

Keskusteluaiheita - Discussion papers

No. 621

Wang Huijiong - Li Shantong

PROSPECTS AND PROBLEMS OF CHINA'S ECONOMY

The authors are working at the Development Research Centre of
the State Council of P.R. China

WANG, Huijong - LI, Shantong, PROSPECTS AND PROBLEMS OF CHINA'S ECONOMY. Helsinki: ETLA, Elinkeinoelämän Tutkimuslaitos, The Research Institute of the Finnish Economy, 1997, 38 p. (Keskusteluaiheita, Discussion Papers ISSN 0781-6847; No. 621).

ABSTRACT: The Chinese economy has experienced rapid growth since China adopted a market-oriented development strategy in 1979. The aim of the economic reform has been an ambitious transformation from a centrally planned economy to a market-oriented one. Double-digit growth over one and a half decades together with the world biggest potential market has made China one of the driving forces in the world economy in 21st century. However, the transition process is no doubt a very difficult one. Various problems have been encountered and different policy measures have been tested. The paper describes China's economic development with a focus on the recent trends, presents short- and long-term prospects, and analyses the difficulties and challenges Chinese policy makers are facing.

This paper is divided into three parts: in the first part, China's economic development experience before 1996 is presented. The economic history during 1949-79 is discussed briefly, while the economic development after 1979 is described in details. In the second part, current economic trends, especially those in 1996 are analysed in full details. Various policy issues, such as monetary and fiscal policies, are described and scrutinised. Short term economic prospects as well as difficulties of the economy are also described. In the last part, prospects of economic development in 1997 together with the long-term prospects are presented, and important issues and challenges related to China's long-term sustainable development are discussed.

WANG, Huijong - LI, Shantong, PROSPECTS AND PROBLEMS OF CHINA'S ECONOMY. Helsinki: ETLA, Elinkeinoelämän Tutkimuslaitos, The Research Institute of the Finnish Economy, 1997, 38 s. (Keskusteluaiheita, Discussion Papers ISSN 0781-6847; No. 621).

TIIVISTELMÄ: Kiinan talouskasvu on ollut nopeaa 1970-luvun lopusta lähtien, kun Kiinassa siirryttiin markkinoiden merkitystä painottavaan kehitysstrategiaan. Talousreformin kunnianhimoisena tavoitteena on ollut muuntaa Kiinan talous keskusjohtoisesta suunnitelmataloudesta markkinataloudeksi. Yli puolitoista vuosikymmentä kestänyt vuosikymmenen kaksinumeroinen kasvuvauhti, maailman suurimpien potentiaalisten markkinoiden ohella, on tehnyt Kiinasta erään 21. vuosisadan keskeisistä muutosvoimista. Kuitenkin talouden muutosprosessi on hyvin vaikea. Prosessissa on ollut useita ongelmia ja useita politiikka-vaihtoehtoja on vertailtu. Keskustelualoitteessa kuvataan Kiinan talouskehitystä erityisesti nykytrendien näkökulmasta, esitellään lyhyen ja pitkän aikavälin näkymiä sekä analysoidaan niitä talouteen vaikuttamisen vaikeuksia ja haasteita.

Keskustelualoite jakaantuu kolmeen osaan. Ensimmäisessä osassa kuvataan Kiinan talouskehitys ennen vuotta 1996. Vuosien 1949-79 taloushistoria esitetään lyhyesti, kun taas vuoden 1979 talousreformin alun jälkeinen talouskehitys kuvataan yksityiskohtaisesti. Raha- ja finanssipolitiikan lukuisia ongelmia kuvataan ja analysoidaan samalla kun esitellään lyhyen aikavälin talousnäkymiä ja talousvaikeuksia. Viimeisessä osassa esitellään sekä vuoden 1997 että pitkän aikavälin talousnäkymiä. Samoin analysoidaan Kiinan pitkän aikavälin kestävä talouskehityksen haasteita.

PART I PROLOGUE

1.01 It is difficult to understand prospects and problems of China's economic development without some background information: the history of development of China since the establishment of PRC; the economic development since the launch of economic reform. Therefore, this paper is divided into three parts: in part 1 of this prologue, a briefing of China's development experience before 1979 is given, a retrospect of economic development from 1979-1995 is presented slightly more in detail. In part 2 of this paper, a detail analysis of current economic development in 1996 is given together with description of policies related to development. A part of prospects and problems of Chinese economy can also be revealed in this part. In part 3 of this paper, prospect of economic development in 1997 together with the long term prospect will be presented, and the issues related to long term development will be discussed.

1.02 Development experience before 1978 (1949-1978)

China had followed the Soviet model of Central Planning System since 1953. The first five year plan followed exactly the Soviet system of planning. By the end of the first five year plan, the government found the weakness of a central planning system. The government decentralized the planning and decision power down to the provincial level and also a part of state owned enterprise down to the administration of the local government. Latter on, economic disorder happened, then the planning power is decentralized from 1962-1964. There is further decentralization in the Cultural Revolution period (1966-1975). So China has never established a rigid central planned economic system as the former Soviet Union. Price of agricultural goods is suppressed, the surplus value is used to support the development of industry. Therefore, the rural area people live in a life of low standard. The government spent all efforts to improve social aspects of the country, education, health care etc. Tertiary sector is also underdeveloped due to the allocation of input and output of production process by the government, Development of natural science and engineering is very much emphasized.

Good lessons in this period:

1. The development of the nation is a balanced growth, the education, health of the people improved greatly;
2. The country had established a preliminary foundation of industry in all aspects, especially the heavy industry.

Negative lessons:

1. To much emphasis is put on social equity without consideration to mobilize initiative and motivation of individual;

2. Neglect growth of tertiary sector, this breaks the chain of an integrated economic activity, the industrial sector and the state owned enterprises were not grown up in a market environment. They are very unfamiliar with the operation of market mechanism;

3. Isolated from the outside world;

4. There is nearly no human resources trained in modern social science, the economists, the banker, the people who knows modern financial operation, modern management of enterprise, accountant, lawyer etc.;

5. Soviet model of administration, highly fragmented, very weak horizontal connection among ministries and committee, weak information system.

Since economic reform began in China in late 1978, there has been great improvement in the growth of the economy and in the living standards of Chinese people. In 1995 GDP was four times GDP in 1980; per capita GNP has increased 2.34 times from 1980 to 1995, with annual growth rate of 7.14%; the external trade increased 13 times. Therefore, the progress of transition of China from a central planned economy to a socialist market economy is relatively successful through a gradual approach.

1.03 Development from 1980-1995 (Since the Launch of Economic Reform and Opening)

1. Rapid Economic Growth

China has achieved an impressive economic growth since the launch of economic system reform and opening to the outside world in late 1970's. The growth rate of GDP averaged 9.9% during the past 17 years, with a growth rate of primary, secondary, and tertiary industry of 4.6%, 10%, and 9.8%, respectively.

The Eighth-Five Year Plan (1991-1995) has been successfully accomplished with an average annual growth rate of GDP around 12% in this period. In 1995, China had a GDP growth rate of 10.5% (see table 1.1). The economic development with high speed in 90's is mainly led by investment and net export.

Table 1.1 Economic Growth in China (1978-1995)

	1978	1980	1985	1990	1991	1992	1993	1994	1995
GDP (Billion Yuan)	362.4	451.7	896.44	1854.8	2161.8	2663.8	3463.4	4662.2	5826.1
GNP (Billion Yuan)	362.4	451.7	898.91	1859.8	2166.3	2665.2	3456.1	4649.6	5727.7
GDP Growth Rate (%)	11.7	7.8	13.5	3.8	9.3	14.2	13.5	12.6	10.5
Index (1978=100)	100	116	192.9	281.7	307.6	351.4	398.8	449.3	496.7
Average Growth Rate (1979-1995)	9.9%								
Average Growth Rate (1991-1995)	12%								
Per Capita GNP (Yuan)	379	460	855	1638	1882	2288	2933	3904	4754

2. Changing Economic Structure

China's rapid economic development is also accompanied with rapid structural change. Table 1.2 shows the share of non-agriculture sector in GDP has been changed from 72% in 1978 to 79% in 1995, and the share of labor force in non-agriculture sector was 29.5% in 1978, 37.6% in 1985, 40% in 1990, and 47.1% in 1995.

Table 1.2 Structure of Gross Domestic Products

	1978	1980	1985	1990	1994	1995
Primary Industry	0.28	0.30	0.28	0.27	0.21	0.21
Secondary Industry	0.48	0.49	0.43	0.42	0.50	0.48
Tertiary Industry	0.24	0.21	0.29	0.31	0.33	0.31

The economic structural change is also accompanied by structural change of ownership system which is shown in table 1.3 and 1.4. Before 1978, in China the non public owned sector was almost non-existent (public owned sector includes state owned and collective owned). The non state sector has expanded very fast. In 1978, the share of state owned enterprises in Gross Output Value of Industry had a dominant share of 78%, which decreased to 47% in 1993, and declined further to 34% in 1995. As can be seen from Table 1.5, in terms of Government Revenue, the state owned sector is still a major contributor.

Table 1.3 Structure of Gross Output Value of Industry by Ownership (%)

	1978	1980	1985	1990	1994	1995
Total	1.00	1.00	1.00	1.00	1.00	1.00
State Owned Enterprises	0.78	0.76	0.65	0.55	0.37	0.34
Non-State Owned Enterprises	0.22	0.24	0.35	0.45	0.63	0.66
Collective Owned Enterprises	0.22	0.24	0.32	0.36	0.38	0.37
Individuals	0.00	0.00	0.02	0.05	0.10	0.13
Others	0.00	0.00	0.01	0.04	0.15	0.17

Table 1.4 Urban Employment by Ownership (%)

	1978	1980	1985	1990	1994	1995
Total Urban Employees	1	1	1	1	1	1
State Owned Enterprises	0.78	0.76	0.70	0.70	0.67	0.65
Non-State Owned Enterprises	0.22	0.24	0.30	0.30	0.33	0.35
Collective Owned Enterprises	0.22	0.23	0.26	0.24	0.20	0.18
Individuals	0.00	0.01	0.04	0.04	0.07	0.09
Others	0.00	0.00	0.00	0.02	0.06	0.08

Table 1.5 Government Revenue by Ownership (%)

	1978	1980	1985	1990	1994	1995
Total Revenue	1.00	1.00	1.00	1.00	1.00	1.00
State Owned Enterprises	0.87	0.87	0.78	0.71	0.71	0.71
Non-State Owned Enterprises	0.13	0.13	0.22	0.29	0.29	0.29
Collective Owned Enterprises	0.13	0.13	0.20	0.19	0.17	0.17
Individuals	0.00	0.01	0.02	0.05	0.06	0.06
Others	0.00	0.00	0.01	0.05	0.06	0.06

3. Rapid Expanding of External Sector

The experience of economic development in the past 17 years shows that economic reform and opening to the outside world are two wings for China's economy to take off. Table 1.6 shows that the total value of foreign trade has increased from US\$ 20.64 billion in 1978 to US\$ 280.85 billion in 1995 with annual average growth rate of 12.5%, within which the value of exports is from US\$ 9.75 billion in 1978 to US\$ 148.7 billion in 1995 with growth rate of 13.2%. The value of import is from US\$ 10.89 billion in 1978 to US\$ 132.1 billion in 1995 with growth rate of 11.7%. The ratio of total external trade to GNP increased from 10% in 1978 to 41% in 1995.¹ The foreign trade structure changed tremendously between 1978-1995. The ratio of manufactured and primary goods to the total value of export stood roughly at 50:50 in 1980; 74:26 in 1990; and 86:14 in 1995 which is shown in table 1.7. The figures reveal the trend and potential of China's competitive capability in term of manufacturing output.

Table 1.6 Total Value of Import and Export

	1978	1980	1985	1990	1994	1995
Value (Billion USD)						
Total	20.64	38.14	69.60	115.44	236.62	280.85
Export	9.75	18.12	27.35	62.09	121.01	148.77
Import	10.89	20.02	42.25	53.35	115.61	132.08
Balance	-1.14	-1.90	-14.90	8.74	5.4	16.69
Growth Rate (%)						
Foreign Trade		30	29.9	3.4	20.9	18.7
Export		32.6	4.6	18.2	31.9	22.9
Import		27.7	54.1	0.1	11.2	14.2
Share in GNP (%)						
Foreign Trade /GNP	0.10	0.13	0.23	0.30	0.44	0.41
Export/GNP	0.05	0.06	0.09	0.16	0.22	0.22
Import/GNP	0.05	0.07	0.14	0.14	0.21	0.19

¹ For the large country like China, a ratio of foreign trade to GNP of 41% seems too high. Since launching reform and opening policy, the processing trade expanded very fast, it has a share of over 40% -50% of total external trade and low value added rate. If we convert GNP to USD with PPP (Purchase Power Parity) instead official exchange rate, the ratio looks normal.

Table 1.7 Structure of Import and Export

	1980	1985	1990	1994	1995
Export	1.00	1.00	1.00	1.00	1.00
Primary Goods	0.50	0.51	0.26	0.16	0.14
Manufactured Goods	0.50	0.49	0.74	0.84	0.86
Import	1.00	1.00	1.00	1.00	1.00
Primary Goods	0.35	0.13	0.18	0.14	0.18
Manufactured Goods	0.65	0.87	0.82	0.86	0.82

The absorption and utilization of foreign capital is an important aspect of opening policy. We have achieved significant progress on it. Overall, there were three phases. The inception phase is 1980-1986. Resources of the foreign capital were mainly from Hong Kong, Macau, and other overseas Chinese, and concentrated on Guangdong, Fujian and other coastal area in location and on labor intensive processing sector and hotels, and other services. From 1987-1991, the foreign investment spread southeast coastal area to Pudong of Shanghai and Bohai Rim, the share of productive project was going up. Since 1992, the foreign investment spread further through coastal area, along the rivers, along the borders and some major cities in Central-Western area. The resources of foreign capital is diversified and transnational companies also invested in China, the share of capital and technology intensive project is increased. Table 1.8 shows that the total FDI in 1992 and 1993 is more than the total FDI of the previous 12 years. Comparing with previous years, FDI was 2.5 times in 1992, doubled in 1993, increased 22% in 1994, and 11% in 1995.

Table 1.8 Utilization of Foreign Capital (100 million USD)

	Total Value of Foreign Capital	FDI	Foreign Loan	Other Foreign Investment
1979-1989	577.85	154.95	393.21	29.69
1990	102.89	34.87	65.34	2.68
1991	115.54	43.66	68.88	3
1992	192.02	110.07	79.11	2.84
1993	389.6	275.15	111.89	2.56
1994	432.13	337.67	92.67	1.79
1995	481.39	375.21	103.27	2.85

4. Improving Living Standard

Chinese people also have got benefits from rapid economic development and reform. The improvement of people's living standards is shown in table 1.9. The annual per capita of net income of farmers and urban households increased from 133.6 Yuan and 316 Yuan in 1978 to 1577.7 Yuan and 3892 Yuan in 1995, with growth rate of 8.1% and 6.4% respectively. In 1978, the saving deposit balance of households was only

21.06 billion Yuan and per capita saving deposit balance was 21.9 Yuan; by the end of 1994, the saving deposit balance of households was 2151.88 billion Yuan and increased 110 times, in addition, there were more than 10 billion USD of saving deposit balance, over 500 billion Yuan of cash in hand, and over 300 billion Yuan of various bonds, the total financial assets of households was more than 3000 billion Yuan, per capita financial assets of households was over 2500 Yuan. Since May of 1995, the system of five working days per week has been carried out, people have more time to enjoy their life.

Table 1.9 Improvement of Living Standard

	1978	1985	1990	1994	1995
Annual per capita of net income of farmers (Yuan)	133.6	397.6	686.3	1221	1577.7
Index (1978=100)	100	261.2	300.7	355.5	375.4
Annual per capita of net income in urban area (Yuan)	316	685.3	1387.3	3179.2	3892.9
Index (1978=100)	100	161.6	197.8	273.7	287.2
Annual Average wage of staff (Yuan)	615	1148	2140	4538	5500
Saving Deposit Balance of Households (108 Yuan)	210.6	1622.6	7034.2	21518.8	29662.3
Per Capita Saving Deposit Balance (Yuan)	21.88	153.29	615.24	1795.48	2448.98
Per capita Living Space in Rural Area (m ²)	8.1	14.7	17.8	20.2	21
Per capita Living Space in Urban Area (m ²)	3.6	5.2	6.7	7.8	8.1

PART II PERFORMANCE AND ANALYSIS OF CHINESE ECONOMY IN 1996

2.01 Macro-Economic Trend of Chinese Economy in 1996

1. Economic Development

In 1996, China has achieved its effort to curb down the inflationary pressure from previous years and kept an appropriately higher economic growth rate. GDP is 6779.5 billion yuan in 1996 with a growth rate of 9.7% compared to 1995. There is also improvement of the economic structure. The value added of the primary sector is 1355 billion yuan with a growth rate of 5.1%, the VA of the secondary sector is 3314.8 billion yuan, a growth rate of 12.7%, the VA of the tertiary sector is 2109.7 billion yuan, a growth rate of 8%. The structure of GDP on the supply side is shown in table 2.1.

Table 2.1 GDP and its components (1996)

Sector	Value Added (billion yuan)	Share of VA in GDP %	Growth Rate %
Primary	1355.0	20.0	5.1
Secondary	3314.8	48.9	12.3
Within:			
Industry	2858.0	42.2	12.7
Construction	456.8	6.7	8.6
Tertiary	2109.7	31.1	8
GDP	6779.5	100	

The sectoral performance will be described as follows:

(1) The Agricultural Sector

The agricultural sector has achieved a good performance through the increase of input, expansion of the area of plant crops, adjustment of structure of various plant, stabilization of the price of producers' goods for agriculture, further raise the procurement price of grain, increase the procurement of grain for store, all above means have mobilized greatly the initiative of the farmers. In addition, the favorable climate in general results a good harvest of grain. The grain harvested reached 490 million tons, a growth rate of 5%. The other major agricultural products with positive growth rate are: sugar cane 67 million tons, tobacco 2.9 million tons and fruit 45.7 million tons. Due to the effect of price factor, there is decline of area sown for certain products, cotton and oil bearing crops have a negative growth rate, cotton produced is 4.2 million tons, oil bearing crops 22 million tons.

Husbandry and fishery products kept a high growth, meat is 58 million tons, a growth rate of 10.3%, fishery product is 28 million tons, a growth rate of 11.2%.

(2) In the secondary sector, the industrial sector remains the engine of growth with a growth rate of 12.7%. The growth rate of different ownership system differs, which is shown in diagram 2.1.

There are four major features of the industrial growth in 1996: the first, there is steady monthly decline of the growth rate, growth rate of gross value of industrial product declined from 20.17% in January to 17.2% in December; the second, the rate of sales to production rises steadily quarterly, it rises from 93.04% in the first quarter of 1996 to 98.88% in the fourth quarter, but the annual rate in 1996 is lower than previous year; the third, the growth of light and heavy industry is more or less in synchronism, the annual growth rate of the light industry is 13.1% while it is 12.4% for the heavy industry in 1996; the fourth, there is further adjustment of the structure of products, there is steady growth of energy and raw material production, while the product of communication and information equipment has a higher growth rate. But there is negative growth rate of traditional products, the negative growth rate of the production of the generating equipment is a sign of warning because the phenomenon is incompatible with the growth of demand of electricity. the amount of production for selected products and their growth rate is shown in table 2.2.

Table 2.2 Production of Selected Products 1996

Item	Unit	Quantity	Growth Rate (Compared to 1995)
Yarn	tons	4,900,000	-9,6
Cloth	meters	22,120,000,000	-15
Color TV sets	set	21,090,000	2,5
Total Energy Production (Standard and Equivalent)	tons	1,260,000,000	4,6
Coal	tons	1,380,000,000	4,5
Steel	tons	101,110,000	6
Electricity	KWH	1,075,000,000,000	6,7
Power generating equipment	kW	15,690,000	-5,9
Machine tools	unit	165	-19
Integrated circuits	chip	435,760,000	39,3
Programme Controlled telephone	set	19,340,000	

Table 2.2 can illustrate the current situation of Chinese industry. There is decline of traditional sectors, as yarn, machine tools etc. There is growth of new high technological sector such as integrated circuits and programme controlled telephone set. There is need to restructure the product structure to expand to new market needs.

The V.A. of the construction sector is 456.8 billion yuan, within which the V.A. of state owned construction enterprise is 116.9 billion yuan, the project constructed by SOEs reached 214 thousand in number.

2.02 Growth Analysis

Table 2.3 is prepared to show the sources of growth for both the supply and demand side to give an overall picture. Detail description of the performance of the demand side will be followed.

Table 2.3 Contributions to GDP Growth by Demand

	Total Investment	Consumption	Net Export
1979	-16.5	119.4	3.0
1980	37.6	60.8	1.6
1981	-18.6	106.8	11.8
1982	23.0	59.2	17.8
1983	52.8	54.5	-7.3
1984	46.5	58.8	-5.3
1985	65.7	60.1	-25.8
1986	39.5	46.4	14.1
1987	51.7	33.3	14.9
1988	77.4	30.4	-7.8
1989	165.5	-61.7	-3.9
1990	-30.8	60.1	70.7
1991	30.7	67.6	1.7
1992	54.2	52.9	-7.1
1993	75.8	40.9	-16.7
1994	46.5	35.6	17.9
1995	50.3	46.3	3.4
1996	69.3	31.1	-0.4

1. Investment

The total fixed assets of the whole society invested in 1996 is 2366 billion yuan with a growth rate of 18.2% compared to 1995. The real growth rate is 12.7% with the price factor taken into account, the fixed assets investment rate is 34.9%. The structure of the investment from different perspective is given in table 2.4 (a) (b) (c). The large and medium projects completed in 1996 have been increased to 134 in number compared to the target number of 97 set up in the beginning of the annual plan. The number of key projects constructed reaches the highest record of recent years.

From the analysis of the target to be achieved in macro-economic control and the relationship of investment and economic growth, it is fair to judge that the aggregate investment is more or less normal but there is room of improvement for the structure of investment. The sectoral share of investment of agriculture, energy and raw material is still low although the growth rate seems to be high; the aggregate level of investment on real estate is high; redundant construction is serious and there are too many new projects launched for construction, it increased by 10.7% compared to pre-

vious year; there is also increase of inventory, it is estimated to be 500 billion yuan by the end of 1996, a share of 7% of GDP. It is increased by two percentage points compared to previous year, a reflection of poor operation of the micro-economy. The Central and Western region still have low growth rate and low share of investments.

Table 2.4 Structure of Investment (Type of Investors)

Type of Investor	Investment billion yuan	Growth Rate (%)	Share of Total Investment (%)
State owned economy	1235.9	13.4	52.2
Collectively owned economy	349.0	6.1	14.8
Household and individuals	333.0	30.1	14.1
other types of economy	448.1	37.0	18.9
	2366.0	18.2	100

Table 2.4 (b) Sectoral Share of Investment 1996 (Rural Collective and Individual in Urban and Rural are not Counted)

Sector	Investment billion yuan	Growth Rate %	Share of investment %
Agriculture, husbandry, fishery water conservancy etc.	33.6	27.5	1.9
Energy	293.8	21.1	16.9
Raw material	150.5	2.9	8.7
Machinery and electronic industry	87.2	21.1	
Light and textile industry	99.9	10.7	5.7
Transport, Post and Communication	301.2	22.1	17.3

Table 2.4 (c) Regional Share of Investment 1996 (Rural Collective and Individual in Urban and Rural are not Counted)

Region	Investment billion yuan	Growth Rate %	Share of Investment %
Eastern	1038	17.4	64.2
Central	368.2	16.6	22.8
Western	211.3	11.2	13.0
Total	1617.5		100

2. Consumption

The total value of consumption should include a part of products consumed in the rural area not to be sold in the market. The following figures refer to the consumer's products through market transaction. But its trend of growth can be roughly estimated to be the overall trend of consumption with the growth of urbanization and market in China. Table 5 (a) and 5 (b) present some facts.

Table 5 (a) General Retail Sales of Consumption goods (1996)

Item	Amount billion yuan	Growth Rate (Real) %	Share of Total
G.R.S. of urban consumption goods.	1492.1	13.5	60.6
G.R.S. of consumption goods at county and below county level	969.3	11.2	39.4
Total G.R.S. of Consumption goods	2461.4	12.5	100

Table 5 (b) Structure of G.R.S. (Types of Ownership)

Type of Ownership	Amount of Sales billion yuan	Growth Rate (%)	Share of Total (%)
State economy	678.7	9	27.6
Collective economy	468.7	13.5	19.0
Private	79.1	40.6	3.2
Other economies	1235.1	27.4	50.2

It can be shown from table 5 (b) that other economies and private economy have a high share of total general retail sales and a higher growth rate than the SOEs and collectives.

3. External Trade

There is further expansion of external trade in 1996, the amount of external trade (import and export) reaches 289.9 billion U.S.D., with a growth rate of 3.2%. The export has the locus of U-shape, first declines, then rises, the total amount of export is 151 billion U.S.D., with a growth rate of 5.1%. The trade surplus is 12.3 billion U.S.D. in 1996.

The major features of external trade in 1996 are as follows:

(1) Overall Trend

There is continuous decline of export in the upper half year. Based upon comparison of monthly value of export, the rate of decline is -0.1%, -2.6%, -19.2%, -5.1%, -5.1% and -12.6%. It turns into positive growth rate since the later half year. The growth rate is +1.4%, +12.8% respectively in July and August etc. With regard to the import, there is boom of import growth in the first quarter of 1996, import growth is declined since April 1996, there is further decline of this growth in the second half year of 1996. Table 2.6 gives other aspect of the external trade in 1996.

Table 2.6 Performance of General trade and Processing Trade

Item	Amount billion U.S.D.	Growth Rate %	Share of Total export %	Share of Total Import %
Export of general trade	62.8	- 12	42.7	
Export of processing trade	84.3	+ 14	57.3	
Import of general trade	39.4	- 9		38.7
Import of procession trade	62.3	+ 7		61.3

(2) Trend of Sectors

The performance of sectors of external trade is shown in table 2.7 and table 2.8.

Table 2.7 External Sectoral Performance 1996 (Type of Ownership)

Item (Import and Export of)	Amount of trade billion U.S.D.	Growth Rate %	Share of Total %
State owned enterprise	145.2	- 11	52.7
Foreign Invested Enterprise	137.1	+ 25	47.3
Barter Trade	1.39	- 52.1	

Table 2.8 Major Sectoral Performance of Export

Item	Value billion U.S.D.	Growth Rate %	Share of Total Ex- port %
Garments	25	4	17
Yarn and textile product	12.1	-13	8
Steel (Real term)	4.2 million Ton	-29	
Acquatic products	1.7	-17	1.1
Machinery and	48.2	10	32
Electronic equipment			

Machinery and electrical equipment have taken a high share of import, the value of import of them reach 61.4 billion U.S.D. with a share of 44% of import and a growth rate of 3.6%. The major categories of the import goods are: textile machinery, machine tools, plastics and rubber processing equipments, integrated circuits, air plant, automatic data processing equipment, components and parts of T.V. set, wireless communication equipment and cars, etc.

(3) Analysis of causes of change of performance of external sector

The 30% rise in the U.S. dollar over the previous twelve monthes has effected real exchange rate in the Asia Pacific region and slowed export growth of the economies in East Asia. The effect of the change of the real exchange rate is not the sole factor

in contributing to this change of external trade performance. There are other policy impacts from the Chinese aspects.

--- Change of policy on reduced VAT rebates on export and a high base of comparison.

On May 25th, 1995, the China's State Council had issued a document "A Notice of Reducing VAT Rebates on Export and Strengthening of Management of Rebates on Export". The VAT rebate was set at 17% generally in 1994. It was reduced to 14%, it was announced in this document that the reduced rate of VAT rebate on export will be effective since July 1st 1995. On Oct. 6th 1995, there is further cut of rate of VAT rebate. Due to this policy impact, there was rush of export in the upper half year of 1995, the growth rate of export from Jan.-June 1995 was 88.3%, 55.2%, 51.2%, 34.2%, 35.8% and 28.8% respectively. This creates a high base of comparison for export in 1996 to 1995. This is the major cause of negative growth rate of export in the upper half year of 1996;

The government could not rebate the VAT of export in time also discouraged the exporters in the upper half year. The authority becomes aware the fact and VAT of export was rebated in the lower half year. This has promoted the growth of export since July 1996;

--- Effect of change of interest rate

China had raised twice the interest rate to curb down the rate of inflation in 1995. The preferential interest rate of loans of procurement for exporters were also abolished in 1995. This has effected the performance of exporters. The People's Bank (The Central Bank of China) has lowered interest twice in 1996. This has some positive effects on the promotion of export;

--- Inefficient SOE exporters

The SOEs had the highest export performance in the first quarter of 1995 to take the advantage of policy change, but they trailed behind other exporters (foreign invested enterprises, collective enterprises and others) since mid-1995. It is shown in table 2.7 that the foreign invested enterprises have a growth rate of 25% while the SOEs have a negative growth rate of negative 11% in 1996. This shows the inefficient SOE exporters and there is further need to reform the external trade sector of China;

--- Effect of external and domestic market

China has not entered the WTO, therefore, it cannot enjoy the benefits of multilateral arrangement, there is increase of restrictions from countries of bi-lateral textile arrangement with China, such as U.S.A., Canada and European Community. The amount of restrictions reached 250 with total amount of 12.4 billion U.S.D., increased by 40% compared to 1993 40-50% of China's textile export is subjected to this quota restriction; trade protectionism from regionalization of economy also has

impact to China's export. There are also factors of decline of export of grain, crude oil and steel due to fluctuation of demand of domestic and international market;

--- Effect of Tariff

China reduced nominal import tariff rates from an average rate of 36% to 23% in April 1996, but this has limited impact for the import because the State determined also to abolish and reduce the exemption and reduction of import tariff for imported equipment and raw material of investment of foreign invested enterprise, and also for technological upgradation projects of domestic enterprises etc.

2.03 *Other Aspects*

1. Public Finance

The implementation of the national fiscal budget is satisfactory in general. The budget revenue kept its potential of growth throughout the whole year, and its growth rate is higher than budget expenditure. Based upon preliminary estimation, the budget revenue is 736.66 billion yuan, which is 107.2% of the budget, an increase of 112.4 billion yuan compared to previous year with a growth rate of 18%, which is slightly higher than the growth rate of GDP in nominal term; the fiscal expenditure is 791.4 billion yuan which is 105.7% of the budget, an increase of 109.1 billion yuan than the previous year with a growth rate of 16%. The budget expenditure is greater than the revenue by 54.78 billion yuan which is smaller than that in previous two years. But it should be pointed out that the budget revenue income is only 10.9% of GDP. There is need to further improve the budget revenue income in order to strengthen the necessary capability to implement the fiscal policy of the Central government.

2. The Financial Sector

The successful soft landing of the Chinese economy in 1996 relies largely on the improved performance and regulation of the financial sector. The major financial indicators are shown in table 2.9 which can explain partly the fact in next section.

It can be seen from table 2.9 that the People's Bank of China made the curb of inflation to be the top priority. The background of monetary policy in 1995 and 1996 is to implement a relatively tight monetary and fiscal policy. Due to the low share of fiscal budget revenue income of GDP, there is no more room to play for fiscal policy. A tight monetary policy continued for two years have curbed down the high inflationary pressure since 1993. The monetary and credit performance in 1994 are highly relaxed: the growth rate of M1 and M2 is 26.8% and 34.4% respectively. It can be seen by comparison of growth rate of M1 and M2 in 1994, 1995 and 1996 that a consistent effort of controlling the money growth is pursued. Besides, the People's Bank had adjusted lending rate twice in 1995, other means are also adopted to depress the over-

heated demand for loans. Financial supervisory function is also strengthened in 1995 and 1996, the commercial banks are requested to exercise the asset/liability ratio management.

Table 2.9 Major Financial Indicators 1995 and 1996

Item	1995		1996	
	Amount billion yuan	Growth Rate %	Amount billion yuan	Growth Rate %
1. Outstanding deposits of all Financial Institution	5390	31.8	6859.6	27.3
2. Year End Saving Deposits by urban and rural household	2970	37.7	3852.1	29.6
3. Outstanding loans of all financial institutions	5050	22.7	6115.7	21.2
4. M_0	788.5	8.2	880.2	11.6
5. M_1	2398.7	16.8	2825.1	18.9
6. M_2	6075.0	29.5	7611.9	25.3
7. Foreign Exchange Reserve	73.6 bil U.S.D.		105 bil U.S.D.	42.7

3. Utilization of Foreign Capital

There is a stable growth of utilization of foreign capital. The total amount of projects from foreign investors approved in 1996 is 24529, the amount contracted is 73.21 billion U.S.D., actually utilized is 42.35 billion U.S.D. with a growth rate of 12.88%. The number of TNC invested in China is increased, it is estimated that at least 200 more out of 500 largest TNC's are investing in China. By the year end of 1996, the accumulated number of projects from foreign investors approved is 283793, the amount of foreign investment contracted is 469.33 billion U.S.D., actually utilized amounted to 177.22 billion U.S.D., foreign invested enterprises in operation is more than 140 thousand in number. By the end of 1996, the loans appraised from the foreign government is 3.18 billion U.S.D., the loan actually utilized is 2.18 billion U.S.D. an increase of 42.7% than the year beginning of 1996.

Foreign financial institutions have become an important element of Chinese financial system in operation. In 1997, there will be appropriate increase of foreign financial institutions in China. Establishment of operating branches of foreign financial institutions will be allowed under the condition of strengthening of supervision.

4. Price

Continuous effort exercised to suppress the inflationary pressure is the priority task in 1996. The rate of inflation is reduced greatly and the economic growth momentum is kept in 1996, the balance of aggregate supply and demand is fully focused, supervision and monitoring of the market price of essential commodities are strengthened.

The general retail sales price index is 6.1% in 1996, a decrease of 8.7 percentage points compared to previous year; the CPI index is 8.3%, a decrease of 8.8 percentage points. The major features of variation of market price in 1996 are:

- (1) The scale of rise of price of producer's goods is the lowest in recent years;
- (2) there is steady variation of the market price throughout the year of 1996, the monthly increase of RPI compared to same period last year is below 8% and 10% respectively, and there is moderate monthly increase of price compared to previous month;
- (3) the major factor underlying the rise of price are driven by housing and service cost;
- (4) the price increase of all regions declined monthly in synchronism to each other.

The variation of GRI and CPI in 1995 and 1996 is shown in figure 2.2.

2.04 Major Macro Economic Policies and Reform in 1996

The stabilization of macro-economic environment with growth is through a combination of implementation and reform of major macro-economic policies. A part of them have been described in previous sections. Hereunder, those macro-economic policies will be described in order with very brief statements of those parts described before.

1. Fiscal and Taxation policy

The major fiscal and taxation policy implemented in 1996 are four aspects:

- (1) Important reforms are proceeded on taxation system of import and export. Tax rate on export rebate has been adjusted downward. Supervision system of account of guarantee fund on import material is implemented on processing trade; there is adjustment of custom tariff in large scale and large scope since April 1st 1996, several items of import tax reduction and exemption are also cleared and rectified;
- (2) The tax sharing fiscal system is further perfected, the transitional transfer payment system from the central to local government is implemented, the local government has also implemented transfer payment system to difficult regions under its administration. Although the current arrangement of fiscal transfer can be studies further to see whether it is beneficial or not beneficial to improve the regional income disparity. The tax sharing fiscal system is further normalized below the provincial governmental levels;
- (3) Rectify the order of public finance and taxation with full effort;

- (4) Actively participate and support other reform measure with fiscal means.

The major issues of fiscal aspect in 1996 are: there is serious leakage of normal tax income; there is low increase of fiscal income due to poor economic performance of enterprises; the serious erosion of the normal tax base due to extra-budget revenue system.

2. Financial Policy

The Central Bank of China has kept an appropriately tight monetary policy throughout 1996, by the mean time, various monetary policy instruments are applied for fine tuning, major results have been achieved. The following reform measures and monetary operation also had been undertaken.

(1) Electronic screen type inter-bank money lending market of the national banking system is established in the year beginning. Currently, there are transactions on overnight, seven days, twenty-days, thirty-days, sixty-days, ninety days and 120 days. The interbank money lending market established is divided into two networks, the primary and the secondary.

(2) The business on indexed deposit is stopped in operation since April 1st, the interest rate for deposit and credit of the bank has been adjusted downwards of 0.98 and 0.75 percentage points in May 1st, these interest rates are further adjusted downwards of 1.5 and 1.2 percentage points on August 23rd. The interest rate on deposit and credit between the Central Bank and financial institutions is also adjusted.

(3) Open market operation for treasury bill is started. The target of open market operation of the People's Bank is for the implementation of monetary policy to keep the reasonable liquidity of the financial system. There are now fourteen commercial banks classified into first rank entity of transaction. They are also first rank entity qualified in the operation of Chinese treasury bill. The open market operation of China is in the form of re-purchasing, the operation is proceeded in the form of interest call for tenders.

(4) Reform of foreign exchange clearing and sales system. The buying and sales of foreign exchange of foreign invested enterprises is put in the national clearing and sales system since July 1st, 1996, by the mean time, the "regulation of management of clearing, sales and payment of foreign exchange" is revised and announced. RMB has become convertible in the current account since Dec. 1st.

(5) A series of new regulations is issued, such as "management on credit certificate", "general regulations on credit", "credit from main bank system" etc. Tentative main bank management is experimented for 300 key large and medium SOEs and also large and medium SOEs in Beijing, Tianjin, Shanghai, Wuhan, Shenyang etc.

3. Policies on Foreign Trade and Foreign Exchange

There are two major factors which influenced the performance of external trade of China in 1996: one is the influence of the change of domestic economic policy, the other is the influence from external international environment which refers to the fact that China has not become a member of WTO, therefore it suffers from the negative impact of missing the right from multilateral agreement of that organization.

The major domestic economic policy factors influenced the foreign trade of China in 1996 are:

(1) Change of policy on export tax rebate, the State has adjusted downward twice the tax rate on export rebate;

(2) Influence of exchange rate, the exchange rate of RMB kept a rising trend in 1996, this exercises a definite pressure on the operation of foreign trading enterprises, although this impact is moderate in general;

(3) Influence of adjustment of policy on import taxation, the State decided to abolish, reduce and normalize the policy on reduction and exemption of import tax, in accompanying the reduction of custom import tariff a part of non-tariff barrier is also eliminated;

(4) The State has adjusted the interest rate downward twice in 1996.

In 1996, China has realized RMB convertible in current account, this is one of the major achievements on the reform of foreign exchange management. The authority of the Central Bank had send a formal letter to IMF on Nov. 1996 declaring that China will accept the responsibility of section 23 and 4 under article 8 of IMF agreement to realize RMB convertibility of the current account, China will not implement discriminative differentials exchange or multiple exchange rate to the payment and transfer of current international transactions (not targeted to transfer of capital), this includes no restriction to payment and transfer of all non-tangible trade, these principles will be followed in all regulations of China. Therefore, China has realized in advance its promise to implement RMB convertibility in current account by the year 2000 to meet the requirement of article 8 of IMF agreement.

The major achievements in the reform and management of foreign exchange system in 1996 also includes the following aspects:

(1) Establishment of statistical system on balance of payments;

(2) Actively perfect the management of current account;

(3) Strengthen the management of recording the total short term foreign exchange;

(4) Strengthen the examination and supervision of foreign exchange business of financial institutions;

(5) Perfect the operation and management of foreign exchange reserve; promote the healthy development of foreign exchange market.

Since the unification of the exchange rate in early 1994, the exchange rate of RMB to U.S.dollar and other Western currencies remains a stable trend with slight increase. The exchange rate of RMB to U.S. dollar appreciates 0.3% further in addition to the appreciation of 2.9% and 1.5% in previous two years. The major reason underlying a strong RMB is the rapid continuous increase of the foreign exchange reserve and also supply in excess of the demand. The impact on the promotional effect of export due to devaluation of RMB in the initial period of unification of exchange rate is eliminated basically, both domestic and foreign enterprises dealing with external trade is facing more and more the pressure of high cost in foreign exchange. The People's Bank will continue to maintain a relative stable exchange rate of RMB through purchasing and sales in the foreign exchange market to relax the supply and demand pressure of foreign exchange.

4. Policy on Utilization of Foreign Capital

China has made some adjustment on policies of utilization of foreign capital in 1996 based upon the international practice. This unification of policy will create an equal and competitive environment for various types of enterprises. The major adjustments are: (1) There was no policy change for special Economic Zone and Shanghai Pudong zone, some concrete measures are subjected to perfection. (2) There was larger adjustment and reform on tax policy for import.

The contents of adjustment of import tax policy in 1996 are:

(1) Overall level of custom import tariff is reduced greatly, it is reduced from 35.9% to 23% since April 1st;

(2) Foreign invested enterprises established and approved after April 1st will pay normal tax on imported equipment and material based upon regulation;

(3) Foreign invested enterprises with total investment less than 30 million U.S.D., which was approved and established before April 1st can still enjoy the exemption of import custom tariff and VA tax for imported equipment of self-use (including material for construction) within the investment target before Dec. 31st 1996; those foreign invested enterprises with total investment above 30 million U.S.D. will enjoy better grace period.

(4) Implement seriously the guideline "to utilize the foreign capital actively, reasonably and effectively", to upgrade the quality and level of utilization of foreign capital;

- (5) Adjust the export commodity structure with full effort;
- (6) Rectify the order of management and operation of foreign trade and foreign economic relations;
- (7) Develop the international market in all aspects;
- (8) Accelerate the development of information industry of foreign trade and economic relations, catch up the global advanced level;
- (9) Push forward reform of development assistance to abroad with full effort;
- (10) Strengthen the legislation, legal execution and legal knowledge popularization, accelerate the process of establishment of legal system in the area of foreign trade and economic relations.

5. Reform of Economic System and State Owned Enterprise

China has launched the economic system reform around 18 years. Two official documents have been announced. China has encouraged the development of different types of ownership system the non state sector is booming and there is decline of share of production of the State Owned Enterprise in the process of transition from a former central planned economy to a market economy. The booming of the non-state sector is promoted by market force. The State owned enterprise has the weakness known worldwide due to its low vitality. China has pushed forward the reform of SOEs for several years. The basic guideline of reform has been set up in the "Decision of the CPC Central Committee on Issues Concerning the Establishment of a Socialist Market Economic Structure" by the 14th National Congress of the Chinese Communist Party. The major aspects of economic system reform in 1996 are: Attention is focused on the enterprise reform to be the key priority, proceed to increase the mobility and restructure of capital stock, explore to establish supervision and operating system of state assets, actively push forward social security and housing sector reform, deepening the circulation system reform by focusing on grain and cotton, strengthen, the reform of system of investment financing, combine the urban and rural reform in organism. Five concrete reform measures are implementing:

- (1) Accelerate the reform steps of state Owned Enterprises, strengthen the effort for structural adjustment;
- (2) Accelerate the social security system reform to cope with the reform of SOEs;
- (3) Further improve the housing sector reform, to develop housing market with full effort;
- (4) Actively push forward the circulating system reform focusing on the grain and cotton;

(5) Perfect further the fiscal and tax system; perfect the financial system so as to enhance the macro-economic control capability.

Reform of the SOEs in 1996 is focused on the following;

(1) Concentrate effort to reform large SOEs and enterprise groups

The State has decided to concentrate its effort on the reform of 1000 large SOEs, within these, around three hundred enterprises are identified with capital support from the banks, the supervision of credit for them is also strengthened.

The State has experimented 57 enterprises groups in 1996, their decision power is extended, the right of external trade is also delegated.

(2) Further liberalize small state owned enterprises. There are now around 240 thousand state owned enterprises, most of them is managed by municipality and counties. Reform of these enterprises is responsible by the local government for the organization and implementation. Various forms are implemented, such as restructuring, alliance, merger, stock share cooperative system, lease, contract operation and sales.

(3) It is seen by the state that the effective means to improve the overall quality of the state economy is to restructure the capital assets of them through bankruptcy, encouragement of merger, implementation of redeployment of employees. The State has experimented optimization of capital structure of SOEs in 58 cities. In 1997, the number of experimental city will be extended to 110. The State has determined to take 30 billion RMB from the reserve fund for bad debt, for merger, bankruptcy and re-employment.

(4) Increase equity and reduce debt through multi-channel, five policy measures will be adopted by the State: the first is to change gradually the debt (due to "change from allocation to credit") to become the equity capital of the state; the second, the debt formed from the construction of fixed assets since 1989 will be changed gradually into the equity capital of the state; the third is to select some large enterprises to be financed through issue of stocks or convertible bond; the fourth, those regions with surplus fiscal capacity should support the backbone enterprises in difficulty through fiscal resource; the fifth, encourage the enterprise to supplement the public accumulating fund and equity capital through their own resource to reduce the debt burden of enterprise.

(5) Strengthen the operation and management of enterprises. The SOEs should change the concepts, face the market, strengthen internal management system adaptable to competitive environment;

(6) Seriously push forward enterprise on "reduce loss increase profit"

Social security system reform is a necessary condition in deepening of enterprise reform. A unified basic pension and insurance system for the workers and staffs should be implemented. The reform of the health insurance system is to master the experimental work in more than 50 cities. Continuous perfection of unemployment insurance and insurance on injury. Manage better various social insurance fund, improve the level of service.

PART III PROSPECTS AND PROBLEMS OF CHINESE ECONOMY

3.01 *Introduction*

The pervious parts presented current situation of Chinese economy with analysis of its factors of growth, the effect of policies together with a brief retrospect of the past. In this part of the paper, the prospects of China's economy in 1997 and to the year 2000 will be described. The economy of current year will be described based upon the projection done by Our Center with reference to the annual governmental planning target, the description up to the year 2000 will be based on China's "Ninth Five" year plan and outline of 2010 Long Term Target. China is undergoing a process of transition from a former central planned economy to a socialist market economy, the planning and administrative mechanism are still in effect partially while the market mechanism is not perfected yet. The quantitative targets set up in the governmental plan can generally be fulfilled while the low efficiency of the economy is generally due to the incomplete transformation of the economic system. Therefore, it is raised in the government document to implement two basic transformations: to push forward the basic transformation of the economic system from a planned economic system to socialist market system; to change the economic growth pattern from extensive growth to intensive growth.

Potential factors for long term growth and problems will also be discussed in this part.

3.02 *Prospect of Economic Growth in 1997*

China has prepared the annual plan of 1997. Generally, the planning target will be on the lower side. And the projections done by various institutions will generally be higher than the target. Table 3.1 gives the economic growth target of 1997 set up by the government and also with two projections, one is done by our center, the other is quoted from North Asia Monthly projected by Merrill Lynch.

It can be seen from table 3.1 that the projections done by various institutions are generally more optimistic on the economic growth rate etc. It is reported by the State Bureau of statistics the performance of Chinese economy from Jan-April 1997 which is shown in table 3.2. It can be shown from the preliminary messages given by table 3.2 that the growth potential is kept with growth of investment rate around 15% while the general retail sales price index (which is the index used by China for measurement of inflation) is 2.3%.

Table 3.1 Prospect of Growth of Chinese Economy in 1997

Item	Unit	Projection 1	1997 Planned Target	Projection 2
1 Growth Rate of GDP	%	10-10.5%	8	11
1-a Growth rate of VA of Primary Sector	%	4.3%		
1-b Growth rate of VA of Secondary Sector	%	13.4%		
1-c Growth rate of VA of Tertiary Sector	%	8.2%		
2 Investment of Fixed Assets of Whole Society	B.Y.	2800 Billion Yuan	Investment Rate 32%	
2-a Growth Rate in Nominal Term	%	19.2%		
2-b Growth Rate in Real Term	%	12.5%		
3 General Retail Sales Price Index	%	5.6%	6	
4 Consumer's Price Index	%	7-8%		6,5
5 Registered unemployment Rate of Cities and Towns	%	around 3%	around 3%	
6 Growth Rate of Fiscal Budget Revenue Income (exclude debt income)	%	17.3%	Reduce Budget Deficit 4 B.Y.	
7 Growth Rate of Fiscal Budget Expenditure	%	16.5%		
8 Increase of Household Saving Deposit	B.Y.	1300 Billion Yuan		
9 Increase of Issue of Money	B.Y.	130 Billion Yuan	120	
10 Increase of Bank Credit	B.Y.	1200 Billion Yuan		
11 Amount of Import	bn.U.S.D.	156 Billion U.S.D.	around 155 bn U.S.D.	159,7
11-1 Growth Rate of Import	%	9.6%		
12 Amount of Export	bn.U.S.D.	165 Billion U.S.D.	around 155 bn U.S.D.	169,2
12-1 Growth Rate of Export	%	9.2%		

Note: 1 Projection done by DRC

2 Projection done by Merrill Lynch North Asia Monthly April 1997

Table 3.2 Statistics of Selected Items (Jan-April) 1997

Item	Amount	Growth Rate
Total External Trade	90.2 billion U.S.D.	Growth Rate 13%
Within which: Export	50.3 billion U.S.D.	26.9%
Import	40.0 billion U.S.D.	-0.5%
Investment on fixed assests	242.5 billion U.S.D.	Growth Rate 15%
With which: Capital construction		18.8%
Technology Rehabilitation		18.6%
Real Estate		2.8%
others		12.4%
General Retails Price Index		2.3%
Consumer's Price Index		4.7%

3.03 Prospects of Chinese Economy by 2000 and 2010

1. Chinese Economy in the year 2000 and 2010

It is targeted in China's Ninth Five Year Plan that by the year 2000, China's GDP is expected to increase from 5.76 trillion yuan to 8.5 trillion yuan in terms of 1995 prices, with a growth rate around 8.1%. During the Ninth five Year Plan period, per capital income of urban dwellers will have an averaged annual growth rate of 5%, while the per capital net income for rural people will have an averaged annual growth rate of 4%.

It is targeted by the government that by the year 2010, GDP will double the figure of the year 2000, i.e. the annual growth rate will be around 7.2%, the population will be controlled within 1.4 bn.

The target of investment rate is 30% of GDP, amounted to 13 trillion yuan during the Ninth-Five Year planning period with average annual growth rate of 10% within which, the investment of the state owned enterprise will be 8.8 trillion yuan, a share of 68% of total investment.

2. There are also projections on material production in the year 2000 which is listed in table 3.3.

Table 3.3 Projection of Outputs of Major Products by the Year 2000

Item	Unit	Output	Supplementary remarks	
Grain	m. tons	490-500	25 to 35 m. tons more than 1995 (490m.t. in 1996)	
Cotton	m. tons	4.5	1995:4.5	1996: 4.2
Coal	bn tons	1.4	1995: 1290m	1996: 1.38
Power	trillion KWH	1.4	1995: 1	1996: 1.075
Chemical Fertilizer	m. ton	28.4	1995: 24.5	1996: 26.6
Steel	m. ton	105	1995: 94	1996: 101
Ethylene	m. ton	4.2	1995: 2.43	1996:3.01
Cars	m. unit	2.7	1995:1.5	1996:1.49
Integrated Circuits	bn piece	2.5	1995:310m	1996: 435m
Number of Telephone	m. set	174	1995: 85m	1996: 108m

Source: Derived from: Li Peng Report on: Nation Economic and Social Development "Ninth Five Plan" and Outline of 2010 Long term Target
People's Publisher 1996 March

It can be seen from table 3.3 that most of the outputs targeted has achieved high growth in 1996, production of coal and steel in 1996 is not far away from the target set up for 2000. Therefore, the target set up in the Ninth-Five Plan is generally on the conservative side. For example, the difficulty in raising the agricultural production is fully taken into consideration, therefore, the target of grain production is set up to be

490-500 m.t., but it was reported that the output of grain has reached 490 m.t. in 1996. This fact should also be kept in mind that agricultural production influenced greatly by the climate, therefore, it should be cautious to the good figure of grain production in 1996.

3.04 Potential of Growth of Chinese Economy

1. Chinese Economy from the International perspective

China has achieved more than one and half decade of extra-ordinary high growth rate of the economy. Based upon the government target of Ninth-Five plan, then GDP of China will reach 8.5 trillion yuan by the year 2000. It is equivalent to 1024 billion U.S.D. if exchange rate of 8.3 yuan/ 1 U.S.D. is used Chinese economic strength will be ranked the Seventh in the World, if GDP is measured in terms of U.S.D. (By the year 1994, there are six developed countries with GDP more than 1 trillion U.S.D., they are: U.S.A. (6.64 trillion U.S.D.), Japan (4.59 trillion), Germany (2.05 trillion), France (1.33 trillion), Italy (1.02 trillion) and U.K. (1.02 trillion).

In terms of outputs of major industrial products, China has taken the lead of production in many products which is shown in table 3.4. This table also provides the message of the rank of order of products. This table can illustrate clearly the industrial capability created in China as explained in part 1 of this paper. This development is also confirmed by international organization that: "Development of the Chinese manufacturing sector is shown to have been extensive since 1949, with the emphasis on achieving the maximum degree of self-sufficiency across the range of products considered desirable. Until the reform era, the emphasis was on the development of heavy industry, a bias that was corrected only in the early 1980', after which the growth of manufacturing value-added accelerated in response to the incentives provided by reforms."

Therefore, in real term, the overall Chinese economic strength seems to be higher than one trillion U.S.D. by the year 2000. There is debate about the indicators used in measuring the wealth of a nation or per capita, there are traditional measurement of GDP, there is measurement through PPP, and also the recent research with measurement of wealth by taking human resources, produced assets and natural capital into consideration. These facts should be reminded. But it is impossible to discuss here.

2. Human Resource-one of the potential factor of Chinese Economy for Long Term Growth

The huge population of China is a well known fact globally. China has 1211.2 million of population in 1995, which is more than the sum of 25 high income economies (849.9) in 1994. This huge population means a huge market which creates a large de-

mand pull for the economic growth. this is one of the reason of rapid growth of FDI inflow to China.

Figure 3.1 Various Forms of FDI - Amount of Capital Pledged

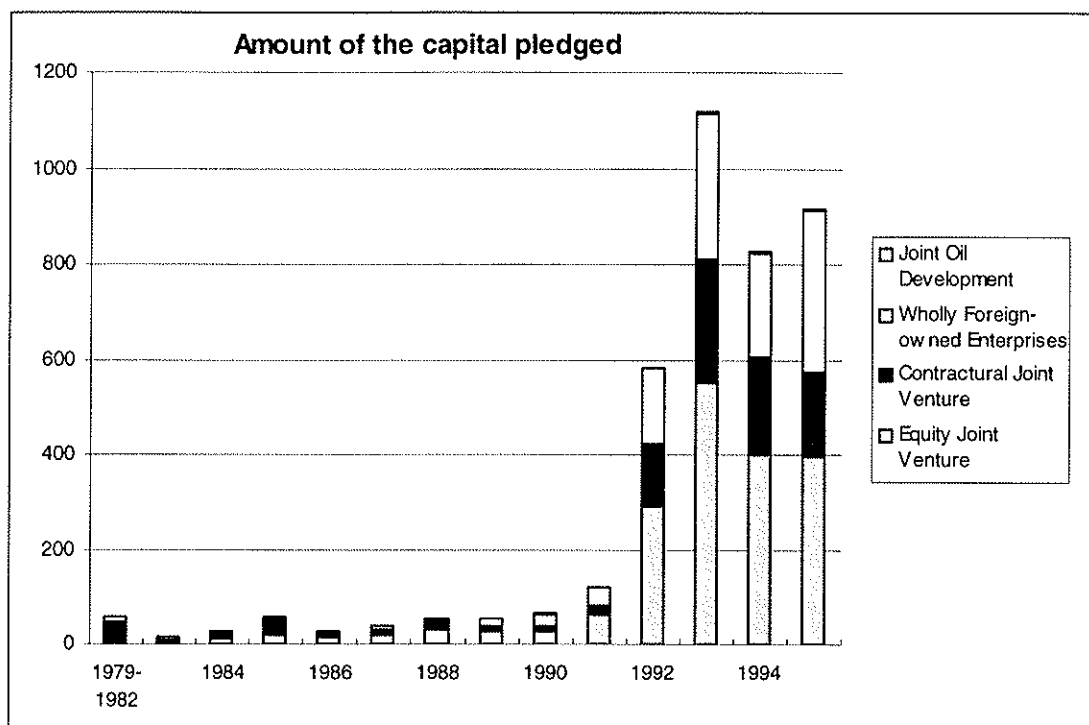
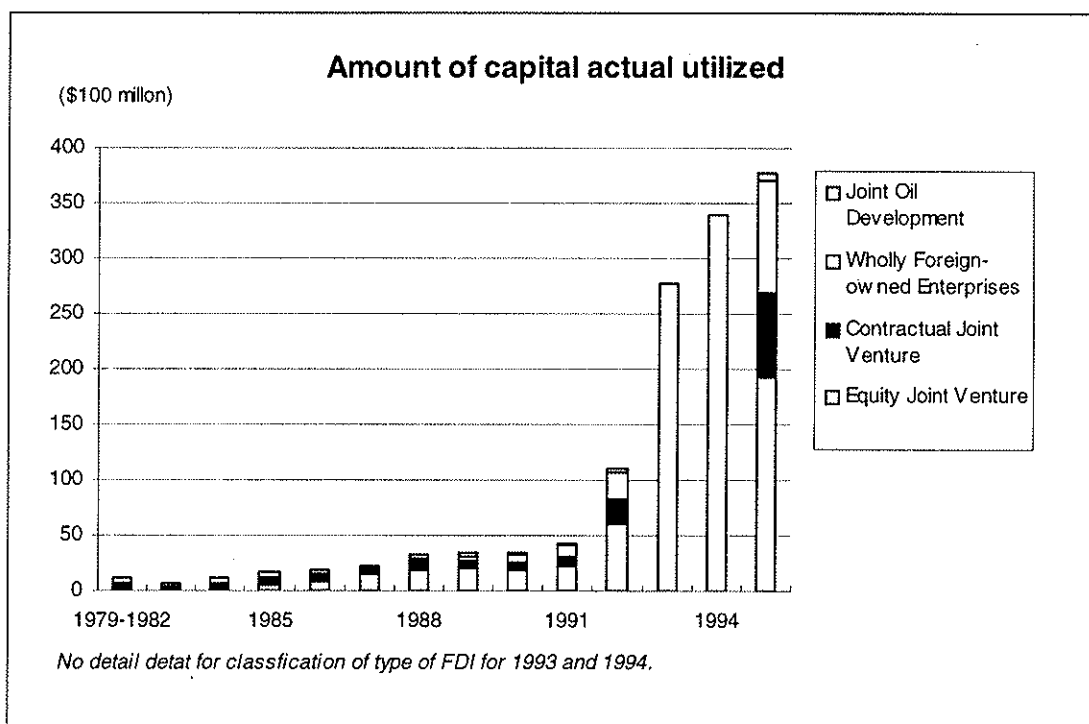


Figure 3.2 Various Forms of FDI - Amount of Capital Actual Utilized



This huge population a tremendous potential of labor force on the supply side. Table 3.5 provides the major information.

(1) Population in 1995: 1211.2 million, in 1990 1143.3 million

(2) Population within working age in 1990: 679.0 million

(3) The key potential aspect of human resource is the absolute number of the professionals

Table 3.5 Sectoral Employment 1995

Sector	No. of Employees (10 ⁴ person)	Share of Total (%)
Primary	33018	52.9
Secondary	14315	23
Tertiary	15055	24.1

Table 3.6 Scientific and Technical Personnel in State Owned Units

Year	Total	Engineering	Agriculture	Health care	Scientific Research	Teaching
1978-6.30	4345000	1571000	294000	1276000	310000	894000
1 995	19133834	5625850	535731	3035335	302879	9634039

It can be seen from table 3.6 that the scientific and technical personnel in state owned enterprises reached 19133834 in number, which is 7.3% 15.3%, 23.4% and 33.5% respectively of the total number of population in U.S.A., Japan, Germany and France.

There is also rich reserve of the human resource. China has 1054 colleges with new student enrollment of 926000 persons each year, with student enrollment of 2.9 million in 1995. The middle school is 95216 in number, with new student enrollment of 23.5 million and student enrollment around 61.9 million persons in 1995.

There is a large capital stock. In 1995, the total assets of industrial enterprises with independent accounting reached 7.92 trillion yuan, there is also a large assets in the financial sector.

3.05 Problems to be Faced in Long Term Growth

Although China has already established a foundation of long term growth, but there are several problems or challenges to be faced in long term growth. Some problems can be overcome in an integrated global economy, for example, the constraints of natural resource, in a modern world of open economy, the resource can be overcome through a sound global trading system. Some problems faced in development and re-

form process have to be solved through better development strategy and policies and measures for further reform. The problems will be grouped as follows:

1. Problems due to constraints of natural endowments

Although China is known for its abundant endowment of natural resources, but due to its huge population, the per capita natural resource and the quality of natural resource is poor. Among the natural resource endowments, three types of resources will have some impacts on development and must be handled properly:

(1) Land resource

China has limited land resource per capital the arable land in 1995 is 94.97 million hectares, with per capita arable land 0.0078 hec. In 1995, the persons engaged in agricultural activity is 323.35 million with per capita land of 0.029 hectare. The population will reach around 1.54 billion or more by the year 2070, therefore, the conflict between population and limited land will become more serious in long term. It had once even raised a debate internationally on the food supply of China in coming century. China can feed herself through all means, but this is an issue must be focused.

(2) The water resource

China is a country which has low per capita available water resource. In 1989, the average per capita renewable water resources is 4600 cubic meters per year in the ESCAP region, while China has only 2520 cubic meters per year. Parts of China suffer from water shortage primarily due to high population density.

(3) The Energy Resource

The energy resource problems can be described by reference of table 3.5. It can be seen from table 3.5 there is decrease of average annual growth rate of energy production and consumption; coal plays a dominant role in the structure of energy production and consumption due to the rich coal reserve in China; although China is reported to have rich hydro-energy resource, but its share in production and consumption is around 6% only; the consumption of crude oil is higher than the demand due to resource limitation.

Therefore, the long term energy issue are: the growth of energy industry cannot cope with the growth of the national economy. The average annual growth rate of GDP is around 9.8% from 1978 to 1995 while the growth rate of primary energy is only 4.9%. It can also be found that in 1994, the average energy consumption for low, middle, and high income countries are 384 kg, 1593kg and 5168kg oil equivalent, and China has per capita energy consumption around 641kg/capita in 1994. If China is going to achieve the target to the level of mid-development countries, its per capita energy consumption should reach 1593 kg, which is at least 2.5 times of its current per capita consumption; China also has a high energy intensity per unit of GDP.

Even PPP is used for the measurement of the economy, China's energy intensity will be around 1.86 times of OECD countries. Low grade of energy is also a cause of low energy and production efficiency. Coal to be a dominant energy resource also creates serious environment issues and harmful to sustainable development.

Table 3.5 Structure of Energy production and Consumption

Year	Energy Production						Energy Consumption					
	Total (10 ⁴ Ton SCE)	Average Annual Growth Rate %	% Share of Total				Total (10 ⁴ Ton SCE)	Average Annual Growth Rate %	% Share of Total			
			Coal	Crude oil	Natural Gas	Hydro Power			Coal	Crude oil	Natural Gas	Hydro Power
1952	4871		96.7	1.3		2.0						
1957	9861		94.9	2.1	0.1	2.9	96.44		92.3	4.6	0.1	3.0
1980	63735		69.4	23.8	3.0	3.8	60275		72.2	20.7	3.1	4.0
1995	128728		75.5	16.7	1.8	6.0	129000		75.0	17.3	1.8	5.9
1952- 1957		15.1										
1957- 1980		8.5						8.3				
1980- 1995		4.8						5.2				

Source: Derived from: China Statistical Yearbook 1996
China Statistical Publishing House

2. Institutional Problems

China had followed the Central planning system before 1978, all organizations and institutions were organized based upon central plan. There is nearly no private property, all enterprises were state owned or collectively owned, there was no financial market, no factor market, the price is set up by the governments etc. Throughout the reform around eighteen years, the market mechanism is established partially. It is also a well known fact that a fair part of state owned enterprises is at a loss, but bankruptcy of enterprises are difficult to be implemented due to the social security system had not been widely established yet. Most of the price has been liberalized, the banking sector is undergoing reform, the former specialized banks are transformed into commercial banks only recently. The government is put full effort to reform the state owned enterprises as a priority program in the reform agenda. But it should foresee the fact that risks are involved in the reform process. China had been successful in the implementation of reform and opening through a gradual approach. Due to the incomplete reform of the state owned enterprise, science and technology, China cannot compete internationally on the high technology products. In a trend of increasing integration of the global economy, whether the Chinese enterprises can enhance their capability of competitiveness will be a major challenge faced by China.

3. Population and Employment Pressure

It is described above that China has the potential of rich labor force, but this is a factor of duality. Due to the large number of population engaged in the rural economic activity, and arable land per capita is limited, there is serious burden to provide employment. On the one side, there will be a large number of population entering into the working age, on the other side there is need to transfer surplus labor force in the primary sector to other economic activities. The Town and Village enterprises had transferred around 100 million of labor force from the agricultural sector to industrial and commercial activities since the launch of economic reform to present. But there is limit to this transfer. Because there is also the need to upgrade the productivity and efficiencies of TVEs. It is planned in the Ninth Five Plan that there will be new employment of around 40 million persons, and additional 40 million rural labor force will be transferred to non-farming activity. It is also reported that by the end of 1996, the registered unemployment is 5.53 million persons, the unemployment rate is 3%. There is around 22 million of surplus labor force of the enterprises to be redeployed, and there is 130 million of surplus labor force in the rural area to be arranged. This will be a major problem faced in long term development.

4. Regional Disparity

Although China had been successful to achieve a high economic growth performance since late 70's, although all regions and provinces had enjoyed the benefit of growth. But regional disparities increased due to different growth rate of different provinces. This fact can be shown in table 3.6.

Table 3.6 Comparison of per capita GDP of coastal opening province and Selected inland province

Per Capita GDP	Liaoning	Hebei	Shandong	Jiangsu	Shanghai	Zhejiang	Fujian	Guandong
1980	768	427	405.3	544	2738	468	343	472.5
1994	6103	3376	4473	5785	15204	6149	5386	6380
Growth Rate 1980-1994 (%)	15.96	15.92	18.71	18.39	13.02	20.2	21.74	20.43
Per Capita GDP	Henna	Hubei	Shanxi	Jiangxi	Shaanxi	Gansu	Guizhou	Sichuan
1980	317	428	437	342	437	388	219	315
1994	2475	3341	2819	2376	2819	1925	1553	2516
Growth Rate 1980-1994 (%)	15.8	15.8	14.24	14.85	14.24	12.12	15.0	16.0

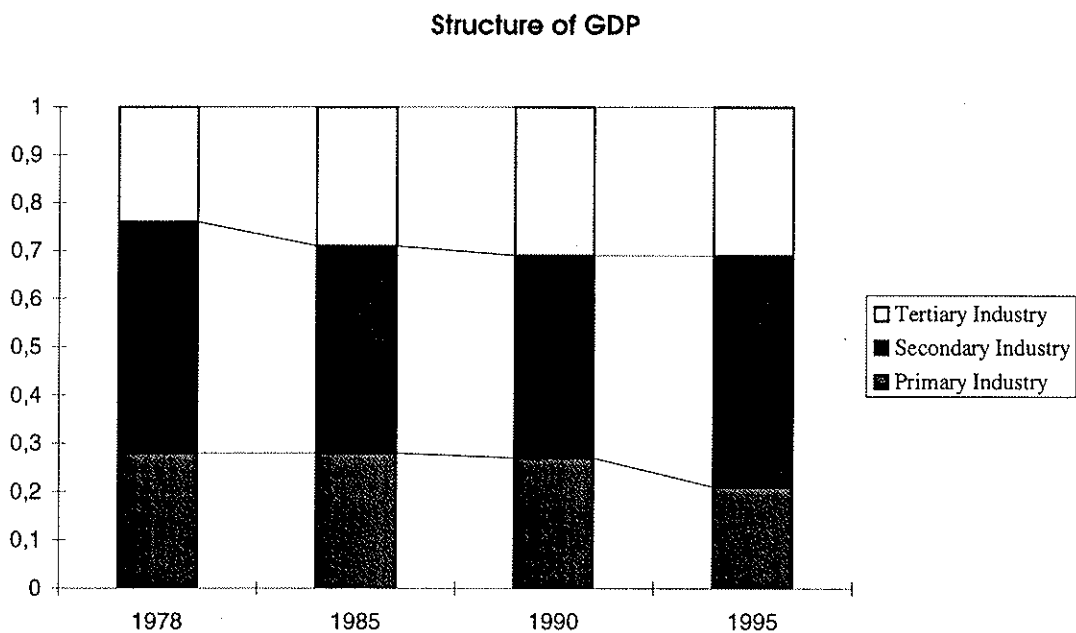
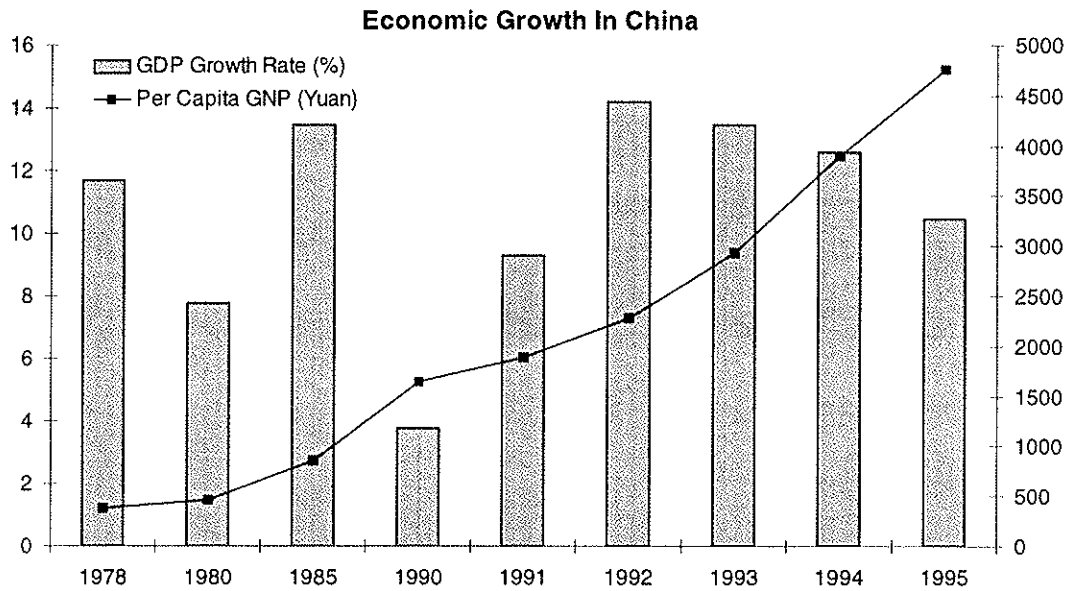
It is pointed out in the governmental report that it is necessary to gradually narrow the gap of development between regions by ensuring coordinated development of the regional economies. Beginning with the Ninth Five Year Plan period greater attention will be paid to supporting development of inland area, carry out policies which can help to slow the widening trend and gradually increase the intensity of the efforts in this regards.

5. Sustainable Development

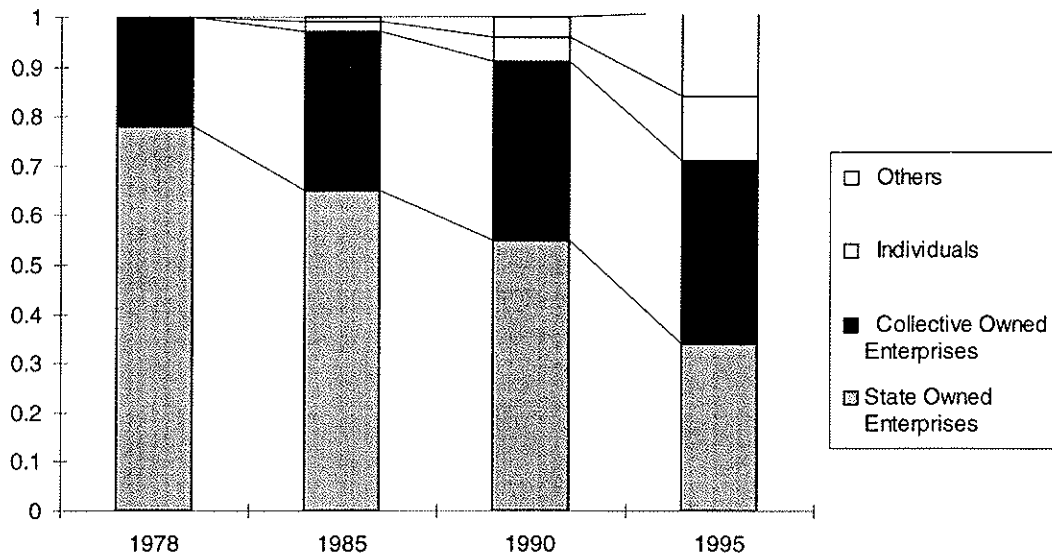
China had prepared an official document: China Agenda 21 in 1994. Sustainable development is advocated. But the dominant share of coal in production and consumption does have some negative impact to sustainable development.

Appendix

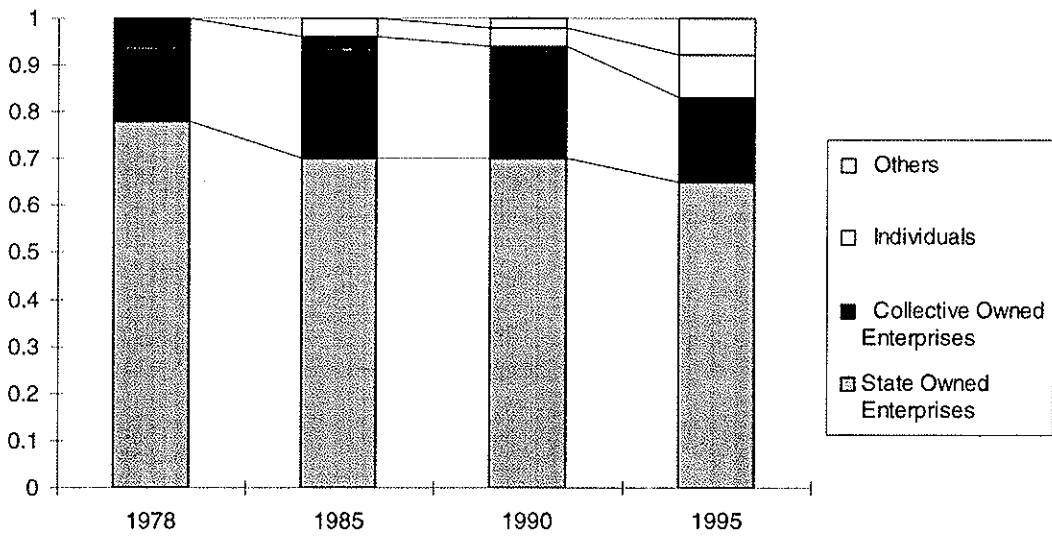
This appendix gives pictorial description of tables in part I. Appendix x will facilitate to analyze the influence of consumption, investment on GDP and CPI. Appendix xi shows the effect of agriculture and industry to GDP. Appendix xii presents the effect of agriculture and industry to National income since 1953.



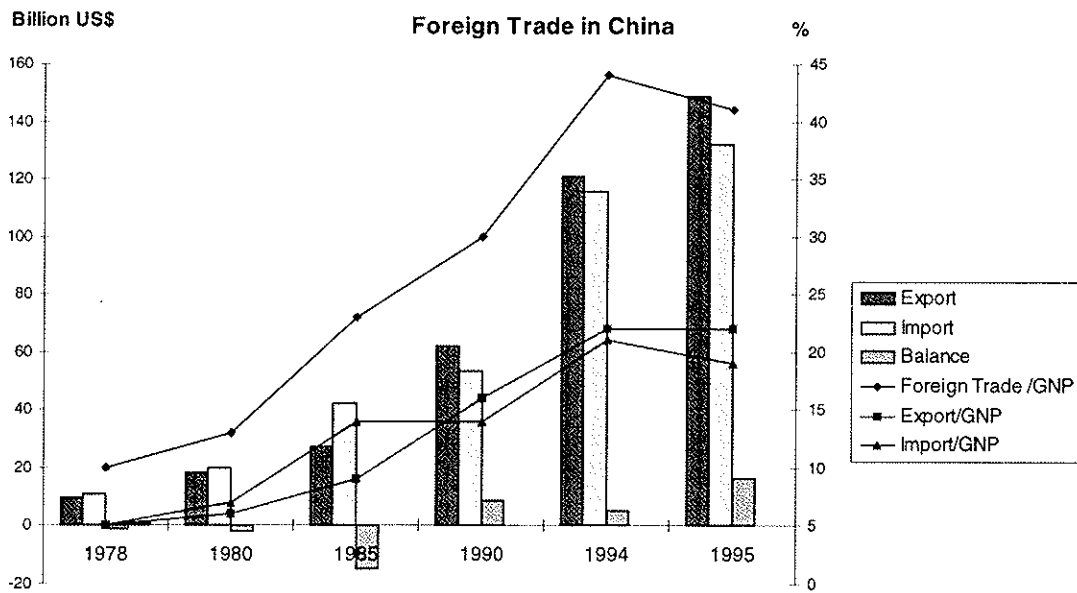
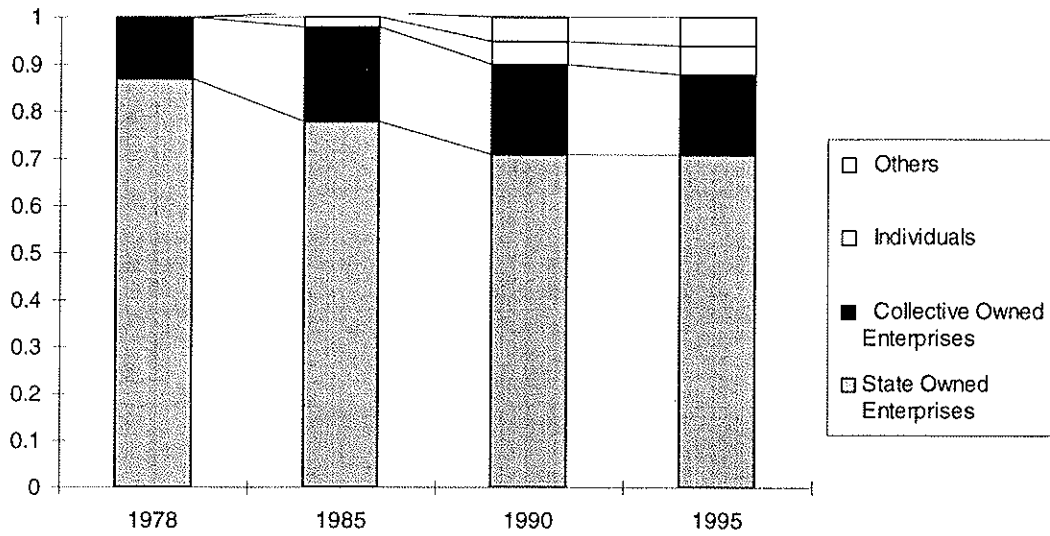
Structure of Gross Output Value of Industry By Ownership

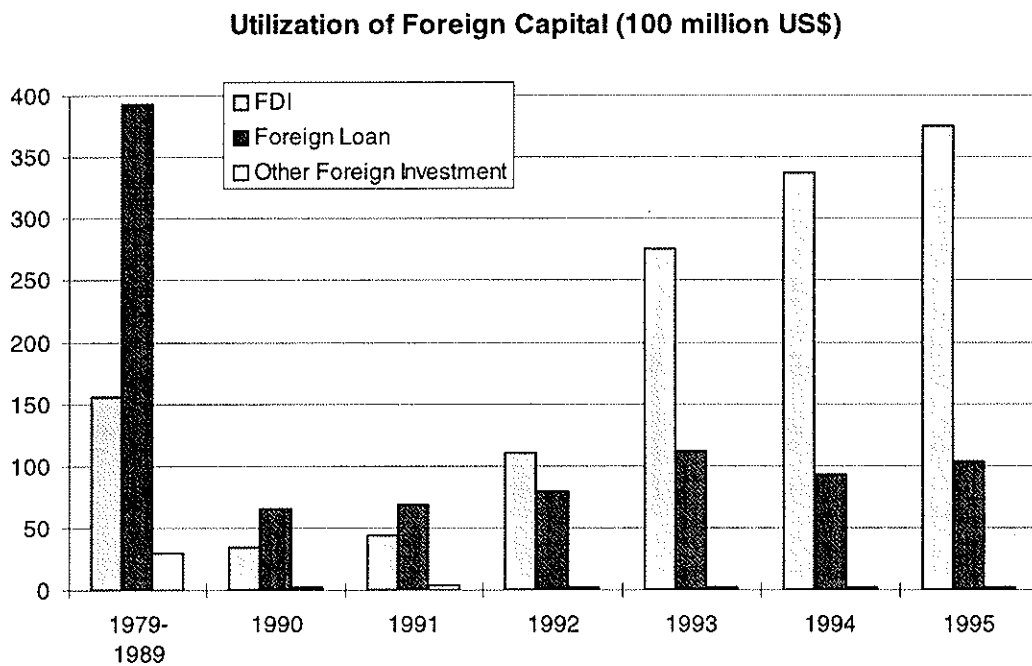
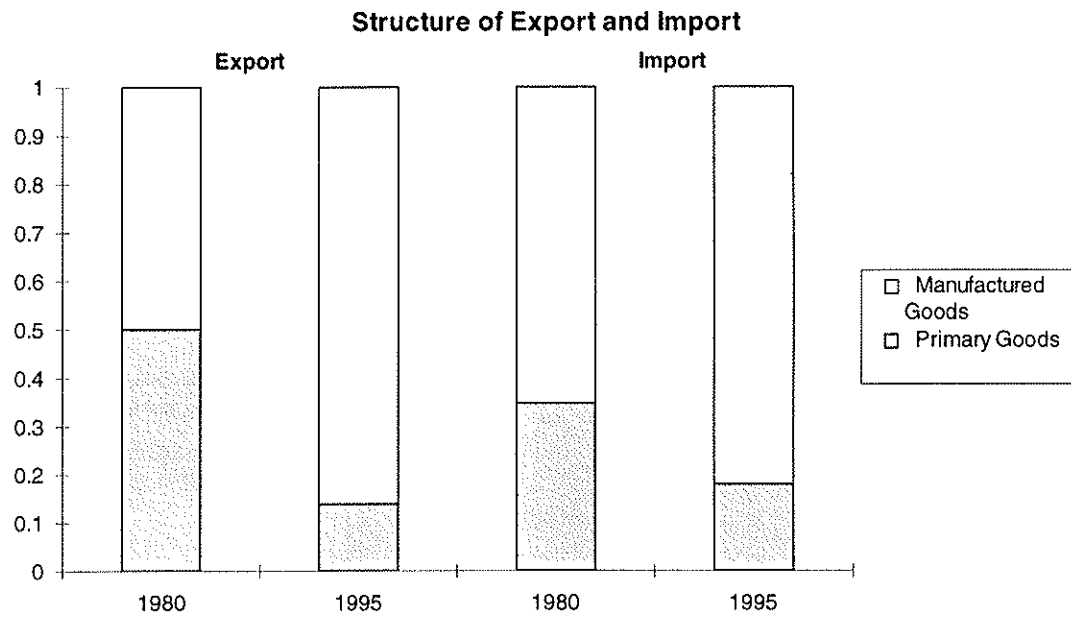


Structure of Urban Employment by Ownership

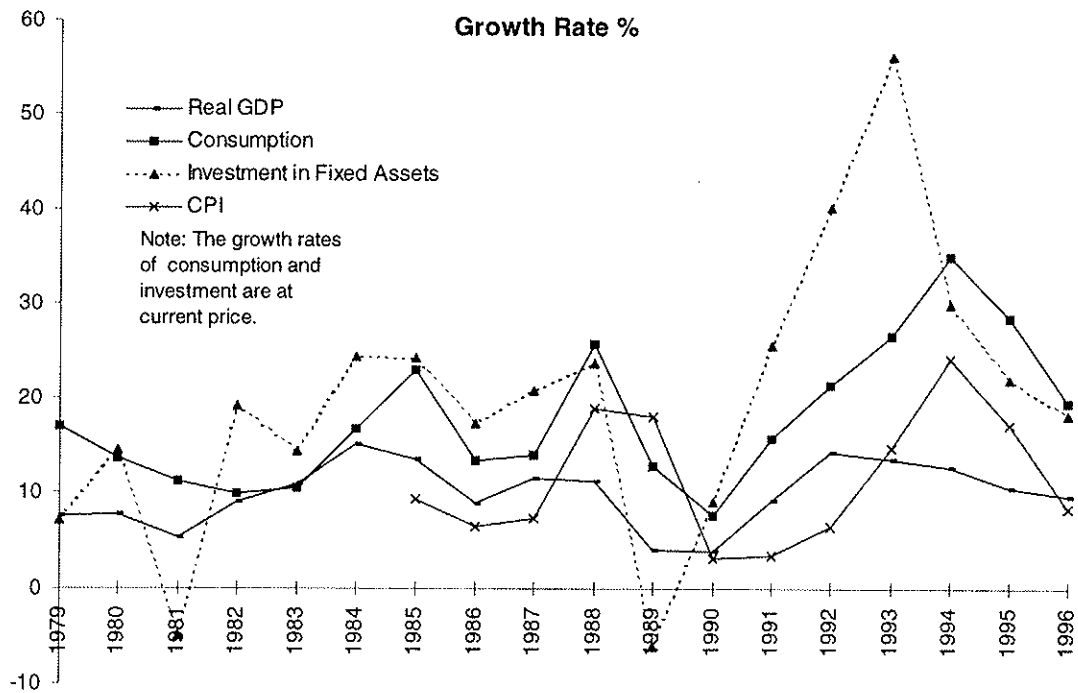
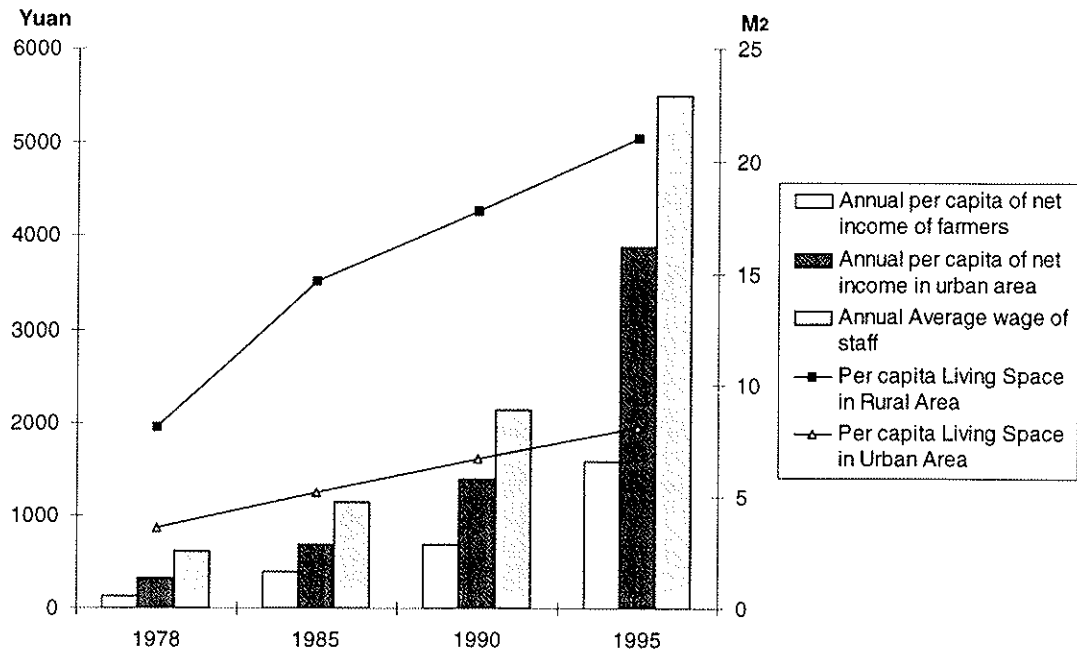


Government Revenue by Ownership

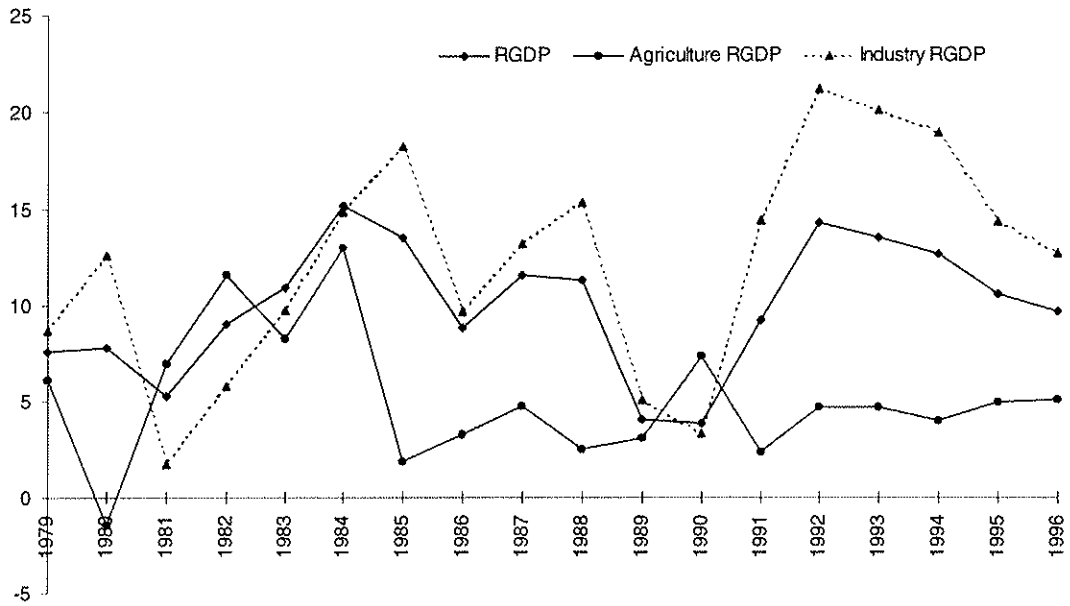




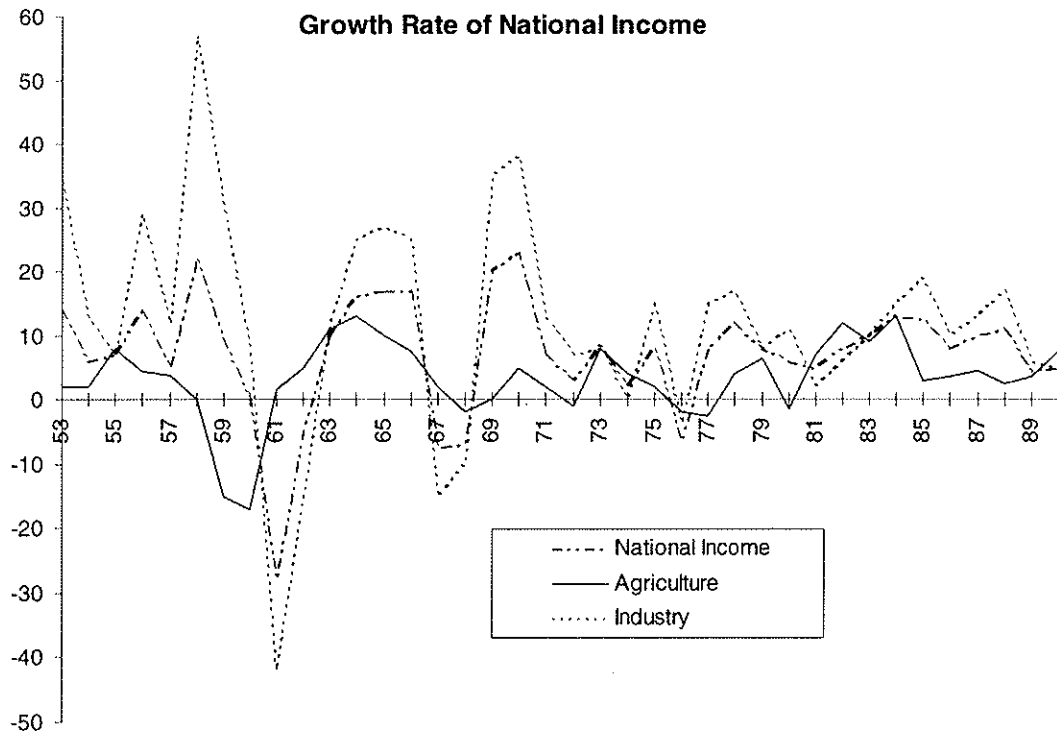
Improvement of Living Standard



Growth Rate of Real GDP



Growth Rate of National Income



ELINKEINOELÄMÄN TUTKIMUSLAITOS (ETLA)
THE RESEARCH INSTITUTE OF THE FINNISH ECONOMY
LÖNNROTINKATU 4 B, FIN-00120 HELSINKI

Puh./Tel. (09) 609 900
Int. 358-9-609 900
<http://www.etla.fi>

Telefax (09) 601753
Int. 358-9-601 753

KESKUSTELUAIHEITA - DISCUSSION PAPERS ISSN 0781-6847

- No 593 PEKKA VISURI, Baltian maiden turvallisuuspoliittinen asema. 11.04.1997. 42 s.
- No 594 TARMO VALKONEN, Corporate Taxation and Investment Finance in Finland: A General Equilibrium View. 23.04.1997. 32 p.
- No 595 VESA KANNIAINEN, Empire Building by Corporate Managers: Corporation as a Savings Instrument. 30.04.1997. 24 p.
- No 596 SYNNÖVE VUORI, Alternative Ways of Measuring Technology Spillovers - Results with Finnish Data. 30.04.1997. 25 p.
- No 597 ERKKI KOSKELA - MARKKU OLLIKAINEN, Optimal Design of Forest and Capital Income Taxation in an Economy with an Austrian Sector. 13.05.1997. 26 p.
- No 598 KNUT A. MAGNUSSEN - METTE ROLLAND, The European Economy. Medium-term perspectives. 20.05.1997. 22 p.
- No 599 RIIKKA KIVIMÄKI, Family Life and Working Life Colouring and Structuring Each Other. Case Examples. 21.05.1997. 15 p.
- No 600 HEATHER JOSHI - PIERELLA PACI, Wage Differentials between Men and Women: Evidence from British Birth Cohort Studies. 21.05.1997. 13 p.
- No 601 JUKKA LASSILA - HEIKKI PALM - TARMO VALKONEN, FOG: Suomen kansantalouden limittäisten sukupolvien malli. 21.05.1997. 83 s.
- No 602 JOUKO NÄTTI, Atypical Employment and Gender in Finland. 02.06.1997. 33 p.
- No 603 MIKA MALIRANTA, The Determinants of Aggregate Productivity, The Evolution of micro-structures and productivity within plants in Finnish manufacturing from 1975 to 1994. 09.06.1997. 38 p.
- No 604 DAN STEINBOCK, The Competitive Advantage of Finland: The Primary Research Projects. 11.06.1997. 41 p.
- No 605 MARKKU KOTILAINEN, Construction in the Nordic Countries. 13.06.1997. 27 p.
- No 606 REIJA LILJA, Similar Education - Different Career and Wages? 30.06.1997. 38 p.

- No 607 RITA ASPLUND, Private vs. Public Sector Returns to Human Capital in Finland. 08.08.1997. 68 p.
- No 608 PETRI ROUVINEN, Suomi - Euroopan kilpailukykyisin? 08.08.1997. 9 s.
- No 609 AIJA LEIPONEN, Yritysten osaamisintensiivisyys ja kansainvälistyminen. 08.08.1997. 27 s.
- No 610 MIKA PAJARINEN, Ulkomaiset suorat sijoitukset ja ulkomaalaisomistus Suomessa: katsaus historiaan ja viimeaikaiseen kehitykseen. 19.08.1997. 48 s.
- No 611 JYRKI RUUTU, Suomalainen työehtosopimusjärjestelmä, palkat ja inflaatio. 20.08.1997. 44 s.
- No 612 MIKA MALIRANTA, Plant Productivity in Finnish Manufacturing. Characteristics of high productivity plants. 22.08.1997. 43 p.
- No 613 PETRI ROUVINEN - PEKKA YLÄ-ANTTILA, Konkurrenskraften i Norden. 08.09.1997. 21 s.
- No 614 HANNU HERNESNIEMI, Toimialojen tuotannon kasvun työllisyysvaikutukset Suomessa vuosina 1980 - 1996. 09.09.1997. 31 s.
- No 615 ATRO MÄKILÄ, Elintarviketeollisuuden osaamistarpeiden ennakointi - kyselytutkimus. 19.09.1997. 41 s.
- No 616 SEPPO LAAKSO, Asuntojen hinnat ja asuntojen ominaisuuksien kysyntä pääkaupunkiseudun asuntomarkkinoilla. 22.09.1997. 16 s.
- No 617 ELISABETH HELANDER, Finland's Research Clusters: Important Assets for a New Member of The European Union. 25.09.1997. 10 p.
- No 618 ATRO MÄKILÄ, Vakuutusyhtiöiden osaamistarpeiden ennakointi - kyselytutkimus. 30.09.1997. 28 s.
- No 619 RITA ASPLUND, The Disappearing Wage Premium of Computer Skills. 03.10.1997. 22 p.
- No 620 ERKKI KOSKELA - MARKKU OLLIKAINEN, Optimal Public Harvesting in an Economy with Multiple-use Forestry. 13.10.1997. 26 p.
- No 621 WANG HUIJIONG - LI SHANTONG, Prospects and Problems of China's Economy. 06.10.1997. 38 p.

Elinkeinoelämän Tutkimuslaitoksen julkaisemat "Keskusteluaiheet" ovat raportteja alustavista tutkimustuloksista ja väliraportteja tekeillä olevista tutkimuksista. Tässä sarjassa julkaistuja monisteita on mahdollista ostaa Taloustieto Oy:stä kopiointi- ja toimituskuluja vastaavaan hintaan.

Papers in this series are reports on preliminary research results and on studies in progress. They are sold by Taloustieto Oy for a nominal fee covering copying and postage costs.

d:\ratapalo\DP-julk.sam\06.10.1997