Poverty, credit and microcredit in rural China

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China has put in place a government-organised programme of credit for farmers. Despite this, a very large number of farmers are caught without any access to loans to purchase the agricultural inputs they need. For many, this lack of credit is one of the major factors that keep them trapped in poverty. In light of this, the government agency responsible for poverty alleviation has sponsored an additional credit programme that provides a type of Grameen Bank microcredit. Yet this is not well suited to poor villages that rely upon agriculture.

The usual Chinese system of rural loans

In Mao's day, during the period of collective agriculture, each rural market town contained a government-owned credit association. When the collective fields were divided up among households in the early 1980s, these credit associations became the main source of loans to support the individual families' farming. They initially gave priority to providing credit of 3–12 months' duration to enable families to buy agricultural inputs at the start of the growing season or to buy animals for fattening and quick resale or to tide a family breadwinner over a sudden illness.

In particular, many poor farmers today require loans to purchase chemical fertiliser, which is desperately needed in the very infertile soils of most of China's impoverished areas.[1] The extensive household interviewing that I conducted in the poor hill country of the southwest revealed a doubling, or in some cases even a tripling, of grain output by families who could afford sufficient fertiliser, in comparison to neighbours who did not use any. A vital reason is that the improved grain seeds now on the market depend upon sufficient soil nutrients, and thus fertiliser use has become the dividing line between households that are able to upgrade to the high-yield varieties and those that cannot. Access to a loan to purchase fertiliser is often the difference between development and hunger.

The credit associations, however, have come under strong pressure from the state to be business-like in their loan policies. They therefore normally reject poorer households' requests on the grounds that repayment cannot be guaranteed, as the families do not possess collateral. An applicant's residence and the fields that had been allotted to the family do not count as collateral since evictions are next to impossible.[2]

This policy of non-eviction is praiseworthy, since it protects rural families from descending into the status of landless labourers. But it also means that they need to fall back on draught animals or pigs or other movable assets as their collateral. However, impoverished families do not have the wherewithal to raise such animals precisely because they lack fertilisers and therefore cannot grow enough to feed themselves, let alone livestock. Overall, in the three dozen impoverished villages that I visited in the poor mountainous southwestern provinces of Yunnan, Guangxi and Guizhou, somewhere between 10 and 15 per cent of households were caught in this trap, unable to afford any chemical fertiliser whatsoever. In the worst-off villages, a majority of the families were in these straits.

In many parts of China, the credit associations' lending policies tightened considerably during the 1990s, making it increasingly hard even for families above the poverty line to obtain loans. In an increasing number of provinces, applicants now needed to find a guarantor who would accept part of the risk. Making the task more difficult, in many areas it was stipulated that unless the applicant had substantial assets the guarantor must be the village head. Since serving as guarantor involves personal risk, it is very difficult to obtain such backing. In Hainan Province, I supervised a survey in 1993–94 of 214 rural households spread across both prosperous and impoverished townships. The survey revealed that only 9.8 per cent of families had received any formal loan within the past year, and these households were largely among the wealthiest in their communities.

One reason for this tightening of credit availability is that much of the credit associations' lending volume was being diverted away from the villages to support the development of rural industry. This is even more the case with the other normal source of rural credit, the government-owned Agricultural Bank, which, despite its title, is largely a vehicle through which money gets drawn out of the countryside for non-agricultural investments. On average, the Agricultural Bank has been lending only some 16–17 per cent of its portfolio to village households (Nyberg and Rozelle 1999:27), and almost all of this has gone to the richest. All of these factors add up to a growing credit crisis within many rural communities. As the head of a relatively well-off village told me, 'The poorer villagers here can't even think of getting credit'.

If credit were available, it appears that many of the farmers would want to borrow, even at high interest rates. Poor farmers in Qinghai Province told me in December 2000 that, if need be, they would borrow at 20 per cent a year for desperately needed agricultural inputs, at a time when the commercial bank rate for agricultural purposes stood at 5.6 per cent.

In most of the Chinese countryside, when formal credit is unavailable farmers who are short of funds turn instead to relatives and close friends. But, in the poorer villages, relatives and friends are usually caught in similar financial straits. When desperate, farmers increasingly have had to turn to usurers, at rates of 50 per cent or more in the impoverished districts and reaching as high as 240 per cent (Guo and Xue 2000:412).

The central government's poverty-reduction programmes

The government is well aware of the predicament faced by the poor, and a number of special programmes have been established that are targeted specifically towards helping impoverished families. In particular, the State Council (the central government's cabinet) established a Leading Group for Poverty Reduction in 1986, and in the 14 years up to mid-2000 this organ had funnelled a total of 138 billion yuan into poverty-reduction efforts (State Council Leading Group 2000:32). In 1999 alone, 26 billion yuan (US$3 billion) of central government funds were budgeted to these ends (World Bank 2000:14). The great bulk of these funds has been directed to 592 designated 'national poverty counties'. A quandary, though, is that today more than half of the rural poor live in counties that have not been designated as official poverty counties (Riskin and Li 2001), and most of these poor live in non-impoverished villages. By government policy, they are cut off from most forms of poverty assistance.[3]

Within the nationally designated poverty counties, lists of impoverished households are usually drawn up based on village heads' appraisals. As a means to minimise the corrupt diversion of aid funds, noticeboards in each village listing these poor households are mandated in a good number of the counties. To a certain extent, this safeguard works. My interviewing turned up a number of very poor households that have received interest-free or low-interest loans under this programme. But the central government's efforts to constrain corrupt diversions of the funding have not always been successful. I came upon several instances where quite prosperous households had been provided with substantial aid-the-poor credit, and in all of these cases the households were closely connected to important local officials. In one, for instance, when I asked to interview a recipient, the man I was escorted to was the township Party secretary's elder brother, who lived in a well-furnished home.

Even officially, the central government has not always required that the aid-the-poor credit be directed towards a poor rural household. Starting in 1989 and lasting through the first half of the 1990s, priority was given instead to lending such funds to county factories, even to private firms, in the mistaken belief it would have a trickle-down effect by providing work for the poor. In 1992 and 1993, at the height of this programme, about half of all of the subsidised poverty-reduction loans were lent to industrial enterprises in the nationally designated poverty counties.[4]

But Beijing belatedly discovered that the programme had 'minimal or no poverty reduction impact' (UNDP and The World Bank, 2000:paras. 3.26–27). The poverty counties are poorly located for industrial development, and many of their enterprises, public and private alike, started losing money. Rather than promoting development, the enterprises became a drain on local government coffers. The central government eventually abandoned the trickle-down argument, and by 1996–97 the Leading Group for Poverty Reduction was specifying that loans be aimed instead directly at impoverished village households.

Nevertheless, rural governments sometimes continue to divert poverty funds to county industry. In 2000, the deputy head of the poorest county in eastern Qinghai Province (very close to where the Dalai Lama was born) advised me that the county was currently directing 30 per cent of the aid-the-poor credit provided by the central government into county-based industry, much of it private.

Microcredit projects

In the latter half of the 1990s, the Leading Group began to channel funds into microcredit programmes for the most impoverished farmers, and by 1998, microcredit schemes had been established in some 200 impoverished counties, with central government funding of about 800 million yuan (UNDP and The World Bank, 2000:para. 3.33). The projects have spread considerably since then. This programme drew inspiration from the experience of the Grameen Bank, and, in replication of that model, the loans need to be repaid in small increments at weekly or monthly intervals. Akin to the Grameen model, Chinese villagers also form small groups of four to seven member families, and each group is not eligible for further loans to any of its members if one of the members defaults. This mechanism takes the place of a requirement for collateral or a rich guarantor, in contrast to China's normal bank or credit association loans. And because no one in a group can receive a further loan if any other member defaults, the programme is supposed to provide an incentive for group members to help one another with advice about how to make good use of their microcredit.

In the best of circumstances – in particular, in some of the microcredit programmes separately sponsored in China by the World Bank and the UN Development Programme (UNDP) – the microcredit concept works reasonably well. This has particularly been so in projects where the microcredit has been made available exclusively to women. It has been shown in such programmes around the world that women have tended to be more assiduous and responsible in their use of microcredit loans, are less likely to turn such loans to consumption purposes, and tend to have a higher rate of on-schedule repayment.

The head of the UNDP's rural microcredit programmes in China, whom I interviewed in Beijing in 2000, noted that some of the most financially successful of the programmes have been those reserved for women only. He also noted that the all-women projects tend to have the most active and most participatory group meetings. Several Chinese specialists who have participated in microcredit projects related similar stories.

But, in most cases, the microcredit projects in rural China have run into problems that were inherent in the very nature of the programme. In Bangladesh's densely populated countryside, there are large numbers of landless poor women who engage in petty trade, and the Grameen Bank lends largely to this type of poor woman. By borrowing from the bank to increase their stock of goods, they are able to earn enough through daily sales to repay loans on a weekly basis. But the poor in China's programmes are farmers in marginal hill country, whose earnings are largely postponed until harvest time or until after an animal has been raised, fattened and sold. China's major current poverty-reduction initiative is being thwarted by the very fact that it was shaped to fit the circumstances of a very different type of poor in Bangladesh.

An illustration is provided by Dangchang county, the poorest county in Gansu Province, which is itself one of China's poorest provinces. Dangchang was provided with 3.6 million yuan to disburse as microcredit to the poor, but it distributed only 2 million, in part because its microcredit programme required repayments within a shorter period than the impoverished farmers needed to recoup any agricultural investment (*Jingji xinxi bao* [Economic Information Daily], 11 January 2000). A number of the other microcredit projects financed by the Leading Group operate just as rigidly.

The microcredit programmes are far better suited to villages where opportunities exist for farm families to diversify their sources of income by engaging in non-agricultural micro-entrepreneurial pursuits. I had an opportunity during 2000 to carry out interviewing for several days at a Grameen-style microcredit project with this type of clientele. The programme had been organised by a foreign government aid agency, and the initial intention was that the microcredit would be targeted towards the poorer households in the project area. But a second goal was to show that the programme was financially sustainable. A consequence was that, in each of the half-dozen villages that I visited, the poorest households had gradually been excluded from participating.

Some were excluded by their village's microcredit loan officer, who was seeking a high rate of repayment. Others were excluded by the fact that, with repayment a core issue, no other households were willing to be in the same credit small groups, as they would have to serve as the family's guarantors if it defaulted. Repeated interviewing suggested, however, that these people were not being excluded simply because of potential loan repayment questions. More than this, they are socially marginalised people in their villages. They often tend to have fewer, or no, relatives and do not belong to supportive social networks. Within their communities, their exclusion is a representation and confirmation of their marginalisation.

Some of the programmes sponsored by the World Bank make efforts to ensure that only the poor in each community are allowed to participate and that the village loan officer must be a member of a credit group and must be elected by the credit groups' participants. The foreign government aid agency whose project I studied went a step further, stipulating that in its project a majority of the loan officers needed to be women and that women were specifically to be targeted as loan recipients. (It was subsequently discovered in this project that the female loan officers were themselves more likely to take the initiative to arrange loans for women, and for a while a clear majority of all loans did indeed go to women.) But over time, as the foreign aid agency withdrew from active hands-on participation and handed over the project's administration to Chinese authorities, this all changed.

Rather than being chosen by the community, as was originally envisioned, the loan officers were increasingly simply selected from above. The Chinese programme directors now tended to turn to the most powerful people in the villages to serve as loan officers, perhaps in the belief this would help guarantee a higher repayment rate. After all, if the most powerful person in the village is the one who receives a small commission for every loan repayment, borrowers will feel under extra pressure to repay on time. The consequence is that the programme today reinforces the official political power structure within these villages. It has been reported that 40 per cent of the present loan officers are either village heads or village Communist Party secretaries (all men).[5] Their political power is strengthened by the fact that they now hold it in their discretion whether to provide and extend loans.

Conclusion

Even though these are serious problems, they are not the most significant. The most widespread and intractable problem faced by China's rural microcredit programmes is, quite simply, that the system does not appear well suited to people who cannot make repayments until the end of an agricultural season – and most of China's poor live in communities that rely almost entirely on agriculture. Other forms of credit also require less time and money to administer and can therefore be made available at lower interest rates.

In the best of the projects in China, though, one aspect of the Grameen Bank model has been shown to be worthwhile and ought to be preserved: the mechanism whereby the small groups of borrowers meet regularly and provide each other with suggestions. Such a programme offers a means for poor farmers with inadequate knowledge to learn from neighbours how to properly apply chemical fertiliser and how best to work their land.

Notes

1. Many of us hold reservations about chemical fertilisers because their misuse sometimes produces damaging side effects: to soil structures, rivers, and ecosystems in general. But the alternative in rural China spells hunger and stark poverty, as families that cannot afford chemical fertilisers struggle to raise crops in fields that lack nutrients. To be sure, such families add to the fields whatever organic fertilisers they can find; but, on the whole, those that use chemical fertiliser simultaneously add *more* organic fertiliser to their fields than can households which lack chemical fertiliser. The reason is simple: families with bigger crops also gain more silage as a by-product and are therefore better able to raise livestock, which produce manure that can go back into the fields. And fortunately this diligent use by Chinese farmers of organic fertilisers (including, of course, household faeces) to supplement applications of inorganic fertiliser helps to offset the potentially deleterious effects of chemical fertiliser misuse on soil structures.
   Misuse certainly exists, however. Discussions with agricultural specialists in China reveal that a great many farmers, and even

local agricultural extension officers, know little about how to apply fertilisers in ways that will retain a balanced soil. Higher yields mean more trace elements sucked out of the soil, and many farmers know nothing about the need to replace them. They know little about optimum levels of fertiliser use, and when they can afford to buy all of the fertilisers that they feel they need, they reportedly spread on too much. China would do well to use the mass media to provide advice on the use and abuse of chemical fertiliser. But, unless some miraculous genetic engineering of crops can provide a cure-all to the problem of depleted soils, chemical inputs remain all too necessary.

2. The ultimate reason why farmland cannot be confiscated by banks and why poor farmers also cannot sell off the land to meet debts is that villagers in China do not literally own their own land. Instead, the land remains in the ownership of the former collectives, and the fields have been distributed to the farmers free-of-charge for their use. In many villages, the plots of land get redistributed over time, again without payments, as some households expand in numbers and need more land and as other families shrink in size.
3. In the September, 2001, the central government released a document announcing that the distribution of poverty would be reinvestigated and a new list of 'poverty counties' would be drawn up. It indicated that up to 30 per cent of the poverty funds would be set aside in future years to assist impoverished villages that were not on the new 'poverty county' list, but, notably, this funding would all go to poor villages and the impoverished households in non-poor villages would still be excluded from the anti-poverty program (*South China Morning Post* [Hong Kong], 20 September 2001).
4. This is from paragraphs 8 and 10 of a second volume produced for internal distribution alongside the joint World Bank report, *China: Overcoming rural poverty* (2000).
5. On the power structure today in Chinese villages, see Unger (2000:ch. 10).

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