

23 March 2003

From 5 to 18 March 2003, the 10th National People's Congress (NPC) convened for its 1st Session in China's Capital. The assembly elected a new political leadership and approved important changes in the organization of government. There was little room for surprise in any of the NPC's decision, as the most important questions had been answered four months earlier by the 16th Congress of the Communist Party of China. Nonetheless, the new government slightly shifts focus from all-out to balanced development, recognizing urban unemployment and rural development as critical challenges for China's social stability. 2003 macroeconomic objectives are cautiously optimistic. From the point of view of foreign companies doing business in China, the results of the NPC's Session are positive.

1 Smooth transition from 3rd to 4th generation leaders completed

China's top legislature elected a younger generation of leaders, the last major step in a sweeping transition that has been in the making for some time. The election of the president and vice-president of the People's Republic of China, the chairman of the Central Military Commission, the chairman and vice-chairpersons of the NPC Standing Committee followed the single-candidate system. All the newly elected top leaders received landslide votes from the legislators.

President	<u>Hu Jintao</u> , 60, claims the post of president four months after ascending to the No. 1 position in China's Communist Party, the most powerful position in the land.
Vice President	<u>Zeng Qinghong</u> , 64, has been Jiang Zemin's closest aide for more than a decade - dating to Jiang's days as mayor and party boss in Shanghai.
Premier	<u>Wen Jiabao</u> , 60, the No. 3 man in the CPC, follows in Zhu Rongji's footsteps. He has to lead the government through the next stage of restructuring and to continue the opening the economy to the outside world.
State Council	Members: <u>Huang Ju</u> , <u>Wu Yi</u> , <u>Zeng Peiyan</u> and <u>Hui Liangyu</u> as vice-premiers; <u>Zhou Yongkang</u> , <u>Cao Gangchuan</u> , <u>Tang Jiaxuan</u> , <u>Hua Jianmin</u> and <u>Chen Zhili</u> as state councilors; <u>Hua Jianmin</u> as secretary-general.
NPC Chairman	<u>Wu Bangguo</u> , 61, the No. 2 man in the CPC, succeeds as Chairman of the NPC, a ceremonial post that nonetheless reflects his power in the inner-circle hierarchy.
Head of Military Commission	<u>Jiang Zemin</u> , 76, stayed on as leader of the government's military commission and is expected to wield significant influence from behind the scenes. Some observers suggest that Mr. Jiang's decision to keep that post may put into question the new party hierarchy and the stability of Mr. Hu's leadership.

2 Government Reorganization for improved efficiency

A restructuring aimed at streamlining decision-making and taking government further out of micromanaging the economy was the most significant nonpersonnel decision approved by the NPC. It is the second such government revamp in five years and reflects China's continuing efforts to adapt its

¹ This report is a compilation of a large number of articles published by Chinese and international media. It concentrates on issues relevant for the economy. For a comprehensive overview over all aspects of the 2003 NPC and CPPCC Sessions you may visit http://english.peopledaily.com.cn/zhuanti/Zhuanti_327.shtml

state planning apparatus to an economy in which private and foreign companies play an increasingly important role. The planned changes mainly clarify bureaucratic responsibilities. Nonetheless China is keeping a level of economic planning that is far greater than the norm in most market economies. Also, the restructuring does not represent a challenge to the political control of the ruling Communist Party. Some of the most important changes concern the following agencies:

State Asset Management Commission	<u>SAMC</u> will take over the daily management of state-owned enterprises. There are an estimated 180'000 SOEs worth CNY6 trillion, but reforms have stalled in recent years because of complicated cross-ownership of many of these firms. A key point concerns the division of state assets between the central government and local authorities. Some cities and provinces are reported to have already started selling off state assets out of fear that they could be put under the control of SAMC and its branches at the local level.
China Banking Regulatory Commission	<u>CBRC</u> takes over the regulatory role from the People's Bank of China. The bank will now only be responsible for monetary policy. CBRC will exercise unified supervision and control of banks, property management companies, trust and investment corporations as well as savings deposits financial institutions
State Development and Reform Commission	<u>SDRC</u> replaces the State Development Planning Commission and several similar departments. SDRC's main responsibilities are: drafting and organizing the implementation of national economic and social development strategy, long-term program, annual plan, industrial policy and price policy, monitoring and regulating national economic operation, keeping a balance of economic aggregate, optimizing major economic structures, arranging major State construction projects, and guiding and advancing economic system reform
Ministry of Commerce	China's division between domestic and foreign trade was a copy of the former Soviet Union's system and did not conform to the WTO requirements. Hence, <u>MoC</u> will take over the duties of MOFTEC as well as the price supervisory duties of the SETC. Its main responsibilities are: studying and formulating policy regulations on standardizing market operation and circulation order, expediting the establishment and perfection of a market system, deepening the reform of the circulation system, monitoring and analyzing the conditions of market operation and commodities supply and demand, organizing and carrying out international economic cooperation, organizing and coordinating matters relating to anti-dumping and anti-subsidies and investigation into industrial damages. <u>Lu Fuyuan</u> , 58, became the country's first commerce minister. He moved into the central government in 1993, when he was appointed director general of the auto industry department of the Ministry of Machinery Industry; most recently he served as Party secretary and deputy head of Moftec.
State Food and Drug Administration	<u>SFDA</u> 's main responsibilities are: continue to exercise the function of the SDA, supervise the management of safety of food, health products and cosmetics, organize and carry out investigation and prosecution of major accidents
State Administration of Work Safety	The existing agency will be upgraded into an institution directly under the State Council and will take charge of comprehensive supervision and management over safety production and strengthen supervision over coal mining safety

3 2003 Budget and Economic Performance Targets

China's **deficit** for 2003 is budgeted to be CNY10 billion more than in 2002. The total receipt of the central finance is budgeted to be CNY1.194 trillion, up 5.1%, and the total expenditure is budgeted at CNY1.5138 trillion, up 4.7%, leaving a deficit of CNY319.8 billion. The deficit, plus the domestic and foreign debts overdue, will bring the total debts of the central finance up to RMB 640.4 billion. Putting the budgets of the central and local finances together, the total national receipt in 2003 will be CNY2.0501 trillion, up 8.4%, and the national total expenditure will be CNY2.3699 trillion, up 7.7%. The government clearly declared its intention to continue supporting economic growth by deficit deepening fixed asset investment. Meanwhile the budget also signifies a slight shift toward creating a welfare net to ensure social stability in the face of worsening unemployment. While a rein has been

put on the deficit, the spending mix has also been altered with major allocations to poverty alleviation rather than big-ticket construction projects. Budget allocations for poverty relief includes CNY43.5 billion for projects such as rural tax burden reform as well as benefit rises for both retiring state firm employees and urban welfare recipients.

Although the government's **debt ratio** stands at about 30% of GDP, considered low among developing countries, the real debt ratio could be as much as 70% to 100% of GDP according to a World Bank report. Taking into account the sum the government owes to retired workers in the form of social security benefits, together with the burden of non-performing loans at state banks, the nation's debt is likely to be at least 50% of GDP. The Asian Development Bank estimates China's implicit pension debt to be as high as USD1.5 trillion or 150% of GDP.

The outgoing Government announced the **macroeconomic regulatory targets for 2003**. Nevertheless, they will be the basis for the new team's policies and the yardstick for their success:

- Economic growth rate at 7%
- Over 8 million new jobs for urban residents; registered urban unemployment rate under 4.5%;
- Rise in the consumer price index of no more than 1%;
- Fixed asset investment growth will fall 4.1 percentage points on-year to 12% in 2003
- Increase in the total import and export volume of 7% (compared with 21.8% for 2002)
- M2 broad money supply and M1 narrow money supply will increase by about 16% on-year
- Rural income growth: 4% (2002: 4.8%); Urban income growth: 6% (2002: 13.4%)
(2002 per capita disposable income is CNY7'703 for urban residents, CNY2'476 for rural residents)

3 New Government underlines need for balanced development

In their reports, members of the outgoing government mentioned the **challenges** they had left behind for the next administration: weak domestic demand, irrational supply structure, insufficient growth in rural incomes, rise in unemployment, delayed expansion of the consumer market, income inequalities, tough reforms for state-owned industries, chaotic order of the market economy, industrial accidents, degradation of the environment and waste, red tape and "extravagance" by officials. Observers would add to the list the looming crisis in China's banking sector, the lacking security system and the fiscal revenue gap.

Newly elected Premier Wen Jiabao confirmed that his government would continue the strategic restructuring of the economy and the opening up to the outside world. In order to maintain a sustainable and comparatively rapid development of the national economy, the government will stick to the policy of expanding domestic demand through proactive fiscal policy. Wen Jiabao also stressed the necessity of giving priority to the development of the rural economy, and of promoting a coordinated and well-balanced development between urban and rural areas. China will strive for a proper balance among development speed, dimension of reform and social bearing capacity in order to realize the perfect integration of reform, development and stability, he said. Furthermore, he pledged to support the growth of enterprises in the non-public sectors. Private enterprises shall be treated like enterprises in the public sector with regard to market access, taxation, bank loans and import and export, said Wen.

4 Analysis

In November of last year, the 16th Congress of the Chinese Communist Party already decided all the important questions with regard to the impending leadership change. This year's NPC session merely confirmed the remarkable fact that the People's Republic accomplished the first orderly transfer of authority since its inception in 1949. **Stability** remains the paramount principle, much to the satisfaction of a majority of the Chinese people, many of who have suffered terribly during the PRC's more tumultuous past. The fact that the outgoing President retains potentially strong influence does

not necessarily challenge the new leadership's authority, but may be seen as an additional guarantee for continuity.

During the NPC sessions, it became clear that the **economy remains the priority** of the new central government. While they will basically continue the policies of their predecessors, they may refocus on a **more balanced development** in order to ensure social stability. Following the logic of stability, the new government will hardly resort to drastic measures of reform, and we may see a slow-down in economic restructuring to allow more time for the government to rollout an adequate social safety net. Naturally, the declarations of the new Premier remained very general so far, and it remains to be seen what kind of measures the new leadership will take to implement its policies and tackle the challenges ahead.

The new government accepts the importance of the **private sector**, which currently contributes an estimated 30% of GDP, and of small and medium-sized enterprises as the main source of job creation. In spite of the governments proclaimed good intentions to improve the business environment of the private sector, it remains to be seen how successful it will be in creating a level playing field for private and State owned enterprises. The reorganization of various government agencies looks like a step into the right direction. Away from multiple layers of badly coordinated and often contradicting regulating bodies to a more streamlined bureaucracy which should **facilitate administrative procedures** for the market players. In an immediate future companies may experience even more uncertainties and delays, as the bureaucrats scramble for position and influence within the new set-up. Eventually, we may see a more decentralized and efficient bureaucracy excluded from economic micromanagement and restrained to regulatory functions.

By and large, the results of the 2003 NPC sessions are **good news for foreign companies** doing business in China. The government stands for political continuity, pursues social stability and pledges continued reform and opening up of the economy, all of that is important for the development of a foreign business in China. Just like the local entrepreneurs, foreign companies will enjoy the government's increasing respect for the private sector as well as any improvement of the bureaucracy's efficiency and predictability. Meanwhile, some foreign investors may be disappointed about temporary setbacks in the reform process, induced by the government's new focus on balanced development. Furthermore, the end to discrimination of foreign market players may still be a long way off, in particular when dealing with local governments and courts of law.
