

## CHINA

## 2002: A REMARKABLE YEAR

Against poorer-than-expected world economic recovery, China's economic growth in 2002 in real terms was 8 per cent, 0.7 percentage points higher than 2001. More significant is the accelerating quarterly growth trend, in contrast to the situation in 2001.

In 2001, China's exports lost steam and the rate of growth declined sharply. But in 2002, China's exports surged again, rising by 22.3 per cent. This robust growth was supported by global economic recovery, the RMB's relative depreciation, which increased the competitiveness of Chinese exports, and the effect of China's entry into the World Trade Organization (WTO). The private sector played for the first time a very active role in exports in 2002.

Import growth also rose strongly, from 8.2 per cent in 2001 to 21.2 per cent in 2002. But the merchandise trade surplus stood at US\$30 billion.

Investment in fixed assets grew by 16 per cent, the highest pace since 1996. Collective and individual investment also accelerated in 2002, at 11.8 and 15.7 per cent respectively. Meanwhile, encouraged by its WTO entry and robust development, China surpassed the United States for the first time in 2002 as the world's largest recipient of FDI at more than US\$52 billion, a rise of 12.5 per cent. Owing to robust FDI inflows and a higher trade balance, China's foreign reserves built quickly, registering US\$280 billion at the end of 2002.

Total retail sales of consumer goods grew by 10.2 per cent in real terms in 2002, slightly less than in 2001, but both

communication products and vehicle sales showed explosive growth, registering 69.2 and 73 per cent respectively.

After two years of slight inflation in 2000 and 2001, China's CPI went to negative territory again in 2002. The yearly average CPI inflation was -0.8 per cent. In 2002, the prices for consumption goods dropped 0.9 per cent, food prices were down 0.6 per cent, while service prices jumped 1.8 per cent.

Although China enjoyed robust economic growth in 2002, it still faces some serious problems, including worsening unemployment, poor farmer incomes, an inefficient financial system and increasing income disparity.

The most serious challenge facing China is unemployment. According to the Ministry of Labour and Social Security, there are about 7.5 million registered unemployed in cities, but this figure does not count 10 million laid-off workers and 120-150 million surplus rural labourers.

## OUTLOOK FOR 2003

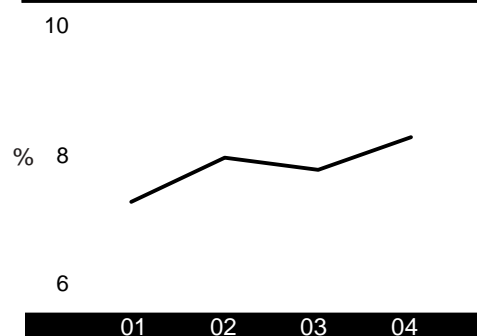
There was a smooth transition of the leadership of the Party at its 16<sup>th</sup> National Congress in 2002 and a new government was put in place in March 2003. The new leaders have vowed to sustain the continuity and stability of macroeconomic policy, to accelerate system reforms and to open further to the world economy.

In 2003, China's economy will grow 7.8 per cent, down a little from 8 per cent in 2002 because of the dampening effect of the SARS epidemic. It will then increase by 8.3 per cent in 2004.

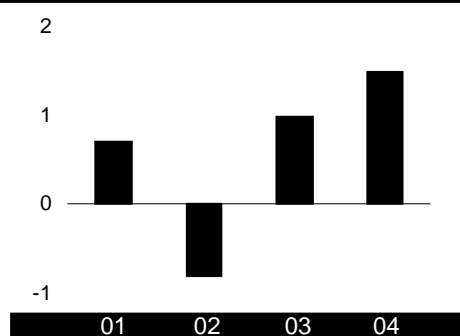
LUO YUNYI and  
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State Development and Planning  
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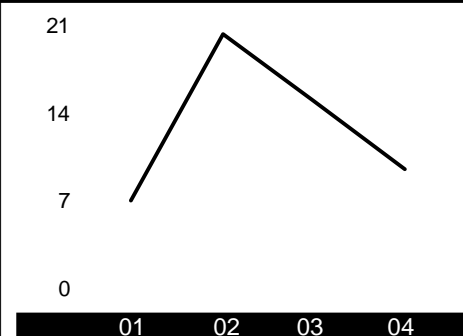
GDP growth



CPI inflation



Export growth



Investment in fixed assets in 2003 is expected to be the major driving force again, growing by 13.2 per cent.

Factors behind this forecast include the newly elected provincial and local governments' enthusiasm for accelerating economic development, the continuing use of debt financing, the government's policy of encouraging development of the private sector, and strong FDI inflow. In first-quarter 2003, FDI increased by 56.7 per cent compared to the same period in 2002.

Property investment, however, may cool somewhat, as PBOC has announced that it will take some measures to prevent a real estate bubble.

Consumption demand in 2003 will remain strong. Supported by the increase in per capita disposable income in urban and rural households (13.4 and 4.8 per cent respectively in 2002), total retail sales of consumer goods have accelerated since September 2002, indicating a stronger rising trend for 2003. Budget injections to the social security fund and a civil servants' salary increase are also expected. For rural households, tax-for-fee reform will further ease the burden on farmers, and farmers' income from non-agricultural activity should soar. All these factors will stimulate consumption, leading to a higher consumption growth rate of 6.1 per cent.

In the auto industry, 2003 is expected to be another boom year.

We expect China's export growth to stay strong. Exports in first-quarter 2003 were 23.6 per cent higher than the same period in 2002. But growth should moderate to 15 per cent over the whole year. This growth will be supported by the strong competitiveness of Chinese-made goods, further liberalisation of

foreign trade, and a better trade environment through quota increases on China's textile exports. The weak US dollar, to which the renminbi is pegged, will also help.

Import growth will exceed export growth in 2003, at 24.4 per cent.

As many multinational companies have moved their production base to China, the 'world's workshop', the demand for processing imports will remain strong.

Overall, net merchandise exports will shrink and the net export contribution to GDP growth should become negative.

Although the CPI fell overall in 2002, it showed moderate rises in the second half of 2002. This was due to rapid growth in the money supply and bank loans, price rises in some industries, especially raw material industries, and also accelerating consumption. China's CPI will increase by 1 per cent in 2003 and 1.5 per cent in 2004.

Creating jobs is one of the most pressing tasks for China's economic managers. The government has vowed to create 9.5 million jobs in 2003 to keep the urban registered unemployment rate below 4.5 per cent, a tough target.

**Fiscal policy.** Amid concern about the gradual accumulation of government debt and crowding-out of private investment, debate about an expansionary fiscal policy has continued. The Chinese government, however, has decided to continue the policy in 2003. Special treasury bond issues will be kept at almost the same level as in 2002. To reduce the farmers' financial burden, reforms to agricultural taxes and administrative fees are being considered.

**Monetary policy.** In February 2003, the central bank announced that the

monetary policy it adopted after the East Asian financial crisis in 1997 would continue in 2003. Interest rates will be kept stable, but market-oriented interest rate reforms should improve the allocation of financial resources. The PBOC should urge state-owned commercial banks to lower barriers to small and medium-sized enterprises' access to loans.

The central bank believes that the current RMB exchange rate still fits China's economic conditions.

## UNCERTAINTIES

The forecasts here take into account the likely effect of SARS, which has hit both foreign trade and the service sector in most areas. The number of businessmen taking part in the Guangzhou 2003 spring trade fair, and the volume of business at the fair, have fallen dramatically. Tourism, catering, retail sales and transportation have been most directly and severely affected by SARS. Occupancy rates have dipped to as low as 20 per cent, down from a normal level of 90 per cent at hotels popular with foreigners in Beijing. In a bid to control the prevalence of SARS, the government has taken many measures, including cancelling the weeklong May Day holiday. In past years, spending during the holiday contributed greatly to overall annual retail sales. With such strict measures, the effects of SARS will be serious in the short term, but less so in the longer term. Our forecast for 2003 has been reduced by 1.2 percentage points compared to our expectations prior to the SARS outbreak.

Domestically, China's fixed assets investment-GDP ratio reached a very high level last year, and this phenomenon has caused policymakers some concern. If these investment projects do not yield the expected return due to severe competition or economic changes, China's financial sector will suffer again from a rising level of non-performing loans.

## Urban registered unemployment rate (%)

By the end of 2002, the urban registered unemployment rate reached 4 per cent, a significant increase over the rate of just over 3 per cent a few years earlier.

