugarcane, and coffee. This made possible introducing cash crops, which became the main avenue out of poverty among households in the villages visited.

Physical Assets. All households interviewed had houses, though the quality varied significantly, reflecting living standards. In the villages visited in Sichuan, building or improving houses seemed to be the highest household investment priority, using remittances sent by
migrants. In most villages visited in Sichuan, most of the houses in the villages had been improved in the last few years, as almost all households had at least one migrant. It seems that the quality of houses was more the result of poverty alleviation than a cause. In villages visited in Yunnan, the quality of houses was substantially lower, reflecting lower living standards, the absence of remittances, and lower capacity to save.

31. **Equipment.** In Sichuan, agriculture was mainly for subsistence, so households made almost no investment in equipment. Many families had motorcycles, which were used for family transportation rather than income generation. As with houses, the availability of equipment was more the result of poverty reduction than a factor affecting it or the avenue chosen out of poverty. In the tobacco villages visited in Yunnan, the most important household investment was a small device used to measure the temperature and humidity in the tobacco-drying room.

32. **Savings and Other Financial Assets.** Most rural households interviewed in Sichuan had savings accounts in rural credit cooperatives (RCCs). Most of the savings came from remittances from migrants and served mainly for school fees for children or to deal with emergencies, especially for paying for medical services and medicines. The OEM found only a very few cases of savings being used for investment in agricultural production.

33. In contrast, most households in the villages visited in Yunnan did not have savings accounts in RCCs. Some households had borrowed from RCCs in the past without repaying in full, so they were afraid to open savings accounts because the RCC might seize their savings. In these villages, pigs or other animals were the more common form of savings. In Yunnan, household savings came from selling such cash crops as tobacco, tea, and sugarcane, instead of from remittances. They were used mainly for improving houses, building drying rooms for tobacco, and paying medical bills. Household savings were rarely used for purchasing inputs, which were provided by the private companies or bosses, who deducted their cost from payments made to farmers for their crops.

34. **Human Capital.** The OEM observed substantial disparities in schooling in the villages visited in Sichuan and Yunnan, which related to topography (lowlands versus mountainous areas) and ethnicity. In Sichuan, the villages visited were in lowlands with good roads linked to townships and county cities. Most households valued education and invested in their children’s education. Most adults, both men and women, had completed primary school, and many were secondary school graduates. A few households even had children attending university in Chengdu, the provincial capital.

35. In contrast, the villages visited in Yunnan were located in mountainous areas, and many of them had poor communications and roads, and so difficult access to townships and larger cities. Ethnic minority groups were dominant, and most households did not value education. While most adults had a few years of primary schooling, many had not finished the 6 years of primary education, and some adults, especially women, were illiterate. In most villages visited, the ethnic minority people could not speak Mandarin, though in villages with two or more minorities, Mandarin was used as the common language.

36. Finally, personal characteristics affected the selection of poverty exit strategies and their success. While almost all households visited were hardworking, other personal characteristics were important in determining capacities to migrate and find off-farm employment.

37. **Social Capital.** For migration and off-farm jobs, social networks and connections in the outside world—relatives, friends, or other fellow-villagers in cities or other provinces—seemed
to be most critical. In the villages visited in Sichuan, migration to coastal provinces started in the late 1980s or early 1990s, so most households had relatives who had migrated and worked in industries or construction there. Migration therefore became an easy decision, as social connections helped new migrants with information about job opportunities and provided them with accommodation for the initial days after their arrival at cities. The social connections substantially reduced the risk and cost of migration.

38. In the absence of social connections, as was observed in the villages visited in Yunnan, the risks felt by potential migrants (most of whom had no experience of living and working in the outside world) and the actual costs of migration were high, because migrants had to pay for a place to stay and look for a job by themselves. County governments in Yunnan tried to solve this problem by collaborating with local governments in Shanghai and Guangdong. These efforts consisted of training potential migrants, subsidies to cover transportation costs, and assistance in finding jobs through contacts established between the Shanghai and Guangdong governments and companies located there. The results of their efforts, however, were mixed (paras. 13–14).

V. Context and Conditions

39. The conditions faced by the poor played a key role in determining the options available to them for escaping poverty and influenced their selection of strategies.

40. **History and Culture.** The OEM found that history and culture varied significantly across regions and influenced poverty exit strategies. Villages visited in Sichuan had a history of migration since the late 1980s because population density was high and households had insufficient land. In contrast, most villages in Yunnan were located in mountainous areas without a tradition of migration, and most interviewees considered migration highly risky. In addition, villages in Yunnan were dominated by ethnic minorities mostly unable to speak fluent Mandarin. This language barrier added further difficulty to migration, and the few people who migrated had gone to small towns within the same county where they had no language problem.

41. **Gender.** Men and women in the villages visited in Sichuan appeared to play an equal role in family decisions. In most cases, the OEM found couples that had migrated together. Occasionally, the OEM observed families in which the woman migrated and the man stayed at home to farm and take care of the rest of the family. In many of the interviews in these areas, women were as active, or more so, in answering questions than men, reflecting their knowledge about household decisions. In contrast, men usually dominated the conversation in the minority-dominated villages in Yunnan. This seemed at least partly because of the language barrier, as women in these villages tended to be less educated than men and less able to understand Mandarin.

42. **Policies and Politics.** Government policies strongly influenced the choices available to rural households in the selection of poverty-exit strategies, as well as their success or failure. The OEM identified a number of important policy reforms in the PRC that have brought large-scale poverty reduction in the PRC (paras. 69–71).

43. **Macroeconomic Growth.** The PRC experienced rapid economic growth in the past 2–3 decades, especially in the coastal provinces particularly attractive to private investors, both domestic and foreign. The rapid growth of the national economy played a critical role in reducing
rural poverty by creating many jobs for young migrants from rural areas. This was particularly relevant for the households visited in Sichuan, as almost all of them had at least one member who had migrated to a city or another province. In contrast, national economic growth did not seem to have a significant impact on poverty reduction in the mountainous villages visited in Yunnan, where few people migrated to urban centers.

44. **Local Economic Growth.** In Sichuan, economic growth in county cities or townships provided employment for some households living nearby. However, the impact of local growth on poverty reduction seemed to be limited. In these areas, most interviewees stressed that the wages offered by local factories were very low, about half of what was paid for similar work in coastal provinces. Since most households had the option of migration, employment in local industries was not particularly attractive. This was not the case in Yunnan, however, where many interviewees preferred to work in industry or services in small towns close to home. The OEM interviewed some young women who had migrated from villages to county cities or townships and worked in restaurants or shops. They seemed to be satisfied with their off-farm jobs. In addition, the OEM interviewed a few males who migrated seasonally within the same county to work in agriculture, for example digging holes to plant rubber. The wages they earned were low but still better than subsistent farming at home.

45. **Geographic Location and Topography.** The geographic location and topography of villages seemed to be important factors determining the choices available to rural households for escaping poverty. In the lowlands visited in Sichuan, households adopted poverty exit strategies based on intensifying and diversifying agriculture between the late 1970s and the mid-1980s. After that, migration to urban areas or other provinces became the main household strategy to escape from poverty. In contrast to the cases observed in Viet Nam, trade and other off-farm activities in rural areas were not important poverty exit strategies in the areas visited in Sichuan, in spite of very high population densities. Some households did invest in small shops or restaurants in small towns near their villages, but they did so after they had risen from poverty, mostly with savings accumulated when they worked as migrants outside of agriculture. After years of migration, they returned home for personal reasons, such as the need to take care of aged parents, and used savings to start their own businesses in their hometowns.

46. In contrast, the villages visited in Yunnan were located in mountainous areas with relatively abundant land and a climate suitable for a number of cash crops, such as tobacco, tea, sugarcane, and coffee. Population density was relatively low in these areas, which had poor roads, difficult communications, and minority residents with little education. These factors discouraged private investment in manufacturing and enhanced the comparative advantage of commercial agriculture over manufacturing. The OEM noted that county governments in Yunnan focused on attracting private firms to invest in commercial agriculture in their counties and developed measures to facilitate contract farming. This influenced farmers’ selection of agricultural diversification as their main poverty exit strategy.

47. **Infrastructure.** Despite the belief that infrastructure investment automatically has a direct and significant impact on poverty reduction, the OEM found that the real impact of infrastructure investment on poverty reduction varied across regions depending on local conditions in the particular area. In the villages visited in Sichuan, the OEM found a weak relationship between investment in an expressway or local roads and rural households’ rise
from poverty. In these villages, most households escaped from poverty through the migration of younger members to cities or other provinces. Their ability to migrate was due to (i) the many jobs created by rapid economic growth in the PRC in the past 2–3 decades, (ii) an integrated labor market nationwide, and (iii) easy access to information about job opportunities arising from the long history of migration in rural Sichuan, where almost all villages had people working as migrants outside their province. The OEM noted that the lack of good infrastructure in the poor regions did not stop people migrating out of their villages, as long as jobs were available in the outside world where they had social connections. Despite the view that expressways enable or facilitate migration, interviewees said that they never used expressways; most migrants traveled by train, which was cheaper. Indirectly, however, expressways had a significant impact on poverty reduction because of their great contribution to overall economic growth in the PRC.

48. Similarly, the real impact of rural infrastructure investment on poverty exit varied across regions depending on local conditions. The OEM observed in some regions only marginal impact on poverty reduction arising from investment in rural infrastructure, including roads and small irrigation systems. Most households rose from poverty through migration, and the infrastructure investment brought them only small benefits. In Yunnan, however, the OEM observed significant impacts from rural roads and irrigation systems. These areas had high potential for developing commercial crops, especially tobacco, tea, and sugarcane. In some villages visited, most households rose from poverty by growing these crops, which were promoted by commercial firms that signed contracts with farmers and purchased their production. In these areas, good roads were critical to attracting commercial firms to engage in contract farming. The OEM interviewed technicians from a tobacco company, who stressed the availability of all-season roads as critical to their selecting a particular village for contract farming tobacco. Without good roads, they observed, transporting tobacco leaves might be delayed by days during the rainy season, causing heavy losses to the company. In the sugarcane farming discussed in para. 24, the private boss financed the construction of a dirt road connecting the sugarcane fields to the village and the township road, charging farmers for construction by deducting an annual fee from his payments to farmers for their crops.

49. **Access to Education.** In the areas visited, education was available to all rural households. The cost of education and the location of schools, however, restricted poor children's access to education in some cases, especially to secondary schools, which were usually far from remote villages with low population densities and so entailed costly school boarding. Although students in the 9 years of compulsory education did not pay school fees, other school-related costs, including books, supplementary fees, and boarding expenses, placed a heavy burden on rural households. Recognizing these problems, a new policy of the central Government now exempts rural households in poor regions from paying book fees and supplementary fees and subsidizes boarding costs. It was too early to assess the impact of this new policy, which was just being implemented at the time of the OEM visit. In some villages in Yunnan, the OEM found dropout rates high even among primary school students, largely because of the low value placed on education, language barriers, and costs.

50. **Access to Health Services.** While government hospitals, village clinics, and private doctors were readily available in all villages visited in Sichuan and Yunnan, the high costs of medicine and medical services were primary concerns named by most interviewees, including both poor and non-poor households, as the latter could easily become poor from misfortunes such as a serious illness affecting family members. In one township hospital visited, the OEM noted that public investment in upgrading office buildings and equipment had only a marginal impact. Due to the high costs of the medical services, that hospital had few visitors even after the upgrade. Many interviewees said that they used simple medical services provided by private
doctors in their villages instead of government hospitals, because village doctors charged much less. This issue has been brought to the attention of the central Government, which initiated new programs to mitigate this key concern of most rural households (para. 71, [ii–[iii]]).

51. **Access to Financial Services.** Farmers’ difficult access to formal financial services was a frequently raised concern in the PRC and other countries. The OEM found, however, that the real situation varied significantly across regions. In the villages visited in Sichuan, most rural households had savings accounts in RCCs and received loans from them for various purposes, such as renovating houses, dealing with health problems, paying for children’s education, and purchasing inputs or equipment. Borrowing for agricultural activities was the least common situation, probably due to the small size of family farms and the largely subsistence nature of farming, especially in Sichuan. The requirements for obtaining loans from RCCs varied among regions. In Sichuan, the OEM visited one branch of an RCC that had provided loans of up to CNY100,000 for business or housing investments. These loans required collateral, preferably real estate in towns, valued higher than the loan. Loans of less than CNY20,000 were provided without collateral. About 70% of the loans were for less than 1 year, usually only a few months. The annual interest rate was 6%, paid quarterly. Default rates were low. Most rural households also borrowed from relatives and friends, especially for dealing with health problems and paying for their children’s education. The poorest households had little repayment capacity and difficulty gaining access credit, either formal or informal.

52. In the villages visited in Yunnan, most rural households had access to formal credit. However, some interviewees could not borrow from RCCs because they had not repaid their previous RCC loans. In these areas, the main source of rural credit was the commercial companies and private bosses that contracted farmers to cultivate the cash crops tobacco, tea, sugarcane, and coffee. The bosses provided inputs to farmers and deducted repayment from revenues payable to the farmers after the harvest. They also provided credit for other purposes, such as medical bills, house renovation, and motorcycle purchases, with implicit interest charges paid by deducting them from harvest payments.

VI. Issues, Underlying Causes, and Alternatives

1. **Expressways and Poverty Reduction**

53. Not all expressway projects have a direct impact on poverty reduction even when they are located in poor regions, because expressways are closed to local traffic except near exits. The OEM observed poor villages that remained poor even when they are located next to an expressway. They did not benefit directly from the expressway except from the resettlement program, which compensated their losses caused by expressway construction. In Sichuan, the project expressway had little direct impact on poverty reduction in the project areas, where most poor rise from poverty by migration and employment outside poor regions.

54. In minority-dominated Yunnan, migration was less common due partly to the language barrier and a culture of reluctance to go far from home. In the areas visited, many poor rise from poverty by engaging in commercial agriculture. In these areas, the project expressway had a direct impact on poverty reduction, as it facilitated moving some cash crops from non-poor areas to poor ones. A typical case was tobacco production, which had traditionally been located
in central Yunnan, near the tobacco company in Yuxi City and in areas with good infrastructure. After the construction of expressways, including the project expressway, some of the old tobacco areas shifted to growing flowers, which had higher value, because the expressways enabled quick transportation of fresh flowers from farms to large cities. Consequently, the tobacco company in Yuxi shifted its investment focus to southern Yunnan, including some poor regions previously dominated by grain production. Some of the new areas rose from poverty after a few years of growing tobacco. Factors underlying the shift also included the high potential for commercial agriculture in southern Yunnan because of relatively abundant land, good soil, and a climate ideal for a number of cash crops.

55. Indirect impacts of expressways on poverty reduction, however, were significant, as observed by the OEM in all areas visited. In Sichuan, most of the households interviewed rose from poverty through the migration of some family members to non-poor regions and work outside agriculture. The migrants escaped poverty and sent home remittances to support their families. Migration became a major household strategy to escape poverty due primarily to two factors. First, many jobs became available following continued economic growth in the PRC in the past 2–3 decades, including formal employment such as in factories and informal jobs in construction and services. Second, the labor market in the PRC has become increasingly integrated as large-scale labor migration became prevalent in the past 1–2 decades. As a major portion of the national trunk highway system, the project expressways in Sichuan and Yunnan contributed to national economic growth and job creation in the PRC. Through labor migration, the benefits of national economic growth spread over the country as surplus labor from poor regions found employment in other regions with dynamic growth.

56. These findings suggest that evaluating the social and economic benefits of expressway projects, including in particular their poverty impacts, should go beyond the limits of conventional methodology, which narrowly focuses on increases in traffic volumes and reductions in travel time and costs in the project areas. The OEM found that the actual benefits of expressways go well beyond the areas in which they are located. The indirect impacts of expressways, although difficult to quantify, are much larger than such direct benefits as toll collections. That is why governments are willing to invest in expressways even in areas with low traffic, where the financial and economic internal rates of return (IRRs) are low and toll collection is insufficient to recover all costs, including operation and maintenance (O&M), investment, and related financial charges. If an expressway in these areas is a necessary part of the national trunk highway system, its investment is justified by its contribution to the system and macroeconomic growth, not by rising traffic volume in the project areas. A thorough understanding of this may reduce pressure on project staff to over-estimate traffic volume in project areas to produce IRRs acceptable for project approval. ADB post-evaluation studies have frequently found that IRRs estimated for projects were high at appraisal and low at evaluation.

---

4 While construction and services are formal sectors, many migrants worked in them informally without a written contract.

5 ADB measures the benefits of road projects by a set of indicators typically including, among others, changes in (i) traffic volume and toll collection, (ii) passenger fares and freight rates, and (iii) accident and death rates. Estimating these benefits is limited to the areas crossed by project roads.
2. Local Roads and Poverty Reduction

57. A typical justification for public investment in rural roads is the assumption that improved rural roads will reduce shipping times and costs for agricultural goods, improving farmgate prices and thereby reducing rural poverty. In the two projects examined in the PRC, the expected benefits of local roads included (i) improving the flow of goods, services, information, and tourists; (ii) facilitating farmers’ access to markets and reducing transportation costs for products and inputs; (iii) greater economic diversification; and (iv) facilitating labor mobility. Indirect social benefits included increases in primary and secondary school attendance rates and improved access to health facilities and other public services.

58. The OEM found the assumptions above overly simplified and not always valid. In areas visited in Yunnan, the OEM observed that upgrading isolated roads to poor, small villages located in remote and poorly endowed mountainous regions had a marginal impact on poverty reduction. Poor resource endowment and adverse farming conditions meant the poor in remote villages had little surplus to sell and the improved roads, while making walking more convenient, did not mitigate lack of employment, the key cause of poverty, and therefore did not substantially change villagers’ circumstances. A better alternative could have been upgrading roads in other parts of the county that had high potential for commercial agriculture, such as areas adjacent to towns, or large villages in lowlands with sufficient land and favorable conditions, such as sufficient water, even if they are not poor. If the lack of an all-season road was the only constraint to commercial agriculture in non-poor areas, and if half of the farmland in these areas could shift from grain to cash crops after road development, demand for labor would stimulate seasonal migration of the poor from nearby poor villages to work in cash crop production, thus generating employment for surplus labor from poor villages.

59. The OEM found that the real impact of local roads on poverty reduction depends on local realities. In areas with high potential for commercial agriculture, where land is relatively abundant, the climate is particularly suitable for certain cash crops, water is sufficient, and the only key constraint is the lack of all-season roads, upgrading rural roads is worthwhile, as it may contribute significantly to poverty reduction. In Yunnan, the OEM observed a private boss who financed the construction of a dirt road to facilitate transporting sugarcane. While the terms he negotiated with farmers for repaying the road investment over 16 years seemed high to the OEM, interviewed farmers all accepted the terms because the alternative of not having the road would have been worse, as they would have had to rely on growing grain and remained poor.

60. In contrast, isolated roads in remote and poorly endowed areas short of arable land per capita had little real impact on poverty reduction, particularly if the roads did not link to growth centers or road networks. These roads provided small benefits to the residents along the roads, but did not generate conditions sufficient to lift them out of poverty. The remoteness of these areas and their low population densities made commercial firms uninterested in promoting cash crops because scale was insufficient to justify their investment. In these areas, the OEM found few commercial users of the roads upgraded by projects. As no private company invested in these remote areas, poverty reduction would be difficult without creating long-term jobs for surplus labor. As the villages and households remain poor after the project investment, road maintenance is another major concern after project completion, when no more free money comes from external sources. It seems that upgrading roads in these remote and poorly endowed villages should not have been the priority of poverty intervention at the current stage, when public resources are insufficient. The same funds might have brought more poverty reduction if they had been used to mitigate the key causes of poverty in the project areas through job creation.
3. Add-on Components in Expressway Projects

61. Both of the two expressway projects examined by the OEM included a component to upgrade rural roads located in poor regions. Even in the case where improved local roads had a direct impact on poverty reduction, the ADB requirement of including local roads in expressway projects had many negative effects, as observed by the OEM.

62. First, it disrupted the government planning process for local road development in the PRC, where the central and provincial governments are responsible for the construction and O&M of expressways and national highways, while county governments are in charge of local roads, including financing, construction, and O&M, with technical and financial assistance from the central and provincial governments. In the areas visited, all local governments had their own plans—long, medium, and short term—for local road development. Typically, the priorities in local road development plans included (i) linking the county capital to growth centers via expressways or major highways, (ii) using the expressway or highway sections that pass through their county as the spine of a road network in their county, and (iii) upgrading the local road network piece by piece as resources permit. Improving local roads occurred in the following order: (i) county to county, (ii) county to township, (iii) township to village, and (iv) village to sub-village. The local road component in the ADB-financed expressway projects, however, had different priorities. To maximize poverty reduction impacts, consultants from ADB deliberately selected areas with the most poor beneficiaries, including remote sub-villages with low population densities and low economic returns for road development.

63. Second, the ADB requirement caused distortions by changing priorities in local road development. The ADB projects required the completion, within the project implementation period, of both the expressways and the local roads included in the projects. To comply with this requirement, local governments had to adjust their investment plans to make counterpart funds and other resources available for the “ADB roads,” which might not have been high priorities in their original plans. The adjustment was achieved at the cost of delaying investment in other roads that might have been more urgently needed or offered higher social and economic returns, though they might not be located in poor counties with a lot of poor beneficiaries.

64. Third, the ADB requirement resulted in inefficient use of human and organizational resources. Expressway investment and O&M in the PRC were implemented by expressway corporations that had specialized engineers. The ADB requirement made these corporations responsible for investment in local roads included in the projects in addition to expressways. This created inefficient use of human resources as professionals highly specialized in expressways supervised the development of rural roads. In addition, ADB insisted that, in Sichuan, at least 10% of its loan be used to finance local road improvement. The expressway corporation strongly resisted this requirement because it made the company repay the ADB loan without a mechanism for collecting tolls from users of local roads. Pressure from ADB to comply with loan covenants inhibited truth-telling at the grassroots. In fact, no ADB funds were used for local road improvement. Interviews carried out by the OEM with government officials in Sichuan and Yunnan showed that local roads under both projects would have been upgraded with or without the ADB projects, as they had already been included in the local government plans for upgrade before the projects, though with different priorities. The add-on components in ADB projects, at best, accelerated investment in these “ADB roads,” at the cost of distorting the original priorities for road development of the local governments.
In addition to complaints regarding local roads components, the OEM heard others from government officials about unreasonable requests from ADB that expressway projects include activities on AIDS control, women empowerment, or ethnic minority development. These add-on components, while satisfying ADB’s desire to address social issues, had certain negative effects. First, the expressway corporation lacked expertise to properly address these social issues, which were the responsibility of local governments. Second, the add-on components consumed time, money, and attention, and their inclusion in expressway projects distracted the executing agencies’ attention from their primary mandate of constructing high-quality roads at minimal cost. Third, the add-ons brought requirements for monitoring and evaluating the poverty impacts of the expressway project, for which a long-term international consultant and some short-term consultants had to be hired at high cost, primarily to write monitoring reports for ADB. Scarcely foreign currency could have been used to hire short-term experts needed to address critical issues that were beyond the capacity of local experts.

If ADB is serious about getting real results instead of merely demonstrating its concern for rural poverty, stand-alone projects should be designed for rural poverty reduction. They should provide tailor-made solutions to local problems based on a thorough understanding of the key causes of poverty in particular project areas. The pressure for every project to include add-on components to obtain a direct impact on poverty reduction, and the practice of artificially inflating the number of poor beneficiaries in ADB projects to ensure their approval, has achieved more rhetoric than real results.

Instead of expecting every single project to have a direct impact on poverty reduction, it may be better to allow some projects, such as expressway projects, to focus sharply on promoting economic growth, which may significantly reduce poverty, albeit indirectly and unquantifiably. If this suggestion is acceptable, there is no need for such projects to set up a system to monitor and evaluate their direct impacts on poverty. Without pressure for every project to include add-ons or poverty impact monitoring, ADB nonconcessional loans, or ordinary capital resources (OCR), may still be attractive to many borrowing countries, including in particular middle-income countries like the PRC. The OEM found that ADB loans are attractive for their (i) long maturity of 25 years, (ii) relatively low interest rates, and (iii) other benefits associated with ADB’s involvement in project financing, as domestic banks are more willing to finance a project that receives some financing from a reputable agency like ADB.

Consultations with government officials suggest that, without artificial burdens, some borrowers may be interested in taking OCR loans for projects that aim to spur economic growth, even if a small additional charge—say 0.5%—were levied on them. If this idea is acceptable, ADB may charge a small “poverty fee” on OCR loans for projects that aim to spur economic growth but do not include add-ons for poverty reduction or other social issues. Revenues collected from the poverty fee could be used to subsidize stand-alone projects for poverty reduction, such as those that provide low-cost loans for private investment in small-

---

6 In fact, combining project monitoring with evaluation may not be appropriate. Monitoring is an ongoing activity during project implementation and should be conducted by the concerned executing agency based on its operational needs. Evaluation is an activity after project completion, when the executing agency has terminated its operation, and therefore should be conducted at a higher level, by the provincial or central government or ADB, who are more interested in the lessons identified in the evaluation than is the executing agency, unless the latter is assigned to implement another similar project.
scale village infrastructure. Under these projects, participating financial institutions (PFIs) could use their own funds to finance infrastructure loans. Grants from ADB would be needed, however, to (i) provide interest subsidies that encourage private investment in rural infrastructure, (ii) partly cover the lending risks of PFIs in these operations, and (iii) partly compensate PFIs’ administrative costs for this lending. This suggestion needs pilot testing followed by vigorous evaluation of the pilot results before replication. Furthermore, setting the poverty fee rate needs intensive consultation and negotiation between ADB and the government agencies concerned, with the idea that the amount to be levied on OCR loans should not exceed the financial and non-financial costs currently imposed on borrowers by various ADB requirements.

4. Effectiveness of Government Interventions in Poverty Reduction

69. Government interventions to reduce poverty may be classified as (i) policy reforms and (ii) project investment. The OEM observed significant poverty reduction impacts from three policy interventions in the PRC. The first was the household responsibility system adopted in the late 1970s. By distributing land-use rights to individual rural families, this policy gave farmers substantial incentive to produce. In conjunction with progressive liberalization of government controls on agricultural marketing and prices, the policy reforms led to remarkable change in rural PRC. In 6 years, from 1979 to 1985, agricultural net value in the PRC increased by 55%, and agricultural productivity improved by 40%. At little financial cost to the Government, the policy interventions brought the largest poverty reduction in the history of the PRC. Many interviewees said that they escaped poverty during that period.

70. The second policy intervention that significantly reduced poverty was the relaxation of government controls on labor migration since 1989. By allowing self-driven flows of surplus labor from poor regions to those with dynamic economic growth, mostly the coastal provinces, this policy enabled millions of migrants from poor regions to share the benefits of national economic growth. In addition, millions of relatives of the migrants also benefited, even those who remained in poor regions, as the migration reduced population pressure on the limited farmland, and remittances from migrants contributed to improving the living standards of their families. Again, the cost of this policy change to the Government was minimal.

71. The last policy interventions were the recent and ongoing policies that aim to address the so called shan nong issues, which refer to problems and concerns of rural areas, farmers, and agriculture. These new policies include the following:

(i) Elimination of agriculture taxes and other fees levied on farmers by local governments. This policy was announced by the central Government in 2003, to be implemented within 5 years. By late 2005, 27 of 31 provinces in the PRC had abolished agriculture taxes, and the rest, including Yunnan, had substantially lowered taxes and planned to eliminate them in 2006. All farmers interviewed greatly appreciated this new policy because, in the past, some of them had paid CNY150–CNY200 per capita, or CNY800–CNY1,000 ($100–$125) per household annually—a heavy burden on the poor and the near poor. Without targeting and leakage, this policy benefited all who had paid taxes and fees, with those who had suffered the most benefiting the most.

---

(ii) The new rural health cooperative system, which was still in its pilot stage at the time of the OEM visit. While each province had its own specific policies affecting implementation of the system, the general idea was that participants, including all farmers in the pilot areas who chose to participate, would pay an annual contribution of CNY10 per capita to the system, which was matched by another CNY10–CNY20 from the central Government and CNY10 from the provincial government. It was too early to judge how well the new system operates, but rural households interviewed welcomed this idea as it addressed a key concern of most rural residents, poor or not.

(iii) Subsidies on major medical bills for the hardcore poor. The so called “health salvation program” was also at pilot stage at the time of the OEM visit. The idea was to identify the most needy and issue them certificates that would entitle them to a 40% subsidy on their medical bills from major operations or being hospitalized. This program faced many operational difficulties, including in particular insufficient budgets to deliver the promised benefits, but its intention to address a key cause of poverty was appreciated.

(iv) Exemption from book fees and other fees, as well as subsidies for school boarding costs during the 9 years of compulsory education. It was too early to evaluate this ongoing program, but its intention to address another key cause of rural poverty was much appreciated.

(v) Minimal standard-of-living guarantees for rural residents, which provided cash to poor households to bring their annual incomes up to the official poverty line. After initial pilot testing in some provinces, this program was found to be unrealistic in poor regions, where local governments could not bear the financial burden. The OEM found that not all rural poor living below the poverty line needed subsidies. While those unable to work need welfare programs on a long-term basis, the productive poor could lift themselves out of poverty if the key causes of their poverty were mitigated or removed by project interventions.

72. In addition to policy interventions, the OEM studied the impact on poverty reduction of project interventions. In 1993, the PRC Government launched a large-scale program for poverty reduction, the 8–7 Program, which aimed to lift the remaining 80 million poor out of poverty during the remaining 7 years before 2000. Various projects were financed under that program, including (i) subsidized loans for poor households or enterprises that generate jobs for the poor; (ii) promoting agricultural production, including farm extension, input subsidies, and grants for small irrigation facilities; and (iii) rural infrastructure investment, including roads, electricity, drinking water systems, biogas for home cooking, and improved village paths and housing. Some of the infrastructure projects were implemented through a food-for-work mechanism, through which laborers from poor villages worked for in-kind payments.

73. In the early years, the 8–7 Program targeted poor counties. Nationwide, 592 counties were identified as “national poverty counties” and received annual grants from the central Government. In addition, some provincial governments identified their own “provincial poverty counties” and provided them with annual funds for poverty reduction. The number of the national poverty counties remained the same over the 11 years from 1994 to 2005, with only 25 counties leaving poverty—and being replaced by the same number of poverty newcomers. It appeared that the free grant from the Government provided a strong incentive for the national poverty counties to maintain their formal impoverished status. The OEM visited some of the national poverty counties and was impressed by the wealth displayed in the county capitals, which did not appear to be poor but retained the status that entitled them for the central Government grants.
74. In response to criticism about leakage from the targeting program, the Government narrowed the focus of targeting from counties to townships and villages. In 2005, the focus was further narrowed to sub-villages, called “natural villages” in the PRC, some of which have only 20–50 households. Meanwhile, the Government initiated a village program of poverty reduction and development planning that aimed to eliminate poverty in all villages, one by one, through an integrated intervention package. The new package was in fact a combination of earlier interventions, including rural roads, electricity, drinking water systems, village paths, small irrigation systems, farm extension, farm inputs, and subsidized loans. In the areas visited in Yunnan, this village program provided a grant of CNY200,000–CNY300,000 ($25,000–$37,500) to each participating village, allowing them to select interventions from a list of available options.

75. The OEM observed the following problems in the village program. First, the grant of CNY200,000–CNY300,000 provided small and temporary benefits to villagers but was too small to enable the sort of investment that could lead to significant poverty reduction. Second, providing even such a small grant to all poor villages in the PRC would place a huge financial burden on the Government, and the shortage of funding would seriously delay poverty reduction.\(^8\) A more serious concern is how ineffective the village program is in achieving its objective of poverty reduction. A recent ADB evaluation study\(^9\) found that free money from government projects encouraged beneficiaries to accept projects that brought them little benefit and did not lift them out of poverty. Similar cases were observed in Yunnan and Sichuan, where projects brought little benefit to the poor because they did not mitigate the key causes of poverty.\(^10\) Moreover, government projects usually financed construction but not O&M, assuming that village leaders and communities would take care of project facilities. This assumption has not been supported in the cases observed, as poor communities usually had no financial resources and lacked strong incentives to take care of public facilities built by governments. A more commonly held belief seemed to be that those who invested should take care of the investment.\(^11\)

---

\(^8\) In Mojiang County of Yunnan Province, for example, the OEM was told that about half of its 1,200 sub-villages were identified as poor. From 2003 to 2005, this county spent CNY6 million to implement the village program in only 30 poor sub-villages. Even assuming that the county can accelerate this process and cover 30 sub-villages in 1 year, implementing the village program in all 600 poor sub-villages will take 20 years.


\(^10\) In one model village visited in Yunnan, for example, all thatched roofs were replaced by concrete roofs financed by a grant from the village program. However, some poor households remained poor as the poor housing conditions were the result of their poverty, not its cause. In another poor village, the OEM found that some of the poorest households used oil lamps instead of electricity, even after their village was electrified by a project, because they could not afford electricity. In a poor township, the township clinic upgraded its buildings and equipment with free grants from a project, but few rural patients visited the clinic, as they could not afford its high charges for medicine.

\(^11\) In one village visited in Yunnan, for example, the OEM found that a drinking water system built through a free grant from a project a few years earlier had completely disappeared for lack of maintenance. Villagers returned to the old way of carrying water from afar.