

OVERVIEW AND RECENT DEVELOPMENTS

China's economy is essentially centrally planned although the private sector is gaining in importance. Since 1953 the Chinese government has regulated economic development through the adoption of a series of five-year plans. Apart from setbacks experienced during the Great Leap Forward, launched by Mao Zedong in 1958 to accelerate economic development, and the Cultural Revolution, launched in 1966 with the aim of re-establishing socialist ideals, China's five-year plans appear to have been implemented without major disruption.

Following the death of Mao Zedong in 1976, more pragmatic, less interventionist policies were adopted. In 1978, the Chinese government initiated a series of economic reforms, the aim of which was to decentralize the economic structure of China, giving greater autonomy to enterprises, farmers and localities, according a larger role to markets and opening the domestic economy to the outside world. Encouraged by the success of these initial reforms, the State Commission for Restructuring the Economic System was formed in 1982 with Zhao Ziyang as Chairman. Zhao Ziyang announced that China would create a "socialist economy with Chinese characteristics". The central government set itself the aim of quadrupling the 1980 gross agricultural and industrial output value by the year 2000. The focus of its reform programme was switched to industry in 1984. Wide-ranging reforms have been introduced to make the industrial sector more efficient by narrowing the scope of central planning and broadening enterprise's decision-making, material incentives and the role of the market.

Between 1979 and 1988, with an average annual growth rate of 9.6 percent, real gross national product ("GNP") more than doubled, while real personal consumption per capita increased at an average annual rate of 7.8 percent. In each of 1987 and 1988, China experienced growth of approximately 11 percent. However, such rapid economic growth was accompanied by macro-economic imbalances and high inflation, which led to a period of readjustment from the end of 1988. A comprehensive austerity program was implemented with the primary goal of curbing inflation and cooling the overheated economy. Economic stabilisation was by and large attained and inflation was substantially reduced by the last quarter of 1989, although GNP growth declined. In 1990, efforts were made to rejuvenate the economy by loosening investment and credit controls. As a result, the Chinese economy staged a strong recovery in 1991, with a growth in GNP of 7 percent, and a GNP growth of 12.8 percent in 1992. A marked recovery in industrial output and continued strong export growth were both important factors contributing to this improvement. Growth in agricultural production slowed in 1991, largely due to natural disasters. The revised Eighth Five-Year Plan (1991-1996) has set a target of GNP growth of 8 to 9 percent per annum, increased from the 6 percent per annum growth rate set originally.

Recently, evidence of further commitment by the central government to economic reform has focussed attention on China and is expected to further spur foreign investment.

		Major Economic Indicators					
		1987	1988	1989	1990	1991	1992+
Gross National Product	<i>% change</i>	11.0	10.8	4.0	5.2	7.5	12.8
Agriculture	<i>% change</i>	5.8	3.9	3.1	7.6	3.0	4.0
Industry	<i>% change</i>	17.7	20.8	8.5	7.8	14.0	20.8
Gross Domestic Investment	<i>% GNP</i>	37.2	38.4	37.6	35.1	39.4	37.0
Gross Domestic Saving	<i>% GNP</i>	35.9	36.3	36.0	37.3	40.3	38.2
Resource Gap	<i>% GNP</i>	-1.3	-2.1	-1.6	2.2	-0.9	1.2
Inflation Rate	<i>% change in PRI*</i>	8.8	18.5	17.8	2.1	3.0	10.9

APPENDIX II GENERAL INFORMATION ON THE CHINESE ECONOMY

		Major Economic Indicators					
		1987	1988	1989	1990	1991	1992+
Merchandise Exports	US\$ billion	34.7	41.1	43.2	51.5	59.2	85.8
	% change	34.9	18.2	5.3	19.2	15.0	18.3
Merchandise Imports	US\$ billion	36.4	46.4	48.8	42.4	50.0	80.6
	% change	4.3	27.4	5.3	-13.3	18.0	26.3
Trade Balance	US\$ billion	-1.7	-5.3	-5.6	9.1	9.2	5.2
Current Account Balance	US\$ billion	0.3	-3.8	-4.3	12.0	12.2	11.5
	% of GNP	0.1	-0.9	-1.0	3.2	3.3	2.1
External Debt	US\$ billion	35.4	42.4	44.8	52.6	55.5	58.5
Debt-Service Ratio	%	9.5	8.6	9.8	10.3	12.0	8.5
Exchange Rate (annual average)	RMB per US\$	3.7	3.7	3.8	4.8	5.4	5.4

* % change in CPI for 1988

Source: Asian Development Bank, derived from People's Republic of China, State Statistical Bureau, *Statistical Yearbooks of China 1989, 1990 and 1991*; International Monetary Fund, *International Financial Statistics (December 1989, January 1991, February 1992 and February 1993)*; *World Debt Tables, 1989-90 Vol. 2, 1990-91 Vol. 2 and 1991-92 Vol. 2, and 1992-93 Vol. 2*.

Source (+): *China Monthly Statistics 1993, Asian Monetary Monitor 1993, China Economic News 1993, China Trade Report 1993, Asian Development Outlook 1992*.

INDUSTRY

China's economy is divided into three sectors: the state sector, the collective sector and the private sector (which comprises the individual and foreign-invested enterprises sectors).

The state sector has been the largest contributor to industrial output, but is declining in importance. It is characterised by low efficiency which is exemplified by large stockpiles of unsold goods and large portfolios of bad debts. The central government has introduced a number of measures to increase efficiency of the large- and medium-sized state enterprises, which have led to the closure of a number of state-owned enterprises.

Conversely, one of the most notable features of the economic reform process in China over the past decade has been the rapid expansion of the non-state economy. This includes collective and private enterprises, as well as foreign and domestic joint ventures between state and collective enterprises, and between state and private enterprises. In 1992, an estimated 61 percent of GNP originated in this sector compared with 49 percent in 1978, when economic reforms were first introduced.

Non-state enterprises were quick to reap the benefits of the dismantling of the country's rigid central planning controls. In the industrial sector, over the decade to 1993, the average annual output growth of non-state enterprises was 63.6 percent, with collective enterprises growing at 42.4 percent and private enterprises at 21.2 percent, as compared to the 8.7 percent growth of the state industrial sector. Moreover, in 1991, approximately 464 million people or 82 percent of the total labour force were employed by the non-state economy, which was also responsible for approximately 21.9 percent of total fixed investment in China.

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In particular, there has been extremely rapid growth in the foreign-invested enterprises sector. Foreign investment has been encouraged by the creation of special areas or zones, generally situated in the coastal provinces whose general aim is to attract foreign investment and technology by offering a variety of investment incentives, including preferential tax treatment, to foreign businesses. Further information concerning these areas is contained in the Special Investment Areas section below.

After contracting sharply in 1989 due to the austerity program introduced at the end of 1988, the rate of growth of industrial production began to improve late in 1990 reaching an estimated 22.4 percent in the first quarter of 1993. A liberal supply of bank credit as well as increases in fixed asset investments were the main reasons for this resumption of industrial growth, which was supported by an increase in retail sales of 15.7 percent and continued strong export demand. The mainspring of this resurgence of industrial output was non state-owned enterprises. Since the initiation of economic reforms in 1978, the non-state share of gross industrial output has increased from 22 percent to a current level of approximately 61 percent. Whereas economic recession during 1989 and 1990 did not engender significant improvement in the efficiency of the state sector, it did have a significant impact on the non-state sector, with more than two million inefficient town and village enterprises being closed down after 1989.

The more efficient and competitive enterprises that remained, as well as the newly established enterprises, were thus well-placed to take advantage of an improvement in the economic environment. In 1992, the output of collective enterprises in the non-state sector grew by 28.5 percent while the remainder of the non-state sector grew by 48.8 percent. In comparison, the state sector, characterised by low efficiency, grew by only 14.4 percent.

	Growth in industrial output (%)							March
	1986	1987	1988	1989	1990	1991	1992+	1993+
Industrial Output	11.1	16.5	20.7	8.3	7.6	14.2	20.8	22.4
(1)By Industry								
– Light Industry	12.7	16.8	22.6	8.4	9.1	14.5	20.9	18.3
– Heavy Industry	9.6	16.0	18.8	8.2	6.0	13.9	20.7	26.3
(2)By Sector								
– State-owned	6.2	11.0	12.7	3.7	2.9	8.4	14.4	8.7
– Collective	16.7	25.0	28.8	10.7	9.1	18.0	28.5	42.7
– Rural	–	–	35.0	12.7	12.5	25.5	} 48.8	} 63.6
– Individual	60.6	48.0	46.0	24.1	21.6	24.0		
– Foreign-invested	34.3	98.0	97.0	44.7	56.0	55.8		

Source: State Statistical Bureau of China

Source (+): China Economic News, March, May 1993; China Trade Report, April 1993; Economic Reporter No 5, 1993.

MONETARY POLICY AND INFLATION

Following the austerity program introduced at the end of 1988, the central government has, since the second quarter of 1990, adopted an expansionary monetary policy in order to stimulate the economy. The relief program in the aftermath of the disastrous floods in the summer of 1991 and a rapid build-up of foreign exchange reserves have also contributed to strong money supply growth. Nevertheless, the impact of credit expansion has been greatly reduced, to a large extent because a large proportion of the credit has been used to finance the growing stock piles of unsold goods which, for the most part, were held by state enterprises.

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As the economic expansion gathers momentum, inflation has again become a growing concern. Although the national retail price index (which relates to the country as a whole) showed an increase of about 9 percent in 1992, that figure masked much higher inflation in particular areas. The cost of living index in 35 major cities, for example, rose by 10.9 percent in 1992 and 15.7 percent in February, 1993. In the big cities, such as Beijing, Shanghai and Tianjin, double-digit inflation emerged. However, while fast economic growth contributed to the high inflation, many one-time price adjustments of commodities and consumables were also responsible.

EXPORTS AND IMPORTS

The external sector of the Chinese economy remained strong in 1992. Export growth at 18.3 percent was slightly higher than in 1991. Imports were 26.3 percent greater than in 1991. The overall result in 1992 was a trade surplus of US\$5.2 billion.

New measures, such as granting permission to trading organizations to retain a higher proportion of foreign exchange earnings, provided further incentives for trading companies and local governments to expand their exports. In addition, the more than 25 percent depreciation in the Chinese currency over the past four years improved the competitiveness of Chinese goods in world markets. Most importantly, however, China has successfully built an export-oriented industrial complex in the southeastern coastal region. Chinese products are presently marketed through trade and business connections in Hong Kong, and increasingly, in Taiwan, as well as through the networks of foreign partners in joint ventures. The rapid expansion of export-oriented industry has been a major reason for the sustained export performance of recent years.

The substantial recovery of imports in 1991 and 1992 was, in part, due to the relaxation of import controls, although the main impetus came from recovery of the domestic economy. The economic recovery led to an increased demand for imports, particularly machinery, transport equipment and raw materials. Net invisible receipts, including improved earnings from tourism, were slightly higher than the 1991 figures.

FOREIGN EXCHANGE RESERVES AND DEBT

China's foreign exchange reserves are now estimated at US\$45.23 billion at the end of September 1992. While the rapid growth of foreign reserves strengthened China's external debt position, there is growing concern about the high opportunity cost of holding very large amounts of foreign reserves. External debt was estimated (Asiaweek) to be US\$60.5 billion in June 1993.

FOREIGN INVESTMENT

Since the introduction of the open door policy in 1978, the central government has actively encouraged foreign investment in China. In 1992, China approved foreign-funded projects with contracted investment standing at US\$57.5 billion, which represents a 3.8 fold increase over the 1991 figures. The growth in contracted foreign investment averaged 33.7 percent per year during the period 1987 to 1991. The slowest growth of 6 percent was registered in 1989 after the Tiananmen Square unrest.

The central government has successfully implemented a number of policies to stimulate foreign investment, most notable the incentives associated with investment in designated special cities and areas. The government has also begun leasing land on a long-term basis of up to 70 years in designated areas, including the special economic zones.

In 1992, over 84,000 foreign-funded enterprises were approved by Chinese officials. The value of the foreign investment projects is estimated to be US\$178.46 billion.

FOREIGN EXCHANGE ADJUSTMENT CENTRES

A most fundamental development in the field of foreign investment has been the granting of permission to foreign investors to trade RMB or foreign exchange for legitimate use. The regulations granting such permission were quickly given practical force with the setting up of foreign exchange adjustment centres in most cities throughout the country. Initially, the activities of the centres were confined to transactions between foreign-invested enterprises, but as the centres proved to be highly successful and effective, the restrictions were gradually relaxed to allow state enterprises, and later, individuals to participate in foreign exchange swap transactions. The adjustment centres provide an official forum where foreign enterprises can swap their RMB profits for foreign exchange or swap foreign exchange for RMB to pay local expenses.