

2 China

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I. Introduction

Geographical Features

The People's Republic of China (PRC, thereafter referred as China) has a land area of about 9.6 million sq km, next only to Russia and Canada.

China is located in the east of the Asian continent, on the western shore of the Pacific Ocean, bordered by Korea to the east; Mongolia to the north; Russia to the northeast; Kazakhstan, Kyrgyzstan and Tajikistan to the northwest; Afghanistan, Pakistan, India, Nepal and Bhutan to the west and southwest; and Myanmar, Laos and Vietnam to the south. Across the seas to the east and southeast are the Republic of Korea, Japan, the Philippines, Brunei, Malaysia and Indonesia.

China's geography is highly diverse, with hills, plains, and river deltas in the east and deserts, high plateaus, and mountains in the west. Taking a bird's-eye view of China, the terrain gradually descends from west to east like a staircase, from the top of the four-step "staircase", the Qinghai-Tibet Plateau, averaging more than 4,000 m above sea level, to a continental shelf, the fourth step of the staircase, where the water there is mostly less than 200 m deep.

Climate and Resources

China has a variety of temperature and rainfall zones, including five temperature zones and a plateau-climate zone: one cold-temperate zone, mid-temperate zone, warm-temperate zone, subtropical zone, tropical zone and a plateau climate zone.

Temperatures vary a great deal. In winter, temperatures can range from an average of 30 degrees centigrade below zero in the north such as Mohe Town in Heilongjiang Province from above 20 centigrade temperature in the south such as Hainan Province. In summer, most of areas are above 20 centigrade, despite the high Qinghai-Tibet Plateau and other mountains such as Tianshan.

Cultivated land, forests, grasslands are distributed widely across China, which are among the largest in terms of sheer area in the world. But due to China's large population, the per-capita areas of cultivated land, forest and grassland are small, especially in the case of cultivated land -- only one third of the world's average.

China is rich in mineral resources, and all the world's known minerals can be found here, such as coal, iron, copper, aluminum, stibium, molybdenum, manganese, tin, lead, zinc and mercury, most of which are in the world's front rank.

Population

Since 1949, six National Population Censuses have been carried out, respectively in the year of 1953, 1964, 1982, 1990, 2000 and 2005. The Chinese government started in the 1980s to punctuate thorough National Censuses with sample censuses, which sample one percent of the population.

According to the third one-percent sample census conducted on November 1, 2005, China's population had risen to 1.306 billion by November 1, 2005, up 3.2 percent from the figure on November 1, 2000 when the Fifth National Population Census was conducted.

Based on the sample census, researchers put China's population at 1.307 billion by the end of 2005. The country's population has grown at an annual rate of 0.63 percent or 8.09 million people in the past five years.

According to the sample census, more than 11 percent of the population are the people of 60 or above and men and women each account for 51.53 percent and 48.47 percent of the population, indicating the prolonged pressure of a graying population and gender imbalance in China. The census also set the transient population in China at 147.35 million.

Table 1 Basic Statistics on National Population Census

Item	1953	1964	1982	1990	2000	2005
Total Population (10 000 persons)	59435	69458	100818	113368	126583	130756
Male	30799	35652	51944	58495	65355	67375
Female	28636	33806	48874	54873	61228	63381
Sex Ratio (female=100)	107.56	105.46	106.30	106.60	106.74	106.30
Population by Age Group (%)						
0-14	36.28	40.69	33.59	27.69	22.89	20.3
15-64	59.31	55.75	61.50	66.74	70.15	72.0
65 and Over	4.41	3.56	4.91	5.57	6.96	7.7
Population by Residence (10 000 persons)						
Urban Population	7726	12710	21082	29971	45844	56212
Rural Population	50534	56748	79736	83397	80739	74544

Notes:

1. Data in this table excluded the population of Hong Kong, Macao and Taiwan.
2. Total population from population censuses includes the military personnel. Military personnel are listed as urban population in population by residence.
3. Total population of 1953 census includes the population from indirect survey, but excludes in the nationality population and urban/rural population

Source: National Bureau of Statistics of China, Chin Statistical Yearbook 2006

Education

As a whole, education in China is still a formidable task. Chinese government, regarding education as a strategic priority, promulgated the China Agenda for Education Reform and Development.

China today has the nine-year compulsory education nationwide system, high achievement among young people and a highly competitive high school and university system. The contemporary educational system is divided into Primary (grades 1-6), Middle School (grades 7-9) and high school (grades 10-12). Certain schools in each major city are designated "key schools" with more funding and better resources than other schools. A nationwide university system was implemented in the 20th century, with undergraduate and graduate programs. Admission is by highly competitive exams.

In addition, Chinese government is also focusing on basically eliminating illiteracy among young and middle-aged population, intensively supporting 100 universities and a batch of key subjects (Program 211), giving adequate support toward occupational and polytechnic education and adult education bound for a great prospect.

Table 2 1985-2005 Basic Statistics on Education

Item	1985	1990	1995	2000	2005
Number of Schools					
Regular Institutions of Higher Education	1016	1075	1054	1041	1792
Secondary Schools	104848	100777	95216	93629	N/A
# Specialized Secondary Schools	3557	3982	4049	3646	3207
Regular Secondary Schools	93221	87631	81020	77268	62486
Primary Schools	832309	766072	668685	553622	366200
Number of Full-time Teachers (10 000 persons)					
Regular Institutions of Higher Education	34.4	39.5	40.1	46.3	96.58
Secondary Schools	296.7	349.2	388.3	472.3	N/A
# Specialized Secondary Schools	17.4	23.4	25.7	5.3	20.30
Regular Secondary Schools	265.2	303.3	333.4	400.5	349.21
Primary Schools	537.7	558.2	566.4	586.0	559.25
New Student Enrollment (10 000 persons)					
Regular Institutions of Higher Education	61.9	60.9	92.6	220.6	504.46
Secondary Schools	1789.8	1815.8	2354.1	3103.2	N/A
# Specialized Secondary Schools	66.8	73	138.1	132.6	241.13
Regular Secondary Schools	1606.9	1619.6	2025.9	2736.0	1987.58
Primary Schools	2298.2	2064	2531.8	1946.5	1671.74
Student Enrollment (10 000 persons)					
Regular Institutions of Higher Education	170.3	206.3	290.6	556.1	1561.78
Secondary Schools	5092.6	5105.4	6191.5	8518.5	N/A
# Specialized Secondary Schools	157.1	224.4	372.2	489.5	629.77
Regular Secondary Schools	4706	4586	5371	7368.9	6214.94
Primary Schools	13370.2	12241.4	13195.2	13013.3	10864.07
Graduates (10 000 persons)					
Regular Institutions of Higher Education	31.6	61.4	80.5	95.0	306.8
Secondary Schools	1279.1	1497.5	1636.9	2302.3	N/A
# Specialized Secondary Schools	42.9	66.1	83.9	150.7	156.71
Regular Secondary Schools	1194.9	1342.1	1429	1908.6	2123.43
Primary Schools	1999.9	1863.1	1961.5	2419.2	

Source: The website of China Education and Research Network, National Bureau of Statistics of China

II. Overview of Macroeconomic Activity and Fiscal Position

Table 3 Essential Economic Data

Item	2001	2002	2003	2004	2005
GDP (RMB billion)	10965.5	12033.3	13582.3	15987.8	18232.1
GDP (USD billion)	1358.8	1491.1	1683.0	1981.1	2259.2
GDP per capita (RMB)	7651.0	8214.0	9111.0	10561.0	11000.0
GDP per capita (USD)	948	1018	1129	1309	1363
GDP growth	8.3	9.1	10.0	10.1	9.9
CPI inflation (%)	0.7	-0.8	1.2	3.9	1.8
RMB: USD exchange rate of BOC of 31 December 2005	8.0702	8.0702	8.0702	8.0702	8.0702
Unemployment rate					
Level-registered (Millions)	6.9	7.7	8.0	8.3	N/A
Rate-registered in urban (%)	3.6	4.0	4.3	4.2	4.2%
EIU estimates (average in %)	N/A	N/A	N/A	9.9	9.0
Fiscal balance (% of GDP)	-2.6	-2.9	-3.1	-1.5	-1.14
Current account balance (% of GDP)	1.3	2.4	2.8	3.6	5.6
Total External Debt (% of GDP)	14.5	13.3	11.8	11.8	12.7
Debt-service ratio (% of export of g&s)	8.1	8.4	7.6	3.6	3.0
Gross official reserves (minus imports, USD billion)	9.4	10.5	10.6	12	13
Exports billion US\$	266.1	325.6	438.2	593.3	762.0
Imports billion US\$	243.6	295.2	412.8	561.2	660.1
Trade Balance billion US\$	22.6	30.4	25.5	32.1	101.9
FDI billion US\$	46.9	52.7	53.5	60.6	60.3
Foreign Exchange Reserve billion US\$	212.2	286.4	403.3	609.9	818.9
External Debt billion US\$	170.1	168.5	193.6	228.6	N/A

Notes: The data of GDP was that before the adjustment conducted in 2006

Sources: World bank 2006, NBS, MofCom, OECD 2006, EIU, CEIC

II.1 Macroeconomic Activity

A. International Environment

In 2005 Chinese economy experienced rapid development. Foreign trade grew at a high rate. Foreign direct investments were maintained at a considerable scale. The reform of the RMB exchange rate formation mechanism was promoted in a steady manner. The exchange rate demonstrated more flexibility, and the balance of payments showed “a dual surplus.

Trade Balance

In 2005, the total value of import and export reached 1,422.1 billion US dollars, an increase of 23.2 percent over 2004. Of this total, the value of export was 762.0 billion US dollars, up 28.4 percent, and the value of import was 660.1 billion US dollars, up 17.6 percent. As a result, China had a trade surplus of 101.9 billion US dollars.

The leading Chinese product export categories in 2005 were “office machines and automatic data processing machines,” “telecommunications and parts” and “electrical machinery and household appliances” comprising just over one third of total trade volume. Aggregated textile categories exports amounted to a 17.6% share of exports. “Electrical machinery and household appliances,” “petroleum and petroleum products” and “scientific instruments and apparatus” are the top three Chinese imports, representing just over 42% of total imports.

China’s most important export markets were the USA (US\$ 162.9 billion, 21.4% of total exports), the EU-25 (19.3%), Hong Kong5 (16.3%), Japan (11%) and the ASEAN-States (7.3%). The most important countries and/or regions of origin from which China imported products were Japan (US\$ 100.5 billion, 15.2% of total imports), South Korea (11.6%), the ASEAN-States (11.4%), Taiwan (11.3%), the EU-25 (11.1%) and the USA (7.4%).

Among the total import and export of China, that of the foreign funded enterprises was 831.7 billion US dollars, up by 25.4 percent over the previous year. Of this total, the value of export was 444.2 billion US dollars, up by 31.2 percent; and that of the import was 387.5 billion US dollars, up by 19.4 percent.

Table 4 Trade Balance

Item	2001	2002	2003	2004	2005
Total Value of Imports and Exports (RMB 100 million Yuan)	42183.6	51378.2	70483.5	95539.1	116921.8
Total Exports	22024.4	26947.9	36287.9	49103.3	62648.1
Total Imports	20159.2	24430.3	34195.6	46435.8	54273.7
Balance	1865.2	2517.6	2092.3	2667.5	8374.4
Total Value of Imports and Exports (USD 100 million)	5096.5	6207.7	8509.9	11545.5	14219.1
Total Exports	2661.0	3256.0	4382.3	5933.2	7619.5
Primary Goods	263.4	285.4	348.1	405.5	490.4
Manufactured Goods	2397.6	2970.6	4034.2	5527.7	7129.2
Total Imports	2435.5	2951.7	4127.6	5612.3	6599.5
Primary Goods	457.4	492.7	727.6	1172.7	1477.1
Manufactured Goods	1978.1	2459.0	3400.0	4439.6	5122.4
Balance	225.5	304.3	254.7	320.9	1020.0

Source: National Bureau of Statistics of China, China Statistical Yearbook 2006

Current Account Balance

In 2005, the surplus in the current account enjoyed a noticeable rise, accounting to USD 160.8 billion, an increase of 134 percent over the previous year, accounting for 72 percent of the overall surplus in the balance of payments, while the surplus in the capital and financial account declined, with a number of USD 63 billion, accounting for 28 percent of the overall surplus in the balance of payments.

A radical rise in the surplus of goods contributed to the increase in the trade surplus. Based on the international coverage of balance of payments statistics, the surplus in goods for 2005 reached USD 134.2 billion, up 128 percent over the previous year. In 2005 the deficit in services decreased by 3 percent to USD 9.4 billion. The deficit in transportation increased by 4 percent to USD 13 billion; the deficit in insurance increased by 16 percent to USD 6.7 billion; the deficit in royalties and licensing fees increased by 21 percent to USD 5.2 billion; the surplus in travel increased by 14 percent to USD 7.5 billion; and the surplus in other business services totaled USD 75 billion, equal to the level in 2004. The surplus in income totaled USD 10.6 billion in 2005, while the deficit in income totaled USD 3.5 billion in 2004. In 2005 the surplus in current transfers increased by 11 percent to USD 25.4 billion.

Table 5 Structure of the surplus in the balance of payments from 2001 to 2005

(Unit: 100 million USD)

Item	2001	2002	2003	2004	2005
Balance in the current account	174	354	459	687	1608
Percentage of the overall surplus in the balance of payments	33%	52%	47%	38%	72%
Balance in the capital and financial account	348	323	527	1107	630
Percentage of the overall surplus in the balance of payments	67%	48%	53%	62%	28%

Source: State Administration of Foreign Exchange

Table 6 Balance of payments of China in 2005 (Unit: 1 million USD)

Item	Balance	Credit	Debit
I. Current account	160,818	903,582	742,763
A. Goods and services	124,798	836,888	712,090
a. Goods	134,189	762,484	628,295
b. Services	-9,391	74,404	83,795
1. Transportation	-13,021	15,427	28,448
2. Travel	7,537	29,296	21,759
3. Communication services	-118	485	603
4. Construction services	974	2,593	1,619
5. Insurance services	-6,650	549	7,200
6. Financial services	-14	145	159
7. Computer and information services	218	1,840	1,623
8. Royalties and licensing fees	-5,164	157	5,321
9. Consulting services	-861	5,322	6,184
10. Advertising and public opinion polling	361	1,076	715
11. Audio-visual and related services	-20	134	154
12. Other business services	7,497	16,885	9,388
13. Government services, n.i.e.	-128	495	623
B. Income	10,635	38,959	28,324
1. Compensation of employees	1,520	3,337	1,817
2. Investment income	9,115	35,622	26,507
C. Current transfers	25,385	27,735	2,349
1. General government	-176	49	225
2. Other sectors	25,562	27,686	2,124
II. Capital and financial account	62,964	418,956	355,992
A. Capital account	4,102	4,155	53
B. Financial account	58,862	414,801	355,939
1. Direct investment	67,821	86,071	18,250
1.1 Abroad	-11,306	565	11,871
1.2 In China	79,127	85,506	6,380
2. Portfolio investment	-4,933	21,997	26,930
2.1 Assets	-26,157	74	26,231
2.1.1 Equity securities	0	0	0
2.1.2 Debt securities	-26,157	74	26,231
2.1.2.1 Bonds and notes	-25,482	74	25,557
2.1.2.2 Money market instruments	-675	0	675
2.2 Liabilities	21,224	21,923	699
2.2.1 Equity securities	20,346	20,346	0
2.2.2 Debt securities	878	1,577	699
2.2.2.1 Bonds and notes	567	1,263	696
2.2.2.2 Money market instruments	311	314	3
3. Other investment	-4,026	306,732	310,758
3.1 Assets	-48,947	10,371	59,319
3.2 Liabilities	44,921	296,361	251,440
III. Reserve assets	-207,016	1,929	208,945
3.1 Monetary gold	0	0	0
3.2 Special drawing rights	-5	0	5
3.3 Reserve position in the Fund	1,929	1,929	0
3.4 Foreign exchange	-208,940	0	208,940
3.5 Other claims	0	0	0
IV. Net errors and omissions	-16,766	0	16,766

Source: State Administration of Foreign Exchange

Foreign Direct Investment

Since the beginning of the policy reforms, over 400000 businesses with foreign participation have established themselves in China, amounting to a total FDI of 603.24 billion US dollars in 2005. The year 2005 witnessed the approval of establishment of 44,001 foreign direct invested enterprises in China, up by 0.8 percent over the previous year; and the foreign capitals actually utilized were 60.3 billion US dollars, down by 0.5 percent.

Of the total foreign direct investment actually utilized, the share of investment in manufacturing and real estate was 70.4 percent and 9 percent respectively, down by 0.6 percentage points and 0.8 percentage points over that in the pervious year, and the share of investment in leasing and business service and in transportation, storage and post service was 6.2 percent and 3 percent respectively, up by 1.6 percentage points and 0.9 percentage points.

A high percentage of foreign businesses' investments were from Hong Kong and the ASEAN region. 29.75 percent of FDI came from Hong Kong in 2005, making it by far the most important national origin (US\$ 17.9 billion in 2005). The Virgin Islands was the second most important national origin of investment with 14.96 percent of the 2005 total. In 2005 Japan took over South Korea as the third largest foreign investor (10.82 percent and 8.57 percent respectively), while both the American and Taiwanese share of total foreign investment fell dramatically by 22.32 percent and 30.97 percent respectively (American FDI represented 5.07 percent in 2005 and Taiwanese FDI 3.57 percent).

According to World Investment Report 2006, in 2005, inward of China's FDI flows was 72406 millions of dollars, more than 2 times as compared with that of the annual average in 1990-2000. In 2005, China's inward of FDI stocks was 317873 millions of dollars, 14.3 percent of gross fixed capital formation.

Table7 FDI overview of China, selected years (Millions of dollars and percentages)

FDI flows	1990-2000 (Annual average)	2002	2003	2004	2005	As a percentage of gross fixed capital formation			
						1990-2000 (Annual average)	2003	2004	2005
Inward	30104	52743	53505	60630	72406	11.3	8.6	8.0	9.2
Outward	2195	2518	-152	1805	11306	1.0	-	0.2	1.4
FDI stocks	1980	1990	2000	2004	2005	1990	2000	2004	2005
Inward	1074	20691	193348	245467	317873	5.4	17.9	14.9	14.3
Outward	...	4455	27768	35005	46311	1.2	2.6	2.1	2.1

Source: UNCTAD, World Investment Report 2006

Table 8 Foreign Direct Investment by sector and by countries or regions

By Sector (2005)									
Sector	Number of Projects (unit)	Contracted Value (USD 10 000)	Actually Utilized Value (USD 10 000)						
Total	44001	18906454	6032469						
Agriculture, Forestry, Animal Husbandry and Fishing	1058	383729	71826						
Mining	252	101632	35495						
Manufacturing	28928	12735725	4245291						
Production and Supply of Electricity, Gas and Water	390	350216	139437						
Construction	457	256677	49020						
Transport, Storage and Post	734	522404	181230						
Information Transmission, Computer Services and Software	1493	451206	101454						
Wholesale and Retail Trade	2602	434404	103854						
Hotels and Catering Services	1207	273670	56017						
Financial Intermediation	40	55144	21969						
Real Estate	2120	1940029	541807						
Leasing and Business Services	2981	858005	374507						
Scientific Research, Technical Service and Geologic Prospecting	926	175503	34041						
Management of Water Conservancy, Environment and Public Facilities	139	92130	13906						
Services to Households and Other Services	329	136616	26001						
Education	51	15974	1775						
Health, Social Security and Social Welfare	22	16459	3926						
Culture, Sports and Entertainment	272	106931	30543						
Public Management and Social Organizations			370						
By Countries or Regions (2004 and 2005)									
Rank	Country/Region	FDI (mio. USD) 2004	Share (%) 2004	Variation (%)year on year	Rank	Country/Region	FDI (mio. USD) 2005	Share (%) 2005	Variation (%)year on year
1	Hong Kong	18998	31.34	7.33	1	Hong Kong	17949	29.75	-5.52
2	Virgin Islands	6730	11.10	16.50	2	Virgin Islands	9022	14.96	34.05
3	Korea South	6248	10.31	39.20	3	Japan	6530	10.82	19.77
4	Japan	5452	9.00	7.87	4	Korea South	5168	8.57	-17.28
5	USA	3941	6.50	-6.13	5	USA	3061	5.07	-22.32
6	Taiwan	3117	5.14	-7.71	6	Singapore	2204	3.65	9.78
7	Cayman Islands	2043	3.37	135.85	7	Taiwan	2152	3.57	-30.97
8	Singapore	2008	3.31	-2.45	8	Cayman Islands	1948	3.23	-4.65
9	West Samoa	1129	1.86	14.52	9	Germany	1530	2.54	44.62
10	Germany	1058	1.75	23.46	10	West Samoa	1352	2.24	19.76
	E.U.-15	4241	7.00	7.90		E.U.-15	5194	8.61	22.47
	E.U.-25	4330	7.14	N/A		E.U.-25	5260	8.72	21.48
	APEC	42314	69.81	8.45		APEC	39043	64.72	-7.73
	ASEAN	37271	61.49	N/A		ASEAN	35336	58.58	-5.19
	EFTA	253	0.42	N/A		EFTA	235	0.39	-7.14
	Iceland	0.50	0.00	0.00		Iceland	0.15	0.00	-70.00
	Liechtenstein	47.80	0.08	1987.34		Liechtenstein	2.86	0.00	-94.02
	Norway	1.78	0.00	-90.44		Norway	26.24	0.04	1374.16
	Switzerland	203.1	0.34	12.15		Switzerland	205.9	0.34	1.36
	Total	60610	100	13.28		Total	60325	100	-0.47

Source: National Bureau of Statistics of China, Chin Statistical Yearbook 2006, Ministry of Commerce

Exchange Rate and Exchange System

Simply speaking, since 1953, there are five phases in China's exchange-rate reform, including the reform that swap center established, that exchange rate system changed to a managed floating, that official rate and swap market rate unified and the departure from the de facto peg in 2005.

In 2005 the reform of the formation mechanism for the RMB exchange rate took an important step, and the development of the foreign exchange market accelerated. On July 21, 2005, China began its reform of the formation mechanism of the RMB exchange rate, and implemented a managed floating exchange rate regime based on market demand and supply and adjusted by reference to a basket of currencies. The People's Bank of China and the State Administration of Foreign Exchange stably promoted the reform of the RMB exchange rate regime. After the reform of the exchange rate regime, the overall RMB exchange rate maintained a stable fluctuation, the flexibility of which was gradually enhanced.

In the first half of 2005, the exchange rate of the RMB against the US dollar remained stable, with a daily average weighted exchange rate of the USD against the RMB remaining at RMB 8.2765 per USD. From July 22 until December 30, the exchange rate of the USD against the RMB fluctuated smoothly, with the RMB closing price announced by the People's Bank of China appreciated from the initial USD 1 against RMB 8.11 (appreciating by 2.05 percent) to 8.0702 at the end of the year, resulting in an appreciation of 2.56 percent over that at the end of the previous year.

By the end of 2005, China's foreign exchange reserves reached 818.9 billion US dollars, an increase of 208.9 billion US dollars as compared with that at the end of the pervious year.

Table 9 Five Phases in China's Exchange-Rate Reform

Phase I. 1953–1978: Highly restricted foreign-exchange system	<ul style="list-style-type: none"> • International trade was solely dominated by state-owned import–export companies. Foreign-exchange business was solely dominated by People's Bank of China. • All foreign-exchange revenue went the government. • China did not borrow abroad and did not accept foreign direct investment. • The exchange rate was an instrument for central planning.
Phase II. 1979–1993: Transition from central planning to market-oriented exchange-rate system	<ul style="list-style-type: none"> • Firms were allowed to keep part of their foreign currency. • A market was established for transactions on foreign-exchange quotas. • Financial institutions other than the People's Bank of China were allowed to enter the foreign currency business. • A dual exchange rate system was used to subsidize export from 1981 to 1985 and from 1988 to 1993. Official exchange rate changed from 1.5 RMB/\$ in 1981 to 5.72 RMB/\$ at the end of 1993. Market exchange rate changed from 2.8 RMB/\$ in 1981 to 8.72 RMB/\$ at the end of 1993.
Phase III. 1994–1995: Various reforms in foreign-exchange rate system	<ul style="list-style-type: none"> • Effective from January 1, 1994, the official exchange rate and market exchange rate merged into single exchange rate (8.70RMB/\$). • The foreign-exchange rate was allowed to slightly fluctuate under “managed float.” • The inter-bank foreign-exchange trading system was established. Many restrictions on foreign exchange were removed.
Phase IV. 1996–July 2005: More market-oriented RMB exchange-rate system	<ul style="list-style-type: none"> • Starting from 1996, the RMB could be freely exchanged under current account. • Strict restrictions were imposed on capital account. • RMB floated in a narrow band around 8.28 RMB/\$.
Phase V. July 2005 to present: Heading toward a more market-determined RMB market	<ul style="list-style-type: none"> • On July 21, 2005, the RMB was revalued at 8.11 RMB/\$, which reflected a 2 percent increase in RMB value. • Regulators will use a basket of foreign currencies, in which the U.S. dollar accounts for less than 50 percent, in allowing exchange rate fluctuations in the foreign-exchange market.

**Table 10 Average Exchange Rate of RMB Yuan Against Main Convertible Currencies
(Middle Rate)**

Year	100 US Dollars	100 Japanese Yen	100 Hong Kong Dollars	100 Euros
1985	293.6600	1.2457	37.57	
1986	345.2800	2.0694	44.22	
1987	372.2100	2.5799	47.74	
1988	372.2100	2.9082	47.70	
1989	376.5100	2.7360	48.28	
1990	478.3200	3.3233	61.39	
1991	532.3300	3.9602	68.45	
1992	551.4600	4.3608	71.24	
1993	576.2000	5.2020	74.41	
1994	861.8700	8.4370	111.53	
1995	835.1000	8.9225	107.96	
1996	831.4200	7.6352	107.51	
1997	828.9800	6.8600	107.09	
1998	827.9100	6.3488	106.88	
1999	827.8300	7.2932	106.66	
2000	827.8400	7.6864	106.18	
2001	827.7000	6.8075	106.08	
2002	827.7000	6.6237	106.07	800.58
2003	827.7000	7.1466	106.24	936.13
2004	827.6800	7.6552	106.23	1029.00
2005	819.1700	7.4484	105.30	1019.53

Source: National Bureau of Statistics of China, Chin Statistical Yearbook 2006

Foreign Debts

After being soared by a record 35 billion dollars in 2004, up 18 percent over 2003, at the end of 2005, China's foreign debts (excluding those of Hong Kong, Macao and Taiwan) totaled 281.04 billion U.S. dollars, a rise of USD 33.55 billion over the end of 2004, equivalent to a rise of 13.6%, 5 percentage points less than that during the same period of the previous year.

Mid and long-term foreign debts rose 614 million U.S. dollars to 124.9 billion dollars, up 0.49 percent. Short-term debts increased by 32.94 billion dollars over the end of 2004 to 156.14 billion dollars, making up 55.56 percent of the total. Registered foreign debts totaled 190.25 billion U.S. dollars, and trade debts were 90.8 billion dollars. By the end of 2005, China's foreign exchange reserved surged to 818.9 billion U.S. dollars, up 34.3 percent year on year, thus ruling out any risk of failure to meet repayments.

The growth rate of registered foreign debts was under effective control, and the net inflow was markedly reduced. By the end of 2005, among the foreign debts balance, the registered foreign debts balance was USD 190.25 billion, a rise of 4.5 percent, 11.5 percentage points less than that during the same period of the previous year. The new drawings of registered foreign debts reached USD 281.05 billion, an increase of 36.5 percent; the repayment of interest and principal was USD 271.59 billion, a rise of 42.8 percent; and the net inflow (deducting principal with interest from the new drawings) was USD 9.46 billion, a reduction of 39.9 percent. By the end of 2005, the registered foreign debts accounted for 67.7% of the balance of the foreign debts, a drop of 5.9 percentage points compared with 2004.

Table 11 Balance of Foreign Debts

Type of Debts	2001	2002	2003	2004	2005
Total (\$ 100 million)	1701.10	1713.60	1936.34	2285.96	2810.45
Loans from Foreign Governments	237.00 (13.9%)	244.23 (14.5%)	254.20 (13.1%)	322.08 (14.1%)	271.95 (9.7%)
Loans from International Financial Institutions	275.70 (16.2%)	277.02 (16.4%)	264.67 (13.7%)	251.01 (11.0%)	267.88 (9.5%)
International Commercial Loans	972.30 (57.2%)	929.10 (53.5%)	1051.73 (54.3%)	1247.83 (54.6%)	1362.62 (48.5%)
Trade Loans	216.10 (12.7%)	263.23 (15.6%)	365.74 (18.9%)	465.04 (20.3%)	908.00 (32.3%)
Balance of Long-term Debts	1195.30 (70.3%)	1155.60 (67.4%)	1165.90 (60.2%)	1242.87 (54.4%)	1249.02 (44.4%)
Balance of Short-term Debts	505.80 (29.7%)	558.00 (32.6%)	770.44 (39.8%)	1043.09 (45.6%)	1561.43 (55.6%)

Source: National Bureau of Statistics of China, China Statistical Yearbook 2006

Table 12 Registered foreign debt flows from 2001 to 2005 (Unit : 100 million USD)

Items	2001	2002	2003	2004	2005
New borrowing	251.6	608.74	1015.44	2059.73	2810.48
Repayment of principal and interest	312.8	696.71	981.27	1902.4	2715.86
Net flows	-61.2	-87.97	34.17	157.33	94.62

Source: State Administration of Foreign Exchange

B. Domestic Environment

In 2005, the national economy grew steadily and rapidly. In 2005 Chinese GDP increased by 10.2%, which was 0.1% more than that in 2004.

Fixed-asset investment grew steadily and the structure was improved. In 2005 China's total fixed-asset investment increased by 25.7%, maintaining a balance with that in 2004. The results of national macro-control over key industries and products gradually became obvious, investment growth in fundamental industries such as agriculture and so forth increased, while investment in the overheated industries such as real estate, steel and iron, and so forth decreased. In 2005 investment in real estate rose by 19.8%, down by 8.3 percentage points against that in 2004.

Consumption demand increased steadily, and the rate of growth in prices fell gradually. In 2005 the actual per capita disposable income of urban residents increased by 9.6%, up by 1.9 percentage points against that in 2004; and the per capita net income of rural residents rose by 6.2%. Consumption demand rose greatly, with actual total retail consumer goods for the whole year increasing by 12%, up by 1.8 percentage points against that in 2004. The overall level of residents' consumption prices for the entire year increased by 1.8% as compared with that in the previous year, and the growth rate decreased by 2.1 percentage points.

The supply of money increased steadily, and the growth rate of credit entered a downturn stage. The supply of broad money for the whole year increased by 17.6%, with the growth rate up by 3 percentage points; the RMB credit of financial institutions increased by 11.8%, down by 1.8 percentage points against that in 2004.

Economic Growth Rate

According to the preliminary verification issued again by National Bureau of Statistics of China in August 2006, GDP of 2005 in China was adjusted to 18308.48 billion Yuan, up by 10.2 percent as compared with the previous year. The value-added of the primary industry was 2307.04 billion, up by 12.6 percent. The value-added of the secondary industry was 7691.29 billion, up by 47.5 percent. The value-added of the tertiary industry was 7296.77 billion, up by

39.9 percent. The value-added of the primary industry and the tertiary industry accounted for 6.3 percent and 39.0 percent respectively of the GDP, a little bit lower than those of the previous year.

Table 13 Gross Domestic Product (Data in this table are calculated at current prices, 100 million Yuan)

Year	Gross National Income	Gross Domestic Product	Gross Domestic Product							Per Capita GDP (Yuan/person)
			Primary Industry	Secondary Industry	Secondary Industry		Tertiary Industry	Tertiary Industry		
					Industry	Construction		Transport, Storage and Pos	Wholesale and Retail Trades	
2001	108068.2	109655.2	15516.2 (14.1%)	49512.3 (45.2%)	43580.6 (39.8%)	5931.7 (5.4%)	44626.7 (40.7%)	8406.1 (7.7%)	10787.4 (9.8%)	8622
2002	119095.7	120332.7	16238.6 (13.5%)	53896.8 (44.8%)	47431.3 (39.4%)	6465.5 (5.4%)	50197.3 (41.7%)	9393.4 (7.8%)	11950.9 (9.9%)	9398
2003	135174.0	135822.8	17068.3 (12.6%)	62436.3 (46.0%)	54945.5 (40.5%)	7490.8 (5.5%)	56318.1 (41.4%)	10098.4 (7.4%)	13480.0 (9.9%)	10542
2004	159586.7	159878.3	20955.8 (13.1%)	73904.3 (46.2%)	65210.0 (40.8%)	8694.3 (5.4%)	65018.2 (40.7%)	12147.6 (7.6%)	15249.8 (9.5%)	12336
2005	183956.1	183084.8	23070.4 (12.6%)	87046.7 (47.5%)	76912.9 (42.0%)	10133.8 (5.5%)	72967.7 (39.9%)	10526.1 (5.7%)	13534.5 (7.4%)	14040

Source: National Bureau of Statistics of China

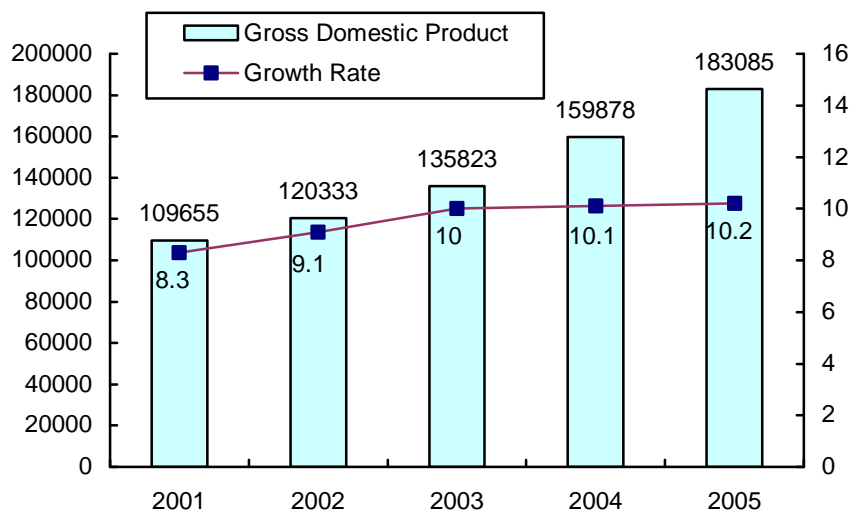
Table 14 The Share of the Three Industries to the Increase of GDP (Data in this table are calculated at current prices, %)

Year	Gross Domestic Product	Primary Industry	Secondary Industry	Industry	Tertiary Industry
2001		100.0	5.0	46.7	42.1
2002		100.0	4.5	49.8	44.4
2003		100.0	3.3	58.5	38.2
2004		100.0	7.7	52.2	40.1
2005		100.0	6.3	54.7	47.9

Note: Share of the three industries refers to the proportion of the increment of every industrial value added to the increment of GDP.

Source: National Bureau of Statistics of China

Figure 1 GDP and Growth Rate during the “Tenth-Five-Year-Plan” Period (100 million Yuan)



Source: National Bureau of Statistics of China

Inflation Rate

In 2005, the general level of consumer prices in China was up by 1.8 percent over the previous year. Of this total, the prices for service items, the retail prices of commodities, the producers' prices for manufactured goods were up by 3.3 percent, 0.8 percent and 4.9 percent respectively. The purchasing prices for raw materials, fuels and power went up by 8.3 percent. The prices for investment in fixed assets were up 1.6 percent. Producers' prices of farm products were up by 1.4 percent. The sales prices for housing in 70 large and medium cities were up by 7.6 percent.

Specifically speaking, of the general level of consumer prices up by 1.8 percent, prices of food were up by 2.9 percent. Prices for tobaccos and alcohols were up by 0.4 percent. Prices for recreation, education, culture articles and services were up by 2.2 percent. Prices for residence were up by 5.4 percent. On the other hand, prices for clothing, prices for household and appliances and services, prices for medical, health and personal articles, prices of transportation and telecommunication decreased by 1.7 percent, 0.1 percent, 0.1 percent and 1.0 percent respectively.

Table15 Price Indices (Preceding year=100)

Year	Consumer Price Index			Retail Price Index	Ex-Factory Price Indices of Industrial Products	Purchasing Price Indices of Raw Material, Fuel and Power	Investment in Fixed Assets Price Index
		Urban Areas	Rural Areas				
2001	100.7	100.7	100.8	99.2	98.7	99.8	100.4
2002	99.2	99.0	99.6	98.7	97.8	97.7	100.2
2003	101.2	100.9	101.6	99.9	102.3	104.8	102.2
2004	103.9	103.3	104.8	102.8	106.1	111.4	105.6
2005	101.8	101.6	102.2	100.8	104.9	108.3	101.6

Source: National Bureau of Statistics of China, China Statistical Yearbook 2006

Table 16 Change in Consumer Prices (preceding year=100)

Item	2001	Urban	Rural	2002	Urban	Rural
General Level of consumer prices	0.7	0.7	0.8	-0.8	-1.0	-0.4
Food	0.0	0.1	-0.2	-0.6	-0.5	-0.7
Of which:grain	-0.7	-0.8	-0.3	-1.7	-1.7	-1.6
Tobaccos and alcohols	-0.3	-0.3	-0.4	-0.1	-0.1	0.0
Clothing	-1.9	-2.2	-1.1	-2.4	-2.7	-2.2
Household appliances and services	-2.3	-2.5	-1.6	-2.5	-2.7	-2.2
Medical, health &personal articles	0.0	-0.7	1.1	-1.2	-2.0	0.1
Transportation and telecommunication	-1.0	-0.9	-1.3	-1.9	-2.0	-1.8
Recreation, education, culture articles and services	6.6	6.7	6.4	0.6	0.2	1.2
Residence	1.2	1.7	0.3	-0.1	-0.2	0.1
Item	2003	Urban	Rural	2004	Urban	Rural
General Level of consumer prices	1.2	0.9	1.6	3.9	3.3	4.8
Food	3.4	3.4	3.4	9.9	9.1	11.5
Of which:grain	2.3	2.3	2.2	26.4	25.7	27.7
Tobaccos and alcohols	-0.2	-0.2	-0.1	1.2	1.2	1.3
Clothing	-2.2	-2.6	-1.4	-1.5	-1.5	-1.6
Household appliances and services	-2.6	-3.0	-1.7	-1.4	-1.9	-0.3
Medical, health &personal articles	0.9	-0.2	2.5	-0.3	-0.8	0.5
Transportation and telecommunication	-2.2	-2.6	-1.4	-1.5	-2.1	-0.2
Recreation, education, culture articles and services	1.3	0.5	2.8	1.3	0.8	2.1
Residence	2.1	2.8	1.0	4.9	4.3	5.8
Item	2005	Urban	Rural			
General Level of consumer prices	1.8	1.6	2.2			
Food	2.9	3.1	2.5			
Of which:grain	1.4	1.5	1.3			
Tobaccos and alcohols	0.4	0.3	0.5			
Clothing	-1.7	-2.0	-0.9			
Household appliances and services	-0.1	-0.3	0.3			
Medical, health &personal articles	-0.1	-0.4	0.5			
Transportation and telecommunication	-1.0	-1.6	0.3			
Recreation, education, culture articles and services	2.2	1.3	3.8			
Residence	5.4	5.6	5.2			

Source: National Bureau of Statistics of China, China Statistical Yearbook 2006

Consumption

In 2005, the value of all household consumption expenditure was 5439 Yuan, up by 7.7 percent over the previous year, with an increase of 581 percent compared with that of 1978. Of this total, rural house consumption expenditure was 2531 Yuan, while consumption expenditure of urban household was 9393 Yuan. The Ratio of urban over rural Consumption (Urban Household=1) was 3.7.

Table 17 Household Consumption Expenditure

Year	Value (yuan): all households/rural/urban			Urban/Rural Consumption Ratio (Urban Household=1)	Index (Preceding Year=100)			Index (1978=100)		
	All	Rural	Urban		All	Rural	Urban	All	Rural	Urban
1978	184	138	405	2.9	104.1	104.3	103.3	100.0	100.0	100.0
1980	238	178	489	2.7	109.0	108.4	107.2	116.5	115.4	110.2
1990	833	560	1596	2.9	103.7	99.2	108.5	229.2	215.4	190.9
2000	3632	1860	6850	3.7	108.6	104.5	107.8	491.0	371.3	391.1
2001	3869	1969	7113	3.6	105.7	104.5	103.2	518.8	388.0	403.6
2002	4106	2062	7387	3.6	106.5	105.2	104.2	552.5	408.1	420.5
2003	4411	2103	7901	3.8	106.5	100.3	106.3	588.5	409.5	447.2
2004	4925	2301	8679	3.8	107.4	103.4	106.4	632.3	423.5	475.7
2005	5439	2531	9393	3.7	107.7	106.5	105.8	681.0	451.0	503.3

Notes: Absolute figures in this table are calculated at current prices, while indices are calculated at constant prices; The effect of price differentials between urban and rural areas has not been removed in the calculation of the urban/rural consumption ratio.

Domestic Investment

In 2005, the completed investment in fixed assets of China was 8, 860.4 billion Yuan, up by 25.7 percent over the previous year. Of this total, investment in urban areas was 7,509.6 billion Yuan, up by 27.2 percent, and investment in rural areas amounted to 1,350.8 billion Yuan, up by 18.0 percent.

Of the investment in urban areas, the investment by state-owned and state-holding enterprises was 4,004.7 billion Yuan, up by 17.5 percent over 2004. Classified by the industries, the investment in the primary industry was 82.3 billion Yuan, up by 27.5 percent. The investment in the secondary industry was 3,159.8 billion Yuan, up by 38.4 percent; and that in the tertiary industry was 4,267.5 billion Yuan, an increase of 20.0 percent. In terms of different sectors, the investment in coal mining and washing was up by 65.6 percent over the previous year; in the production and distribution of electric power and heat power, up by 33.7 percent; in the extraction of petroleum and natural gas, up by 29.7 percent; in railway transport, up by 45.7 percent; in the manufacture of transport equipment, up by 51.1 percent; in the manufacture of textile, up by 38.0 percent; in education, up by 8.4 percent, and in public health, up by 28.9 percent.

In 2005, the investment in real estate development was 1,575.9 billion Yuan, up by 19.8 percent over the previous year. The complete floor space of commercial buildings amounted to 487.93 million square meters, up by 14.9 percent. Total sales of commercial buildings reached 1,808.0 billion Yuan. Of this total, the sales of completed housing accounted for 35.5 percent, and the forward delivery housing accounted for 64.5 percent.

On October 15, 2005, the completion of the Qinghai-Tibet railway, the world's highest railway, terminated the status of zero-railway transport in Tibet. By the end of 2005, a total of 14 power generators had been put into operation in the Three Gorges Project, having generated 94.0 billion kilowatt-hours of electricity. The West-East Electricity Transmission Project from north, central and south channels had built a power transmission capacity of over 32.50 million kilowatts. A total of 3.8 billion Yuan worth of investment was completed for the first phase of the eastern and central routes of South-to-North Water Diversion Project. The total completed investment in the key projects in harnessing of the Huaihe River was 25.0 billion Yuan.

Table 18 Newly Increased Production Capacity through Investment in Capital Construction in the 10th Five-year Plan Period

Item	Unit	2001-2005	Of which: 2005
Newly increased power generating capacity	10,000 kilowatts	17655	6326
Power transformer equipment with a capacity of over 110,000 volts	10,000 kilovolt-amperes	40666	15306
New trunk railways put into operation	Kilometer	7063	1203
Double-track railways put into operation	Kilometer	3556	486
Electrified railways put into operation	Kilometer	5494	863
New highways	Kilometer	351173	129748
Of which: Expressways	Kilometer	23964	6457
Newly increased cargo-handling capacity of 10000-ton berths at harbors	10,000 tons	45232	18989
Newly installed capacity of telephone switchboards	10,000 lines	23254	4608
Item	Unit	2001-2005	Of which: 2005
Newly increased power generating capacity	10,000 kilowatts	17655	6326

Source: National Bureau of Statistics of China

Stock market

In 2005, funds raised through issuing stocks and share rights on stock market amounted to 188.3 billion Yuan, an increase of 36.3 billion Yuan over the previous year. Of this total, funds

from issuing A shares amounted to 33.8 billion Yuan worth of capital, a decrease of 49.8 billion Yuan over 2004. Capital from the issue of 24 H shares reached 154.5 billion Yuan, an increase of 88.7 billion Yuan. The number of listed companies (with A or B shares) on China stock market rose from 1,377 at the end of 2004 to 1,381 at the end of 2005, representing 3,243 billion Yuan worth of market value, a shrink of 12.5 percent over the previous year. Corporate bonds with maturity at one year or longer issued throughout the year totaled 65.4 billion Yuan, an increase of 33.2 billion Yuan over 2004.

Real Estate Market

While the stock market needs policies to stimulate it, China's real estate market needs policies to cool down the overheating investment and exorbitant prices.

Between January and November 2005, the investment in real estate saw a year-on-year increase of 23.6 percent, and reached 1.48 trillion Yuan (\$183 billion), accounting for 23.4 percent of the total fixed assets investment during the period. Retail price of commercial housing at the end of November 2005 was 700 Yuan (\$86) more than the price in the beginning of the year. The price increased month on month.

Table 19 Growth of real estate market

%	1999	2000	2001	2002	2003	2004	2005
Growth of real estate loans	39	117	35	42	37	23	N/A
Growth of real estate investment	14	19	27	24	30	28	23.6

Source: The People's Bank of China

Money Supply

By the end of 2005, money supply of broad sense (M2) amounted to 29.9 trillion Yuan, an increase of 17.6 percent over the previous year. Money supply of narrow sense (M1) amounted to 10.7 trillion Yuan, 11.8 percent increased. Cash in circulation (M0) was 2.4 trillion Yuan, up 11.9 percent. Savings deposit in RMB and foreign currencies in all items in financial institutions totaled 30.0 trillion Yuan at the end of 2005, up 18.2 percent. Loans in RMB and foreign currencies in all items in financial institutions reached 20.7 trillion Yuan, up 12.8 percent.

Loans in RMB from rural financial cooperation institutions (i.e. rural credit cooperatives, rural cooperation banks, and rural commercial banks) stood at 2.2 trillion Yuan, an increase of 345.1 billion Yuan as compared with the end of 2004. The loans in RMB for consumption use in all financial institutions totaled 2.2 trillion Yuan, an increase of 199.6 billion Yuan. Of all consumption loans, those for individual housing totaled 1.84 trillion Yuan, an increase of 244.4 billion Yuan.

The premium of insurance companies totaled 492.7 billion Yuan, up 14.0 percent over the previous year. Of this total, life insurance premium earnings amounted to 324.4 billion Yuan, health and casualty insurance premium earnings 45.3 billion Yuan, and property insurance premium earnings 123 billion Yuan. Insurance companies paid an indemnity worth of 113 billion Yuan, of which, life insurance indemnity was 30.7 billion Yuan, health and casualty insurance indemnity 15.1 billion Yuan, and property insurance indemnity 67.2 billion Yuan.

Table 20 Savings Deposit and Loans in RMB and Foreign Currencies in All Financial Institutions in 2005 (Unit: 100 million Yuan)

Item	Year-end figure	Increase over 2004 (%)
Savings deposit	300209	18.2
Of which: By enterprises	101751	13.8
By urban and rural households	147054	16.5
Of which: Deposits in RMB	141051	18.0
Loans	206838	12.8
Of which: Short-term	91157	6.5
Medium and long-term	92941	16.2

Source: National Bureau of Statistics of China

Employment

By the end of 2005, the total of employed people in China amounted to 758.25 million, an increase of 6.25 million compared with the employment number at the end of 2004. Of this total, 273.31 million were employed in urban areas, an increase of 9.7 million or a net increase of 8.55 million. The urban unemployment rate through unemployment registration was 4.2 percent at the end of 2005, maintaining the same level as that in the preceding year.

Table 21 Employment statistic data in 2005 (10 000 persons)

Item	2001	2002	2003	2004	2005
Economically Active Population	74432	75360	76075	76823	77877
Total Number of Employed Persons	73025	73740	74432	75200	75825
Primary Industry	36513	36870	36546	35269	33970
Secondary Industry	16284	15780	16077	16920	18084
Tertiary Industry	20228	21090	21809	23011	23771
Composition of Employed Persons (total=100)					
Primary Industry	50.0	50.0	49.1	46.9	44.8
Secondary Industry	22.3	21.4	21.6	22.5	23.8
Tertiary Industry	27.7	28.6	29.3	30.6	31.4
Number of Employed Persons by Urban and Rural Areas					
Urban Employed Persons	23940	24780	25639	26476	27331
State-owned Units	7640	7163	6876	6709.9251	6488
Urban Collective-owned Units	1291	1122	1000	897.1599	810
Cooperative Units	153	161	173	192.4	188
Joint Ownership Units	45	45	44	44.1	45
Limited Liability Corporations	841	1083	1261	1436	1750
Share-holding Corporations Ltd.	483	538	592	624.9	699
Private Enterprises	1527	1999	2545	2993.729	3458
Units with Funds from Hong Kong, Macao & Taiwan	326	367	409	469.8	557
Foreign Funded Units	345	391	454	563	688
Self-employed Individuals	2131	2269	2377	2521.2246	2778
Rural Employed Persons	49085	48960	48793	48724	48494
Township and Village Enterprises	13086	13288	13573	13866	14272
Private Enterprises	1187	1411	1754	2023.5223	2366
Self-employed Individuals	2629	2474	2260	2065.8835	2123
Number of Staff and Workers	10792	10558	10492	10576	10850
State-owned Units	7409	6924	6621	6438	6232
Urban Collective-owned Units	1241	1071	951	851	769
Units of Other Types of Ownership	2142	2563	2920	3287	3849
Number of Registered Unemployed Persons in Urban Areas	681	770	800	827	839
Registered Unemployment Rate in Urban Areas (%)	3.6	4	4.3	4.2	4.2

Notes: From 1990 to 2000, the total number of employed persons and the sub-total of urban and rural employed persons have been adjusted in accordance with the data obtained from the 5th National Population Census.

Source: National Bureau of Statistics of China

Agriculture

In 2005, the sown area of grain was 104.27 million hectares, an increase of 2.67 million hectares over the previous year, with an output of 484.01 million tons, up by 14.54 million tons or 3.1% over the previous year. The sown area of cotton was 5.06 million hectares, a decline of 630,000 hectares, with an output of 5.70 million tons, a decrease of 9.8 percent. The sown area of oil-bearing crops was 14.31 million hectares, a decline of 120,000 hectares, with an output of 30.78 million tons, up by 0.4 percent. The sown area of sugar crops was 1.56 million hectares, a decrease of 10,000 hectares, with an output of 95.51 million tons, a decrease of 0.2 percent, and that for vegetables stood at 17.74 million hectares, an increase of 180,000 hectares. Along with optimized varieties, outputs of vegetable and fruit have increased steadily.

The total output of meat for the year of 2005 amounted to 77.0 million tons, up by 6.3 percent. Of this total, the output of beef and mutton was up by 5.6 percent and 9.3 percent respectively. The total output of aquatic products was 51.0 million tons, up by 4.0 percent. The total production of timber for the year of 2005 reached 47.46 million cubic meters, a decline of 8.7 percent as compared with that in the previous year.

Table 22 Output of Major Farm Products (Unit: 10,000 tons)

Item	2001	2002	2003	2004	2005	Increase over 2004(%)
Grain	45262	45711	43067	46947	48401	3.1
Oil-bearing crops	2872	2900	2805	3057	3078	0.4
Peanuts	1447	1495	1337	1431	1434	0.0
Rapeseed	1132	1053	1141	1304	1305	0.0
Cotton	532	492	487	632	570	-9.8
Sugar corps	8790	10151	9670	9528	9551	-0.2
Sugarcane	7700	8883	9051	8948	8760	-2.5
Beetroot	1090	1268	619	580	791	35.2
Cured tobacco	204	213	201	214	241	11.5
Tea	69	74	78	84	92	9.8
Fruits	6536	6809	14470	15243	16076	4.8
Vegetables			53960	54927	56284	2.2

Source: National Bureau of Statistics of China

Industry

In 2005, the total value-added of the industrial sector was 7,619.0 billion Yuan, up by 11.4 percent as compared with that of the preceding year. The value-added of industrial enterprises above designated size was 6,642.5 billion Yuan, up by 16.4 percent. The sales ratio of industrial enterprises was 98.1 percent, standing at the same level as in 2004.

Among the industrial enterprises above designated size, the profits of state-owned and state-holding enterprises stood at 644.7 billion Yuan, up by 17.4 percent; that of the collective enterprises was 55.1 billion Yuan, up by 32.0 percent. The profits made by share-holding enterprise reached 742.0 billion Yuan, up by 28.7 percent; that of foreign invested enterprises and enterprises invested by investors from Hong Kong, Macao and Taiwan stood at 396.7 billion Yuan, up by 6.9 percent, and that of the private enterprises was 197.5 billion Yuan, up by 47.3 percent.

Table 23 Value-added of Industrial Enterprises above Designated Size in 2005 (Unit: 100 million Yuan)

Item	Value-added	Increase over 2004 (%)
Value-added of industrial enterprises above designated size	66425	16.4
Of which: State-owned and state-holding enterprises	26063	10.7
Of which: Collective enterprises	2581	12.4
Share-holding enterprises	32173	17.8
Enterprises invested by foreigners or investors from Hong Kong, Macao, and Taiwan.	18977	16.6
Of which: Private enterprises	11807	25.3
Of which: Light industry	20585	15.2
Heavy industry	45840	17.0

Source: National Bureau of Statistics of China

II.2 Fiscal Position

The prudent fiscal policy adopted in 2005 was the result of adopting a series of measures to strengthen macro control in recent years. The process of implementation was gradual. During this period, pushing forward reforms such as tax reform, social security system reform and rural reform was the main concern of the Chinese government.

According to the Report of central government final accounts in 2005, China's fiscal revenue soared almost 20 percent in 2005 to hit a record 3.16 trillion Yuan (395 billion U.S. dollars). The figure was achieved by the implementation of a prudent fiscal policy since 2005 that enabled stable and rapid economic growth and more forceful revenue collection by finance, taxation and customs departments. The 3,393 billion-Yuan (424.1 billion U.S. dollars) national fiscal expenditure, up 19.1 percent over the previous year, outnumbered revenue by 228 billion Yuan (28.5 billion dollars).

The central treasury pocketed 1,726 billion Yuan (215.75 billion dollars), the two largest sources being value-added tax (VAT) revenue of 793.1 billion Yuan (99.1 billion dollars) and consumer tax, VAT and tariff on imports totaling 527.7 billion Yuan (65.9 billion dollars). Various tax incomes for the whole year of 2005 reached 3,086.6 billion Yuan (excluding tariffs and agricultural taxes), an increase of 514.8 billion Yuan over 2004, with a year-on-year increase of 20 percent. The ratio of profits to sales was 5.9 percent, which was 0.1 percentage point lower than that in the previous year.

Some 702.2 billion Yuan (87.8 billion dollars) of state bonds were issued by the central treasury to claim 692.2 billion Yuan (86.5 billion dollars) in revenue for the state coffers, nearly 300 billion Yuan of which was used to offset the budget deficit.

About 35.3 billion Yuan (4.4 billion dollars) of the 163.7 billion Yuan (20.4 billion dollars) by the central treasury was used for tax rebates to local treasuries, general transfer payment, transfer payment for minority-concentrated regions, educational and scientific undertakings, leaving the rest to pay money overdue to avert financial risks.

Table 24 Government Revenue and Expenditure and Their Increase Rates

Year	Government Revenue (100 million Yuan)	Government Expenditure (100 million Yuan)	Balance (100 million Yuan)	Increase Rates (%)		Percentage of Government Revenue to GDP (%)
				Government Revenue	Government Expenditure	
2001	16386.04	18902.58	-2516.54	22.3	19.0	14.9
2002	18903.64	22053.15	-3149.51	15.4	16.7	15.7
2003	21715.25	24649.95	-2934.70	14.9	11.8	16.0
2004	26396.47	28486.89	-2090.42	21.6	15.6	16.5
2005	31649.29	33930.28	-2280.99	19.9	19.1	17.3

Source: National Bureau of Statistics of China

Table 25 Government Revenue by Item (100 million Yuan)

Year	Total Government Revenue	Taxes	Subsidies to Loss-making Enterprises	Revenue from Extra- charges for Education	Other Revenue
2001	16386.04	15301.38	-300.04	166.60	1218.10
2002	18903.64	17636.45	-259.60	198.05	1328.74
2003	21715.25	20017.31	-226.38	232.39	1691.93
2004	26396.47	24165.68	-217.93	300.40	2148.32
2005	31649.29	28778.54	-193.26	356.18	2707.83

Source: National Bureau of Statistics of China

Table 26 Government Expenditure by Main Item (100 million Yuan)

Items	2001	2002	2003	2004	2005
Expenditure for Capital Construction	2510.64	3142.98	3429.30	3437.50	4041.34
Additional Appropriation for Circulating Capital of Enterprises	22.71	18.97	11.95	12.44	18.17
Innovation Funds and Science and Technology Promotion Funds	991.56	968.38	1092.99	1243.94	1494.59
Geological Prospecting Expenses Operating Expenses of the Departments of Industry, Transport and Commerce	99.01	102.89	106.94	115.45	132.70
Operating Expenses of the Departments of Industry, Transport and Commerce	200.12	232.38	285.23	368.21	444.15
Expenditure for Supporting Rural Production	917.96	1102.70	1134.86	1693.79	1792.40
Expenses on Culture, Education, Science and Public Health	3361.02	3979.08	4505.51	5143.65	6104.18
Expenditure for Pension and Social Welfare	3361.02	3979.08	4505.51	5143.65	6104.18
Expenditure for National Defence	1442.04	1707.78	1907.87	2200.01	2474.96
Administrative Expenses	2197.52	2979.42	3437.68	4059.91	4835.43
Expenditure on Policy-related Subsidies	741.51	645.07	617.28	795.80	998.47

Source: National Bureau of Statistics of China

Table 27 Revenue statistics of Chinese taxes in some years (100 million Yuan)

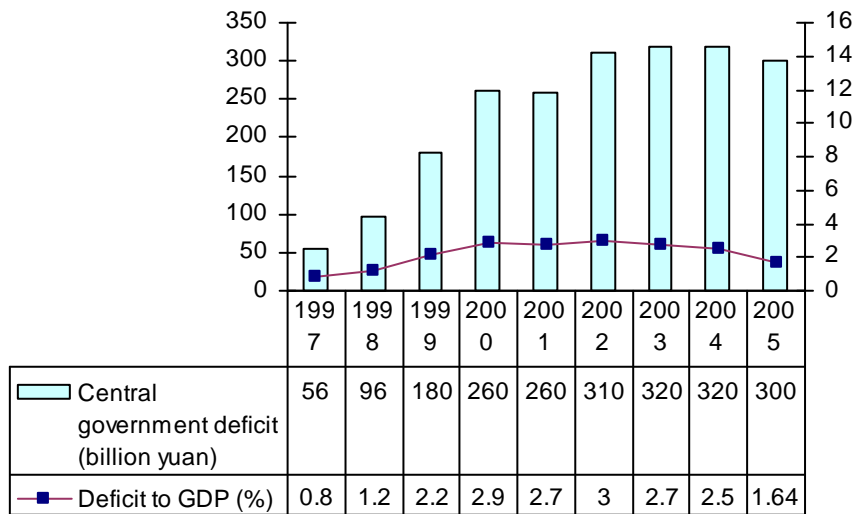
year	Total tax revenue	Value-added tax	Business tax	Consumption tax	Tariffs	Agricultural and related tax	Company income tax	Tax revenue in proportion to total fiscal revenue (%)	Tax revenue in proportion to GDP (%)
1978	519.28				28.76	28.40		45.9	14.3
1980	571.70				33.53	27.67		49.3	12.7
1985	2040.79	147.70	211.07		205.21	42.05	696.06	101.8	22.8
1990	2821.86	400.00	515.75		159.01	87.86	716.00	96.1	15.2
1995	6038.04	2602.33	865.56	541.48	291.83	278.09	878.44	96.7	9.9
2000	12581.51	4553.17	1868.78	858.29	750.48	465.31	999.63	93.9	12.7
2001	15301.38	5357.13	2064.09	929.99	840.52	481.70	2630.87	93.4	14.0
2002	17636.45	6178.39	2450.33	1046.32	704.27	717.85	3082.79	93.3	14.7
2003	20017.31	7236.54	2844.45	1182.26	923.13	871.77	2919.51	92.2	14.7
2004	24165.68	9017.94	3581.97	1501.90	1043.77	902.19	3957.33	91.5	15.1
2005	28778.54	10792.11	4232.46	1633.81	1066.17	936.40	5343.92	91.0	15.8

Note:

1. The tax revenue and the fiscal revenue statistics in this table are based on the final budget of the Ministry of Finance. The GDP statistics are from the State Statistic Bureau. The data in 2005 are the primary statistics.
2. From 1983, the tax revenue includes the income tax paid by the State owned enterprises. Before paying income tax, the State owned enterprises handed over profits to the State.
3. In 1985, the tax revenue exceeds the fiscal revenue for the reason that the excessive amount of losses of enterprises largely reduces the fiscal revenue.
4. The statistics in this table do not include those for Hong Kong, Macao and Taiwan.

Source: National Bureau of Statistics of China

Figure 2 The Fiscal Deficit (1997-2005)



Source: Ministry of Finance

III. Tax Structure: Institutions and The Reality

Taxation is the main source of national revenue and used as a fiscal tool to re-allocate national wealth. Since 1949, China's tax system experienced five important reforms:

The first reform happened at the beginning of the foundation of new China in 1950 when the new tax system of the People's Republic was set up on the basis of sorting out the tax system of the old China and summarizing the experience of the tax system construction of revolutionary base. The second reform was taken in 1958, the major contents of which were simplifying the industrial and commercial tax system to adapt to the requirement of the situation after the completion of the socialist transformation and the reform of the economic administration system. The third reform in 1973 still aimed at simplifying the industrial and commercial tax system, which was the result of the Cultural Revolution. The fourth one was carried out in 1984, the major contents of which were adopting the replacement of profits with taxation for State-owned enterprises and reforming the industrial and commercial tax system to adapt to the requirement of the development of the planned socialist commodity economy. The fifth reform in 1994 was to fully reform the industrial and commercial tax system to adapt to the requirement of establishing the socialist market economy.

The key contents of the industrial and commercial tax reform in 1994 were:

- (1) Fully reforming the turnover tax system by adopting the VAT as the core with the Consumption Tax and Business Tax supplementing and unification for both domestic enterprises and foreign enterprises;
- (2) Reforming the old enterprise income tax system by integrating the old multi-income taxes on State enterprises, collective enterprises and private enterprises into one unified Enterprise Income Tax;
- (3) Reforming the Individual Income Tax by unifying the old Individual Income Tax on foreigners, Individual Income Regulation Tax on Chinese and the Income Tax on Individual Households into one Individual Income Tax;
- (4) Largely adjusting the Resource Tax, Special Purpose Tax, Property Tax, Behavioral Tax, such as expanding the scope of the Resource Tax, starting to levy Land Appreciation Tax,

abolishing Salt Tax, Bonus Tax and Market Transaction Tax, decentralizing the Slaughter Tax and Banquet Tax to the local government at provincial level, and newly adopting Inheritance Tax and Securities Transaction Tax (these two taxes have not been legislated for levying later).

In short, in 1950, China established its own tax system and the current tax system was established in 1994 under the basic requirement of developing socialist market economy.

III.1 Current tax system of China

The current tax system includes 22 types of taxes. The fundamental laws and regulations of taxation are formulated by the NPC and its Standing Committee and the State Council.

Type of taxes

According to their nature and function, 22 types of taxes can be divided into 4 categories, including categories of Goods and service Taxes, Income Taxes, Property Taxes and Other taxes.

In 2005, the total tax revenue collected by the Chinese tax department, excluding Customs Duty and Agriculture Tax, was 3086.6 billion Yuan, accounting for 97.6 percent of the fiscal revenue. Out of the total tax revenue, taxes on goods and services including Value-Added Tax, Consumption Tax and Business Tax were 1656.4 billion Yuan, up by 18.2 percent, accounting for 49.5 percent of the total tax revenue increase; income taxes were 760.5 billion Yuan, up by 30.9 percent, accounting for 34.8 percent of the total tax revenue increase.

Table 28 Graph of Chinese Tax System (By category of taxes)

Categories of Taxes	Type of Taxes	Tax base
Goods and service Taxes	Value-Added Tax, Consumption Tax, Vehicle Acquisition Tax, Customs Duty, Business Tax	Based on the value (volume) of turnover of sales or import & export value (or quantity) of the goods of the taxpayers in the manufacturing, circulation or service sectors.
Income Taxes	Enterprise Income Tax, Income Tax on Enterprises with Foreign Investment and Foreign Enterprises, Individual Income Tax, Land Appreciation Tax	Levied on the basis of the profits gained by producers or dealers, or of the income earned by individuals.
Property Taxes	House Property Tax, Urban Real Estate Tax, City and Township Land Use Tax, Farmland Occupation Tax, Deed Tax, Resource Tax, Vehicle and Vessel Usage Tax, Vehicle and Vessel Usage License Plate Tax, Vessel Tonnage Tax	Levied on the properties kept and used by taxpayers.
Other taxes	Stamp Tax, City Maintenance and Construction Tax, Fixed Asset Investment Orientation Regulation Tax, Banquet tax, Agriculture Tax	

Notes:

1. Banquet Tax has been decentralized to the local government for administration for the decision of levying or not according to the local conditions and it is not levied any longer in all areas.
2. The levying of the Fixed Asset Investment Orientation Regulation Tax has been suspended.
3. Although designed, the Fuel Tax, Inheritance Tax and Social Security Tax have not yet been enacted for levying.

Table 29 Tax revenue statistics of China by type of taxes in 2005

□. Total	308,658,317
National tax revenue	213,344,919
Local tax revenue	95,313,398
1.VAT	106,982,857
2.Consumption Tax	16,343,136
3.Customs Duties	42,200,523
4.Business Tax	42,314,248
5.Enterprise Income Tax	43,631,329
6.Income Tax on Enterprises with Foreign Investment and Foreign Enterprises	11,476,932
7.Individual Income Tax	20,939,136
8.Resource Tax	1,426,322
9.City Maintenance and Construction Tax	7,960,209
10.House Property Tax	4,359,028
11.Stamp Tax	2,267,540
12.City and Township Land Use Tax	1,373,281
13.Land Appreciation Tax	1,400,156
14.Vehicle and Vessel Usage Tax	388,903
15.Vehicle Acquisition Tax	5,576,218
16.Other Taxes	18,508
□. Tax refund on exported goods	-33,715,735

Source: State Administration of Taxation

Tax legislation

For the time being, the State Organs having authority to formulate tax laws or tax policy mainly include the National People's Congress and its Standing Committee, the State Council, the Ministry of Finance, the State Administration of Taxation, the General Administration of Customs, and the Tariff and Classification Committee of the State Council.

Table 30 Tax legislation

Tax legislation	the State Organs	examples	Steps for the formulation
Tax laws	Formulated by the National People's Congress Or formulated by the Standing Committee of the NPC	Individual Income Tax Law of the People's Republic of China Tax Collection and Administration Law of the People's Republic of China	drafting, examination, voting and promulgation
The administrative regulations and rules concerning taxation	Formulated by the State Council in accordance with relevant laws Or under the authorization of the National People's Congress and its Standing Committee	Detailed rules for the Implementation of the Tax Collection and Administration Law of the People's Republic of China Provisional Regulations of the People's Republic of China on Value Added Tax	Planning, drafting, verification and promulgation
The departmental rules concerning taxation	Formulated by the Ministry of Finance, the State Administration of Taxation, the General Administration of Customs, and the Tariff and Classification Committee of the State Council in accordance with the relevant laws and administrative rules	Detailed Rules for the Implementation of the Provisional Regulations of the People's Republic of China on Value Added Tax	Planning, drafting, verification and promulgation

Notes:

1. The people's government of provinces, autonomous regions, municipalities directly under the State Council and some large cities may formulate tax rules in accordance with tax laws and regulations or local regulations and rules of their provinces, autonomous regions and municipalities directly under the State Council. 2. Separate tax system shall be implemented in Hong Kong and Macao SAR, and the Central Government shall not levy taxes in these two special administrative regions.

Foreign Taxation

Out of the tax laws, regulations, and methods already promulgated and executed in China, there are 14 of them currently applicable to the enterprises with foreign investment, foreign enterprises or foreigners, which include VAT, Consumption Tax, Vehicle Acquisition Tax, Customs Duty, Business Tax, Income Tax on Enterprises with Foreign Investment and Foreign Enterprises, Individual Income Tax, Land Appreciation Tax, Urban Real Estate Tax, Deed Tax, Resource Tax, Vehicle and Vessel Usage License Plate Tax, Vessel Tonnage Tax and Stamp Tax.

The enterprises invested by Chinese compatriots residing in Hong Kong, Macao and Taiwan and other overseas Chinese, and Chinese compatriots from Hong Kong, Macao, Taiwan and other overseas Chinese will be treated for tax purpose in the same manner either as Enterprises with Foreign Investment and Foreign Enterprises or foreigners.

By February 1, 2006, China has successively concluded the agreement on avoidance of double taxation on income and prevention of tax evasion with 88 countries, namely: Japan, the USA, France, UK, Belgium, Germany, Malaysia, Norway, Denmark, Singapore, Finland, Canada, Sweden, New Zealand, Thailand, Italy, the Netherlands, Former Czechoslovakia, Poland, Australia, Bulgaria, Pakistan, Kuwait, Switzerland, Cyprus, Spain, Romania, Austria, Brazil, Mongolia, Hungary, Malta, the United Emirates of Arab, Luxembourg, Republic of Korea, Russia, Papua New Guinea, India, Mauritius, Croatia, Belarus, Slovenia, Israel, Viet Nam, Turkey, Ukraine, Armenia, Jamaica, Iceland, Lithuania, Latvia, Uzbekistan, Bangladesh, Yugoslavia, Sudan, Macedonia, Egypt, Portugal, Estonia, Laos, The Seychelles, the Philippines, Ireland, South Africa, Barbados, Moldova, Qatar, Cuba, Venezuela, Nepal, Kazakhstan, Indonesia, Oman, Nigeria, Tunis, Iran, Bahrain, Greece, Kyrgyz Republic, Morocco, Sri Lanka, Trinidad And Tobago, Albania, Brunei, Azerbaijan, Georgia, Mexico and Saudi Arabia (Among them, the agreement signed with the former Czechoslovakia is applicable to both Czech and Slovakia).

III.2 Briefing of taxes under China's Tax system

VAT

VAT is a major tax item in China at present, to which industrial and commercial added value is subject. The "Provisional Regulations of the People's Republic of China on Value Added Tax" currently effective in China was promulgated by the State Council on December 13, 1993 and put into effect on January 1, 1994.

VAT taxpayers include any enterprise, unit, individual householder and other individual engaged in sales of goods, importation of goods, provision of services of processing, repairs and replacement within the territory of the People's Republic of China.

Based on different taxable goods, services, different flat rates and zero rate are adopted.

Computation of tax payable is as follows.

Tax payable for normal taxpayers = Output tax payable for the current period – Input tax for the current period (Output tax payable = Sales volume in the current period × Applicable tax rate)

Tax payable for small taxpayers = Sales amount × Applicable rate (4% for commercial sector, and 6% for other sectors)

Tax payable for importation = Composite assessable price (Customs completion price + Customs Duty) × Applicable VAT rate

Major tax exemptions include: the self-produced primary agricultural products sold by agricultural producing units and individuals; Contraceptive medicines and devices; Antique books; Instruments and equipment imported for direct use in scientific research, experiment and education; Imported materials and equipment granted by foreign governments or international organizations; Imported goods being processed for exportation; Articles imported directly by organizations for the disabled for exclusive use by the disabled and so on.

Table 31 Table of VAT Taxable Items and Rates

Coverage of collection	Rates
Exportation of goods (except otherwise stipulated By the State)	0%
1. agriculture, forestry, products animal husbandry, aquatic products; 2. edible vegetable oil and food grains duplicates; 3. tap water, heating cooling, hot applying, hot water, coal gas, liquefied petroleum gas, natural gas, methane gas, coal/charcoal products for household use; 4. books, newspapers, magazines (excluding the newspapers and magazines distributed by the department); 5. feeds, chemical fertilizers, agricultural chemicals, agricultural machinery and plastic covering film for farming; 6. dressing metal mineral products, dressing non-metal mineral products, coal.	13%
1. crude oil, mine salt and goods other than those listed above; 2. taxable services.	17%

Consumption Tax

Consumption tax is levied on some specific consumer goods, which is a very popular tax in the world. The current “Provisional Regulations of the People’s Republic of China on Consumption Tax” was promulgated by the State Council on December 13, 1993 and came into effect from January 1, 1994.

The taxpayers of Consumption Tax include all enterprises, units, household businesses and other individuals engaged in production, importation and/or retails of taxable consumer goods within the territory of the People’s Republic of China.

Based on different taxable consumer goods, the different flat rates, pre-assumptive fixed rate and compound rate are adopted.

Computation of tax payable is as follows.

Tax payable = Sales amount of taxable consumer goods × Applicable tax rate, or

Tax payable = Sales volume of taxable consumer goods × Applicable tax amount per unit, or

Tax payable = Sale volume of taxable consumer goods × Applicable tax per unit + Sale value of taxable consumer goods × Applicable tax rate

Tax payable for imported taxable consumer goods = composite assessable price × Applicable Consumption Tax rate (Composite assessable price = (Customs completion price + Customs Duty) / (1-Consumption Tax rate))

Major tax exemptions include:

The taxable consumer goods exported shall be exempt from Consumption Tax unless it is restricted by the State rules. No Consumption Tax is levied on aviation kerosene temporarily. 30% Consumption Tax is levied on naphtha, solvent-oil, lubricating oil and fuel oil.

Table 32 Table of Consumption Tax Taxable Items and Rates (Tax Amount per Unit)

Taxable items	Tax rates (tax amount per unit)
1. tobacco (1) Grade A Cigarettes (2) Grade B Cigarettes (3) Cigars (4) Cut tobacco	(1) *150 Yuan per box (50000 pieces) + sales value × 45% (2) *150 Yuan per box (50000 pieces) + sales value × 30% (3) *25% (4) *30%
2. alcoholic drinks and alcohol (1) white spirits made from cereal, white spirit made from potatoes (2) yellow spirits (3) beer of class one (4) beer of class two (5) other alcoholic drinks (6) alcohol	(1) *0.5 Yuan per Jin or 500ml + factory price × 20% (2) *240 Yuan per ton (3) *250 Yuan per ton (4) *220 Yuan per ton (5) *10% (6) *5%
3. cosmetics	30%
4. precious jewellery, pearls, precious jade and stones (1) gold and silver jewellery, diamond and decoration thereof (2) other jewellery, pearls, precious jade and stones	(1) *5% (2) *10%
5. firecrackers and fireworks	15%
6. finish oil products (1) gasoline: a. unleaded; b. leader (2) diesel oil, fuel oil, aviation oil (3) naphtha, solvent-oil, lubricating oil	(1.a) *0.2 Yuan per litre (1.b) *0.28 Yuan per litre (2) *0.10 Yuan per litre (3) *0.20 Yuan per litre
7. motor vehicle tyres	*3% Excluding meridian tyres and renovated tyres
8. motor-cycles (1) cylinder capacity less than 250 ml (2) cylinder capacity over 250 ml	(1) *3% (2) *10%
9. motor cars (1) passenger cars (with 9 seats or less) (2) medium and light commercial cars (with 10 to 23 seats)	(1) *3%, 5%, 9%, 12%, 20% (2) *5% Rate applied on the basis of cylinder capacity of the car
10. golf and tools	*10%
11. high-class watches	*20%
12. yachts	*10%
13. wood chopsticks for use only once	*5%
14. wood floor	*5%

Business Tax

Business tax is levied on specified profit-making causes and business activities. The current “Provisional Regulations of the People’s Republic of China on Business Tax” was promulgated by the State Council on December 13, 1993 and effective from January 1, 1994.

Taxpayers of Business Tax include all enterprises, units, household business and other individuals engaged in provision of taxable service, transfer of intangible assets or in sales of immovable properties within the territory of the People’s Republic of China.

Based on different sectors and taxable items, different flat rates are adopted.

Computation of tax payable is as follows.

Tax payable=Turnover × Applicable tax rate

Business Tax is exempt for: nursing services provided by nurseries, kindergartens, old people’s homes, welfare institutions for the handicapped, matchmaking and funeral services; services provided individually by the disabled to the public; medical services provided by the non-profit making hospitals, clinics and other medical institutions; educational services provided by schools and other educational institutions engaged in degree education, and services provided by students in part-time work; agricultural mechanical ploughing, irrigation and drainage, prevention and treatment of plant diseases and insect pests, plant protection, insurance for farming and animal husbandry, and related technical training services, breeding and the prevention and treatment of diseases of ploultry, livestock and aquatic animals; admission fees for cultural activities conducted by memorial hall, museum, science and technology hall, cultural centre, art gallery, exhibition hall, academy of painting and calligraphy, library and cultural protective units, admission fees for cultural and religious activities taking place at religious premises and so on.

Table 33 Table of Business Tax Taxable Items and Rates

Taxable items	Tax rates (%)
1. communications and transportation	3
2. construction	3
3. financial and insurance businesses	5
4. post and tele-communications	3
5. culture and sports	3
6. entertainment	20 or 5
7. services	5
8. transfer of intangible assets	5
9. sales of immovable properties	5

Note: for finance insurance businesses, in the area for experimental reform of countryside credit firm reform, the tax on countryside credit may be 3%.

Enterprise Income Tax

China's Enterprise Income Tax is a tax levied on the income of the various domestic enterprises. The current "Provisional Regulations of the People's Republic of China on Enterprise Income Tax" was promulgated by the State Council on December 13, 1993 and effective as of January 1, 1994.

Taxpayers of Enterprise Income Tax are any state-owned enterprise, collective enterprise, private enterprise, joint operation enterprise, joint equity enterprise, and other organizations within China (excluding enterprises with foreign investment, foreign enterprises, and the private enterprises and organizations of single proprietorship, partnerships nature)

The taxpayers' world-wide income from production and business operations and from other sources shall be subject to Enterprise Income Tax according to law. The Enterprise Income Tax is computed on the basis of the taxable income that is equal to the total income earned by the taxpayers in a tax year less allowable deductions for the same tax year.

Computation of tax payable is as follows.

Income tax payable = Taxable income × 33% (besides the statutory rate, two lower rates of 18% and 27% are designed for some less profitable enterprises)

Major tax exemptions and reductions include:

Enterprises operating in autonomous regions requesting for preferential treatment and incentives may be, upon the approval of the People's Government at provincial level, given tax reductions or exemptions for a specified period; Tax exemption or tax reduction may be granted to enterprises or businesses that meet the relevant rules of the State.

Income Tax on Enterprises with Foreign Investment and Foreign Enterprises (ITEFIFE)

China's Enterprise Income Tax on Enterprises with Foreign Investment and Foreign Enterprises (Foreign Enterprise Income Tax) is a tax levied on the income of the enterprises with foreign investment and foreign enterprises. The current "Income Tax Law of the People's Republic of China on the Enterprises with Foreign Investment and Foreign Enterprises" was passed and promulgated at the Fourth Session of the Seventh National People's congress on April 9, 1991, and came into effect on July 1, 1991. On June 30, 1991, the State Council promulgated the "Detailed Rules and Regulations for the Implementation of the Income Tax Law of the People's Republic of China on the Enterprises with Foreign Investment and Foreign Enterprises" that came into effect on July 1, 1991.

Taxpayers of ITEFIFE include: enterprises with foreign investment, including Chinese-foreign equity joint ventures, Chinese-foreign contractual joint ventures and wholly-foreign owned enterprises; Foreign enterprises, including foreign companies, enterprises and other economic organizations which have establishments or places in China engaged in production or business operations or which, though without establishments or places in China, have income from sources within China.

As for the tax base, the enterprises with foreign investment with head office in China pay income tax on their world-wide income. Foreign enterprises pay income tax only on their income derived from sources within China.

Tax rates and computation of the amount of tax payable are as follows.

Amount of tax payable = taxable income × applicable tax rate

33% rate (30% of the taxable income plus 3% local income tax) for enterprises with foreign investment and foreign enterprises;

20% (10% applied to interest, rental, royalties and other income) for any foreign enterprises which has no establishment or place in China but derives income of profits, interest, rental, royalties and other income from sources within China or which, though it has an establishment or place in China, the said income is not effectively connected with such establishment or place.

Individual income tax

The individual income tax is levied on the income of the individuals. The “Individual Income Tax Law of the People’s Republic of China” was passed at the Third Session of the Fifth National People’s Congress (NPC) and effective on September 10. It was revised for the third time at the 18th Session of the Standing Committee of the 10th NPC on October 27, 2005. The current “Regulations for the Implementation of the Individual Income Tax Law of the People’s Republic of China” was revised and promulgated on December 19, 2005 by the State Council.

The individual income tax payers are classified into two types:

Individual income tax shall be paid on their world-wide income by the individuals who have domicile in China or who, though without domicile in China, have resided in China for one year or more. Individual who are neither domiciled nor resident in China or who do not have domicile and are resident for less than one year in China shall pay Individual Income Tax only on the income obtained from sources within China. The taxable items of individual income tax are 11.

Table 34 The Taxable Items of Individual Income Tax

a. Wages and salaries income

Wages and salaries are taxed on the basis of the balance of taxpayer's monthly wages and salaries after lump-sum deduction of 1600 Yuan and other items ruled (at present including basic pension insurance premium, medical insurance premium, unemployment insurance premium and house reserve) as expenses and by applying the nine-grade progressive rates.

Monthly amount of tax payable = monthly taxable (monthly aggregate wages and salaries – 1600 Yuan – other deductibles as ruled) × applicable tax rate – quick deduction

The taxpayers who have no domiciles in China but earn wages and salaries from outside China may enjoy additional expense deductions (currently 3200 Yuan per month) in addition to the regular monthly deduction of 160 Yuan in computing the taxable income.

b. Individual household production or business operation income

With respect to the individual household production or business operation income, the amount of tax payable is computed on the basis of the balance of the gross annual production and business operation income after deduction of the related cost, expenses and losses and by applying the five-grade progressive tax rates.

Tax payable for the year = annual taxable income (Gross annual income of production and business – costs, expenses and losses) × applicable tax rate – quick deduction

The production and business income of the individual single proprietorship enterprises and the partnership enterprises shall be treated in reference to the production and business income of individual household enterprises for individual income tax.

c. Income from contracted or leased operation of enterprises or institutions

The income from contracted or leased operation of enterprises or institution is taxed on the basis of the balance of the gross annual income after deduction of the necessary expenses (currently 1600 Yuan per month) and by applying the suitable tax rate in "individual income tax rates schedule".

d. Remuneration for personal service, author's remuneration, royalties, income from lease of property

The income of remuneration for personal service, author's remuneration, royalties and income from lease of property are taxed on the basis of remaining sum of the income after deduction of 800 Yuan when each payment of the income is not over 4000 Yuan or on the basis of the remaining sum of the income after deduction of 20% of the income as the expenses when each payment of the income is over 4000 Yuan and by applying the rate of 20%.

Amount of tax payable = taxable income (gross income of taxable items – 800 Yuan (or 20% of gross income of taxable items)) × 20%

Where the remuneration income is very high in one payment, additional individual income tax shall be levied on that. The specific computation is : for the part of income between 20000 Yuan and 50000 Yuan, 50% additional tax shall be levied after working out the computation of the individual income tax according to the tax law, and for the part over 50000 Yuan, 100% additional tax shall be levied.

e. Income from transfer of property

The tax base is the balance of the proceedings derived from transfer of property after deducting the original value of the property transferred and the reasonable expenses. The applicable rate is 20%.

Amount of tax payable = taxable income (proceedings from transfer of property – original value of property – reasonable expenses) × 20%

f. Interests, dividends, bonuses, contingent income and other income

The tax base is each payment of the income.

Tax payable = the full amount in each payment × 20%

III.3 Non-tax Fiscal Revenue Collected By The Tax Department

According to the rules of the State Council, the items of non-tax fiscal revenue collected by the tax department uniformly include the Educational Surcharge, Mining District Charge and Culture Construction Fee. In addition, the people's government of every province, autonomous region and municipality may rule that the tax department should collect the Social insurance fee.

Table 35 The items of non-tax fiscal revenue

Item	Payers	Base and rate	Computation
Educational Surcharge	The units and individuals who are liable to payment of VAT, Consumption Tax and Business Tax (excluding those paying countryside Educational Surcharge and paying VAT, Consumption Tax on imported goods by rules)	Based normally on the VAT, Consumption Tax and Business Tax actually paid by the taxpayers and the surcharge rate is 3% (reduced by half for cigarette producers)	Educational Surcharge payable=Base × Applicable rate
Mining District Charge	The Chinese enterprises and the foreign enterprises exploiting the offshore oil resource by law in China's inland sea, territorial sea, continental shelf and other sea territory in China's jurisdiction, and the Chinese enterprises and the foreign enterprises cooperatively exploiting the onshore oil resources within China	Computed on the basis of the total output of the raw oil or nature gas of each offshore or onshore oil field, gas field respectively in a calendar year and paid in kind. The charge shall be levied at progressive rates on the part of the oil, natural gas output of the enterprise in excess of the threshold. The rate ranges from 1% to 12.5%.	Computed by year and paid by time or in installments and finalized at the end of the year
Culture Construction Fee	The various kinds of units and individuals paying Business Tax on entertainment, advertisement	Based on the Business Tax paid by the taxpayers on entertainment and advertisement and the rate is 3%	Fee payable=Entertainment and advertisement Business Tax payable ×3%
Social insurance fee	Scope of the payers		Base and rate of the fee
The basic pension insurance	State owned enterprises, city and town collective enterprises, enterprises with foreign investment, urban and township private enterprises and their employees, and the institutions managed as enterprises and their employees.		The rate for the enterprises normally should not be over 20% of the total wages of the enterprises. The rate for employees shall be 8% of the wages at maximum.
The basic medical insurance	State owned enterprises, city and town collective enterprises, enterprises with foreign investment, urban and township private enterprises and their employees, the government organs and their staff, the institutions and their employees, the private non-enterprise units and their employees, social organizations and their permanent staff.		The employers should pay the fee about 6% of the total wages of the units and the employees should pay the fee equal to 2% of the wages of the employees. The rate may change for both the employers and the employees.
The unemployment insurance	State owned enterprises, city and town collective enterprises, enterprises with foreign investment, urban and township private enterprises and their employees, and the institutions and their employees		The urban and township enterprises and units should pay the fee at 2% of the total wages of the enterprises or pay the fee at 1% of their wages. the people's government at provincial level may adjust the rate for their jurisdictions on basis of the local conditions.
The industrial injury insurance	Various enterprises and the individual households having employees. The employee themselves do not need to pay the fee.		The government may determine the rate based on the different injury risk for different sectors and decide a number of rates on basis of the use of the industrial injury insurance and the frequency of the injury for every sector. The base for computing the fee shall be the total wages of the employing units.

Note: The people's government of every province, autonomous region or municipality directly under the State Council may, based on the local practical circumstances, have the city and town individual household enterprises covered in the scope of the basic pension insurance and the basic medical insurance and have the social organizations and their permanent staff, the private non-enterprise units and their permanent staff, the private non-enterprise units and their employees and the individual households having employees in the scope of the unemployment insurance.

III.4 Organization of tax administration and collection

Division of the tax administration power

At present, the tasks of tax administration and collection are shouldered respectively by the departments of finance, taxation and Customs.

The Ministry of Finance is the macro-regulation and control department under the State Council, which is in charge of the financial revenue and expenditure, fiscal policy and the fundamental work concerning State owned capitals.

The General Administration of Customs is the administrative department directly under the leadership of the State Council in charge of the Customs in China.

The State Administration of Taxation (SAT) is the highest tax authorities in China. The SAT is the ministry-level department directly under the State Council that is the functional department in charge of the State revenue work.

Due to the requirements of the revenue sharing system, the tax organizations at and below the provincial level include offices of SAT and local tax bureaus. The SAT conducts a vertical leadership over the offices of SAT with respect to organization, size, personnel, budgets, and assists the provincial governments in a form of dual leadership over the local tax bureaus.

By the beginning of 2005, in China, there are 61 tax departments at provincial level, 30 municipal tax departments at vice-provincial level, 1027 tax departments at local level (such as city, prefectures), 5288 tax departments at county level, and 30915 tax stations (or branches). There are 844000 tax staffs in China, out of which 45700 are national tax staffs (accounting for 54.1%) and 388000 are local tax staffs (account for 45.8%).

By the beginning of 2005, the numbers of taxpayers registered with the offices of SAT and local tax bureaus are respectively 14.084 million and 17.975 million.

Table 36 Division of the tax administration power

Organizations	Items
The offices of SAT	VAT, Consumption Tax (the VAT and Consumption Tax at the stage of import shall be collected by the Customs office), Vehicle Acquisition Tax, Business Tax, Income Tax and City Maintenance and Construction Tax consolidatedly paid by the railway department, the headquarters of various banks and the headquarters of various insurance companies, Income Tax paid by central enterprises, Income Tax paid by joint operation enterprises and shareholding enterprises with investment from both the central and local enterprises and/or non-profit institutions, Income Tax paid by local banks and non-bank financial institutions, Income Tax and Resource Tax (not levied at present) paid by offshore oil enterprises, the income tax paid by enterprises, institutions registered after January 1, 2002, Income Tax paid by enterprises with foreign investment and foreign enterprises, Individual Income Tax on interest income from personal saving deposits, the Stamp Tax levied on security transactions
The local tax bureaus	Business Tax, Enterprise Income Tax, Individual Income Tax, Resource Tax, Stamp Tax, City Maintenance and Construction Tax(excluding the part collected by the SAT Offices as specified above), House Property Tax, Urban Real Estate Tax, City and Township Land Use Tax, Land Appreciation Tax, Vehicle and Vessel Usage Tax, Vehicle and Vessel Usage Plate Tax, Fixed Assets Investment Orientation Tax(stopped levying), Banquet Tax(stopped levying)
Financial departments of the Local Governments	Farmland Occupation Tax and Deed Tax (In some regions, the above taxes are collected and administered by the local tax bureaus.)
Customs	Customs Duty, Vessel Tonnage Tax, VAT, Consumption Tax on imports on behalf of the tax administration

Revenue sharing system between the central government and the local governments

In China, the tax revenue is divided into the central revenue, local revenue and the revenue shared between the central and local governments.

Table 37 Graph of Chinese Tax System (by level of budget)

Budgetary level	Type of Taxes		
Central taxes	Customs Duty, Consumption Tax, Vehicle Acquisition Tax, Vessel Tonnage Tax		
Local taxes	House Property Tax, Urban Real Estate Tax, City and Township Land Use Tax, Farmland Occupation Tax, Deed Tax, Land Appreciation Tax, Vehicle and Vessel Usage Tax, Vehicle and Vessel Usage Plate Tax, Fixed Assets Investment Orientation Regulation Tax, Banquet Tax, Agriculture Tax		
	Type of Taxes	For the Central Government	For the local governments (on base)
	VAT(excluding the part collected by the Customs on behalf)	75%	25%
	Business Tax, City Maintenance and Construction Tax	The part paid by the railway department, the headquarters of various bands and the headquarters of various insurance companies	The rest
Sharing taxes	Enterprise Income Tax, Income Tax on Enterprises With Foreign Investment and Foreign Enterprises	(except for the part belonging to the Central Government as ruled) 60% of the rest	40%
	Individual Income Tax	60%	40%
	Resource Tax	The part paid by the offshore oil enterprises (not levied for the time being)	The rest
	Stamp Tax	97% of the Stamp Tax on securities transactions	3% of the Stamp Tax on securities transactions and the rest

III.5 Comparison of the increase of tax revenue and the GDP growth

China's tax revenue increased 514.8 billion Yuan, a year-on-year increase of 20 percent, to reach 3.0866 trillion Yuan (excluding tariffs and agricultural taxes) in 2005, while the GDP growth rate in 2005 was 10.2 percent, after the latest adjustment. Why the increase of tax revenue far outpaces the GDP growth?

According to the tax authority's explanation, "The growth rate of tax revenue in 2005 is not very high if compared with the GDP growth rate calculated using current price". The phenomenon is normal when analysis is performed in aspects including growth pattern of tax revenue, price, import and export, and management of tax collection.

The first explanation lies in the existence of different criteria for statistics. Tax revenue is calculated using current price; while GDP growth rate is calculated using fixed prices (comparable prices). If taking price factor into account, China's GDP growth rate calculated using current prices will be between 13 to 14 percent. What's more, GDP structure is not the same with tax revenue structure. Tax revenue mainly comes from the secondary and tertiary industries. Leaving the value added in the primary industry out, the value added in the secondary and tertiary industries would far outnumber the GDP growth rate calculated using current prices.

Value-added tax, which represents 50 percent of the total tax revenue, could be taken as a good example. The value added in industry and commerce is the tax base for value-added tax. From January to November 2005, the value added of industrial enterprises above designated size calculated using comparable prices increased 16.4 percent. If the factory price of industrial

products is taken into account, the country's industrial value added will reach 19 percent, which is basically the same to value-added tax's increase of 19.8 percent.

Foreign trade's effect on economic growth differs from that on tax revenue growth. Increase of imports will boost increase of tax revenue. But only exports can help increase GDP. This is one factor that helps explain the phenomenon that tax revenue increase outpaces GDP growth.

Improved management of tax collection also contributes to the phenomenon. In 2005, the taxation authority strengthened management of tax collection and intensified efforts in checks, and further improved services for taxpayers. According to the statistic data provided by SAT, the tax administration departments of all levels cleared defaulted tax payment of 20 billion Yuan. The investigations of cases have helped collect tax of 36.7 billion Yuan.

IV. Country-Specific Fiscal Issue

2005 was the last year of the 10th Five-year Plan. In 2005, main targets set forth for the economic and social development at the beginning of the year had been achieved, and the major tasks of the 10th Five-year Plan had been fulfilled which had laid a solid foundation for the economic and social development for the 11th Five-year Program. The national economy kept stable and fairly fast growth; breakthrough was made in reforms in major fields and key sectors; employment and social security programs were further enhanced; the living standard of urban and rural population improved; China was opening wider to the outside world; and various social undertakings were strengthened. However, the problems, such as irrational economic structure and extensive mode of economic growth are still prominent.

The year of 2005 was also a year which witnessed many special fiscal issues taken place in China.

RMB Appreciation

On July 21, 2005, the People's Bank of China, with authorization of the State Council, made the announcements that China would move into a managed floating exchange rate regime and RMB would no longer be pegged to the US dollar. The exchange rate of the US dollar against the RMB would be adjusted to 8.11 Yuan per US dollar at that time.

The goal of RMB exchange rate reform is to establish and improve a managed floating exchange rate regime based on market supply and demand and keep the RMB exchange rate basically stable at an adaptive and equilibrium level. This is the first large adjustment of the RMB exchange rate regime since 1997.

The reform of the RMB exchange rate regime focuses on the exchange rate formation mechanism instead of only an appreciation in its level. The main content of the RMB exchange rate mechanism reform of July 21, 2005 includes a change in the exchange rate adjustment method, a change in the parity formation and an adjustment in the initial exchange rate. Since then, the exchange rate for the RMB was floated according to a basket of currencies and the relationship between supply and demand in the market. At the end of each business day after the market is closed, the People's Bank of China publicizes the closing price of the exchange rate of the trading currencies (such as the US dollar) against the RMB in the inter-bank foreign exchange market on that day, which acts as the middle price for the transaction of this currency against the RMB for the next working day. The designated foreign exchange banks could adjust the listing exchange rate for their clients.

State Share Sale Reform

Having learned from the experience in June 2001, when the government announced its plan to sell shares it held (nonnegotiable shares) to fund social security, followed by the subsequent sharp fall in share prices caused by the fear of deterioration in the demand-and-supply balance of shares

forced the government to give up its plan, in April 2005, the government, announced a new reform policy. According to the reform, the rights of holders of traded shares and their risks of decline in share prices when nonnegotiable shares are put on the market were taken to consideration. The concept of "compensation" to be paid by holders of nonnegotiable shares to holders of traded shares for the former to acquire the "rights to trade" was introduced.

Tax Reform Issues

A motion on the regulations revoking the agricultural tax was adopted on Dec.29, 2005. Since then, agricultural tax, China's most ancient tax category, which has existed for 2,600 years in China, has become a historical issue.

In 2005, the Chinese government decided to construct a "new countryside" so as to narrow the gap between city and countryside. For Chinese government, the abolition of agricultural tax was only one of the important steps to fulfill the construction of the "new countryside". The abolition of agricultural tax also sharpened the country's agricultural competitive edge in the international market.

Another important decision made by China's top legislature on Oct. 27 was to revise the personal income tax law to raise the cutoff point of the monthly personal income tax from 800 Yuan (US\$99) to 1,600 Yuan (US\$197). For Foreigners working in China, they have to pay personal income tax only if their monthly pay is above 4,800 Yuan (US\$592), up from the previous threshold of 4,000 Yuan (US\$493).The revised law goes into effect as of Jan. 1, 2006.

The new cut-off is in line with these changes as average income has been on the rise continually and dramatically. The expanding rich-poor income gap has aroused widespread concern, and hopes are pinned on personal income taxation playing a larger role in balancing out the disparity. The new legislative move is a step forward towards a more fair taxation system, to relatively reduce the tax burden on low and medium-income earners. But it is only the first step and there is still a long way to go before a mature system is established.

The 11th Five-Year Plan

The Communist Party of China Central Committee's Proposal on the Eleventh Five-year Program on National Economy and Social Development, was adopted at the Fifth Session of the 16th CPC Central Committee which ended on Oct. 11, 2005. This proposal will play a crucial role in shaping the country's development over the next five years.

The proposal attaches great importance to domestic problems including the unbalanced development of urban and rural areas, extensive mode of economic growth, irrational economic structure, weak creativity on its own, great difficulty in solving problems relating to agriculture, rural areas and farmers, great employment pressure.

V. Conclusion: Where We Stand and Where We Go?

Economic History of China

In December 1978, China decided to undertake a program of gradual but fundamental reform of the economic system. The purpose of which was not to abandon communism but to make it work better by substantially increasing the role of market mechanisms in the system and by reducing--not eliminating-- government planning and direct control.

After 3 years' period of readjustment from 1979 to 1981 China, which produced promising results, a basic policy, which was "reform and opening," that is, reform of the economic system and opening to foreign trade, was introduced in 1982.

In agriculture the contract responsibility system was adopted as the organizational norm for the entire country, and the commune structure was largely dismantled. In industry the complexity and

interrelation of production activities prevented a single, simple policy from bringing about the kind of dramatic improvement that the responsibility system achieved in agriculture. Particularly, the practice of remitting taxes on profits and retaining the balance became universal by 1985, increasing the incentive for enterprises to maximize profits and substantially adding to their autonomy. The role of foreign trade under the economic reforms increased far beyond its importance in any previous period. The most common foreign investments were joint ventures between foreign firms and Chinese units. The most conspicuous symbols of the new status of foreign trade were the four coastal special economic zones, Shenzhen, Zhuhai, Shantou, Xiamen, which were created in 1979 as enclaves where foreign investment could receive special treatment. More significant for China's economic development was the designation in April 1984 of economic development zones in the fourteen largest coastal cities. These zones were to create productive exchanges between foreign firms with advanced technology and major Chinese economic networks. Domestic commerce also was stimulated by the reform policies, which explicitly endeavored to enliven the economy by shifting the primary burden of the allocation of goods and services from the government plan to the market.

Although the reform program achieved impressive successes, it also gave rise to several serious problems, such as the challenge to party authority presented by the principles of free market activity and professional managerial autonomy, the wave of crime, corruption, the most fundamental tensions created by the widening income disparities between the people who were "getting rich" and those who were not and by the pervasive threat of inflation, and so on.

Choice of Economic Model

In the recent years, china's economy has had an important impact on the whole world. In 2003, the economic growth rate reached 9.4%, followed by more than 9% in 2004 and 2005. Growth rate of foreign trade in the successive 3 years has increased over 30%.

Faced with the rapid economic development and brisk international trade environment, what should be the suitable role of China's economy in the world? Whether China should keep making full use of the international competitive advantage to promote economic development or China should turn to the change of strategy is still a question.

Although so far China's economic model has made great progress, how to rebalance the economic development and built a new structural pattern has been taken into both the scholars and policy-makers' consideration in China.

In order to realize sustainable development, China needs to change the developmental pattern, to change the current situation of high consumption, high pollution and low output with a firm hand, to change the growth pattern thoroughly, to establish a conservation-minded industrial structure and structure of consumption step by step, heading for a conservation-minded road of development with Chinese characteristics.

Role of Globalization

After the entry of WTO, China's role in globalization has attracted more attention all over the world. The year of 2005 was a year seeing China fully entered into the globalization.

However, trade brush between China and other countries remains a serious problem. China should learn from the past, to establish early warning mechanism and coordination mechanism as well as corresponding relief mechanism in order to improve the odds-on in the negotiation and trade dispute solution. The most important measure is to change the growth pattern of foreign trade and improve the trade environment, rather than simply depending on the extensive economy and the scale economy with low prices to increase the market sharing.

The large surplus in the balance of payments also has some adverse impacts on macro-economic operations. First, the rapid expansion of exports of goods with high investment, consumption, and pollution imposed greater pressures on domestic resources and the environment, and adversely affected the changes in the mode of economic growth and the restructuring process. Second, the

rapid rise in the surplus in foreign trade and foreign exchange reserves tended to cause trade frictions between China and the relevant countries and regions. Third, the large surplus stimulated an uninterrupted increase in the monetary supply and excessive market liquidity. Consequently, it may contribute to a more fragile banking system and create pressures from the rebounding of fixed-asset investments and the rapid rise in asset prices, restricting the positive and effective macro-control functions.

Low cost and low price is the current key advantage of competition for most of the Chinese corporations. However it should not be the single way to exploit the international market and the only profit point of foreign trade for a long period. The fundamental way for Chinese companies to deal with the trade brush in the international market should focus on the high level of brands and high technology.

To be specific, Chinese government should focus on the major obstacles in the field of foreign trade. Firstly, China should deal with pressure from international markets that are gradually becoming saturated since the growth of Chinese exports is increasingly subjected to international markets. Secondly, Chinese government should deal with the conflict between low cost of Chinese exports and the protection of workers' welfare, resources and the environment. Thirdly, increasing international trade protection has caused China to stumble into difficult territory. Finally, the trade imbalance between China and other countries is getting worse. As the RMB appreciates, Chinese enterprises will face greater exchange risks in import-export trade. Increasing pressures from the appreciating RMB will create new requirements and challenges for Chinese enterprises engaged in import-export trade.

Outlook of China's Economy in 2006

China has made remarkable economic progress since the reforms began in 1978. For the past twenty years, the Chinese economy has achieved a growth rate averaging about 10 percent every year. From 1998 to 2003, the proactive fiscal policy and prudent monetary policy had made China successfully got rid of the impact of financial crisis in Asia in 1997 and brought China's economic development into a increased stage. Macroscopic readjustment and control in 2004 and 2005 prevented China from goods and materials shortage and inflation which would be easily caused by the rapid growth of economy. Currently, China is on the fast developing period from 1000 US dollars per capita to 3000 US dollars.

On the other hand, challenges from some significant risks and imbalances should not be ignored. The principal risk arises from the problem of misallocated capital with low possible returns, leading potentially to slower growth and future financial stress. The principal imbalance lies in the composition of Chinese GDP, which is heavily tilted toward investment and net exports and away from domestic consumption and government provision of social services. One of the remaining targets in the near future is to improve capital markets and reduce the imbalance by taking measures to expand domestic demand, especially household consumption.

Under the great effort of changing consumption structure, industry structure and rapid urbanization, with the strategies of "Development of the West Regions", "Growing up of the Middle Part" etc, by implementing "The 11th Five-Year Plan", we strongly believe that Chinese economy in 2006 will continue to attain rapid, sustainable and healthy development.

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