Prospects for promoting China's internal demand: Some issues calling for clarification

Gang LU
Development Research Center of the State Council of China

From 2004 when the Central Economic Work Conference first propounded the idea of "promoting the transformation of the economic growth pattern", to 2007 when the Seventeenth National Congress of the Communist Party of China clearly pointed out that China is going to "accelerate transformation of the mode of economic development, pursue the policy of boosting domestic demand, particularly consumer demand, and propel the transition in the mode of economic growth from relying mainly on investment and export to relying on a well coordinated combination of consumption, investment and export", propelling domestic demand has gradually become a hot issue concerning China's economy. Against the backdrop of the current global financial and economic crisis, due to the decrease of US import demand, various countries and regions displayed a more urgent expectation for China's domestic market and thus the issue of china's internal demand has attracted even more attention from the international community. Hence come many doubts and questions. This paper tries to explain some them.

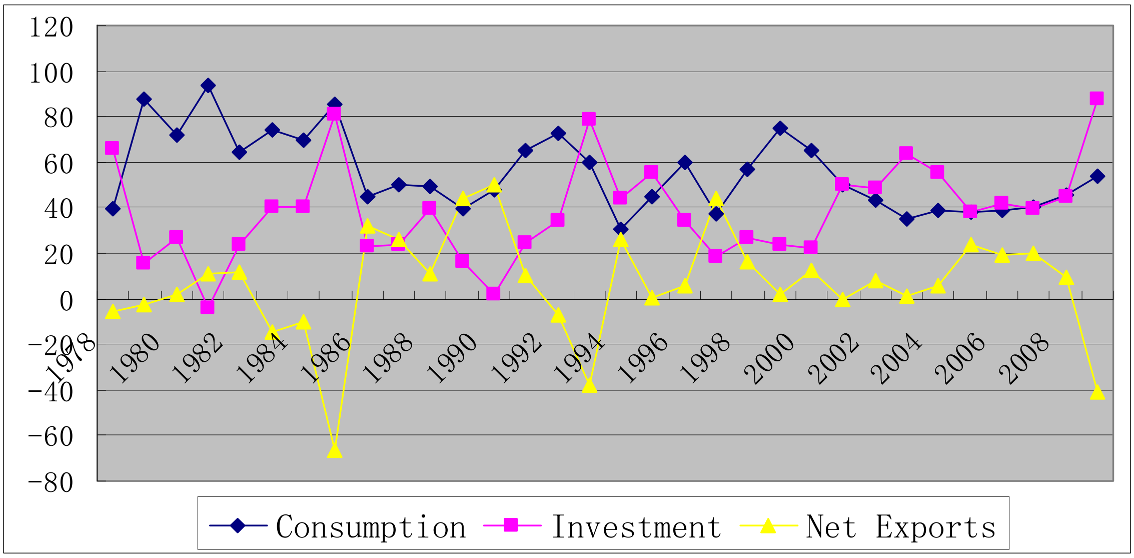
Question 1: The global financial crisis has led to China's great efforts to stimulate investment. Would this prevent China from expanding domestic consumption?

Answer: The financial crisis has not changed China's long-term policy target of expanding domestic consumption.

- It is true that China is stimulating investments in order to deal with the financial crisis, but it should be noted that the abrupt increase in the contribution rate of investment to economic growth at present is only temporary and does not necessarily mean the fundamental change of the economic growth route of China in the mid- and long-term period.

Since 2004, when China first raised the idea of changing its economic growth mode during the central economic work conference, the contribution of investment to the country's real GDP growth has dropped significantly. The contribution rate was 64.5% in 2003, but dropped to 39.3% in 2005 and remained afterwards at roughly 40% until 2008. Over the first half of 2009, however, the situation changed dramatically. During this period, China's real GDP witnessed an increase of 7.1% on a year-on-year basis, including an increase of 6.2 percentage points produced by investment, which means the contribution rate of investment has suddenly jumped to as high as 87.3%, surpassing the last two peaks which appeared in 1985 and 1993, respectively. Therefore, it is safe to say that now China is again relying mainly on investment for its economic growth.

Figure 1 Contribution rate of consumption, investment and net exports to China's real GDP growth (%)



Source: National Bureau of Statistics of China.
Note: Calculated at constant price. Contribution rate refers to the ratios between the increments of the three types of demands to the GDP increment by expenditure approach. The figures for 2009 stand for the first half year.

However, it is worth noting that the contribution of consumption is still on the rise, although slowly, continuing the upward trend since 2004. In the 7.1 percentage points of China's GDP growth in the first half of 2009, 3.8 percentage points is produced by consumption, with a contribution rate of 53.5%, which is the highest level in the last five years. On the other hand, net exports of commodities and services contributed an increase of -2.9 percentage points to GDP growth, producing a contribution rate of -40.8%. Therefore, it can be clearly seen that although the role of investment enhanced considerably in China's GDP growth, the role of consumption also maintained its upward movement, indicating that the rapid increase of investment is only a result of the government's temporary economic stimulation policies which are intended to offset the adverse impact on economy produced by abrupt decrease of exports. The growth of consumption is still stable and healthy.

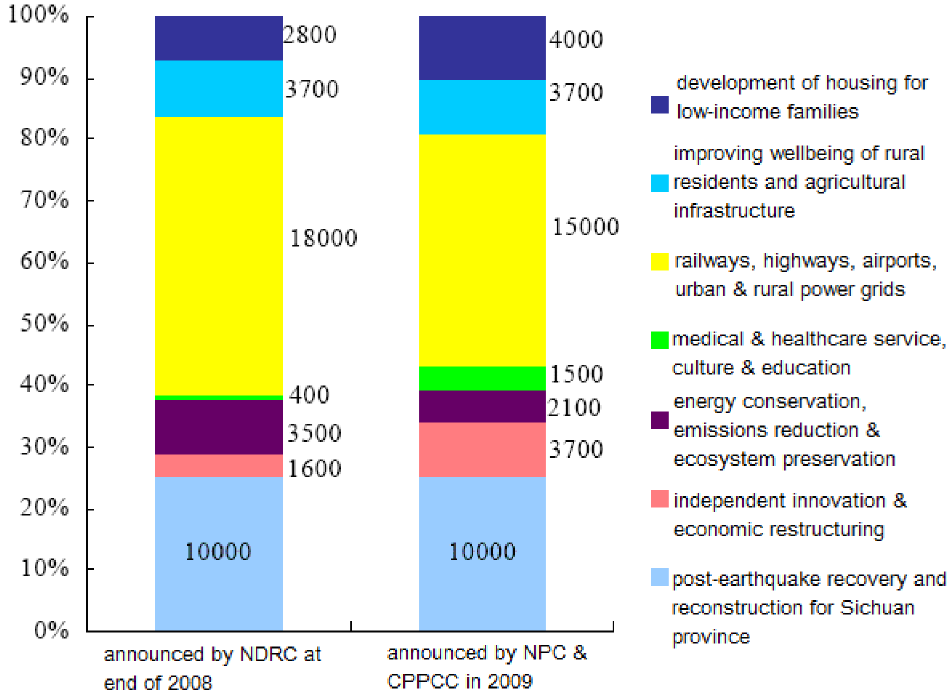
- ■ Transformation of the economic development mode is a strategic decision made by the Chinese government based on the recognition of the unsustainability of China's current economic development mode. This decision does not and will not change due to the financial crisis.

During the 17th National Conference of the Communist Party of China held in October 2007, shifting the country's economic development mode was formally set as a strategic goal. In place of investment and export-led development, the conference declared that China will adopt a more balanced growth path that relies more on domestic consumption. This shows that China's policy makers have made up their minds well before the financial crisis that changing growth mode is a must if China wants to achieve sustainable growth.

The meeting of the Political Bureau of the Central Committee of the Communist Party of China (CCCPC) held on November 28, 2008 made "ensuring growth, expanding domestic demands and adjusting structure" as the aims of the economic work of 2009. The China Monetary Policy Report for Quarter Four, 2008 issued by People's Bank of China (PBOC), China's central bank, on February 23, 2009 indicated that "in the context of a weakening external demand and an accelerating adjustment of the global economic imbalances, the fundamental approach to achieve stable and relatively rapid economic growth is to expedite economic restructuring and reform focusing on expanding domestic consumption demand." Both actions indicated that faced with the global financial crisis, China's policy makers have not changed the designated strategic aim of expanding domestic consumption.

■ Judging from actions, expanding consumption demand is no less important than stimulating investment in China's counter-crisis measures.

Figure 2 Composition of the 4 trillion Yuan Economic Stimulus Package for 2009 and 2010 (Unit: RMB 100 million)



Source: National Development and Reform Commission (NDRC), National People's Congress and CICC Research

In the 4 trillion Yuan Economic Stimulus Package for 2009 and 2010 unveiled by China in November 2008, the total amount of investment on the development of housing for low-income families, the project to improve the wellbeing of rural residents and agricultural infrastructure development, and the post-earthquake recovery and reconstruction scheme for Sichuan Province reached 1.65 trillion Yuan. These three programs are indeed investment projects, but they will substantially enhance the consumption capacity of the residents by improving the social public services. The Second Session of the 11th National People's Congress (NPC) of China held in March 2009 also made structural readjustment to the 4 trillion Yuan Economic Stimulus Package by adding investment of 120 billion Yuan on the development of housing for low-income families, thus making the total amount of investment on the three above projects reaching 1.77 trillion Yuan. When coupled with the investment of 150 billion Yuan on the medical and healthcare service system and culture and education system, the amount of investment related to the expansion of consumption demand in the 4 trillion Yuan investment amounts to 1.92 trillion, nearly half of the total investment.

- The financial crisis has actually promoted the reform in the key fields of medical and healthcare service system, culture and education system and social security, which will weaken the residents' motivation to make precautionary savings and promote consumption in the mid- and long- term.

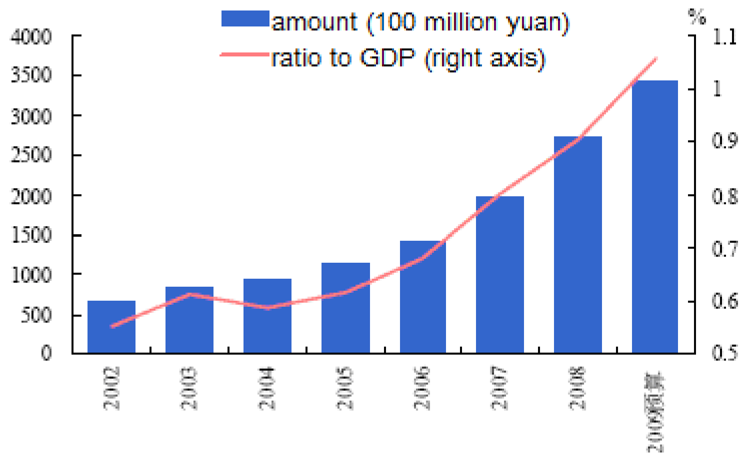
The investment in the medical and health care service system and culture and education system is seemingly small in the 4 trillion investment project, and the investment only increased to 150 billion Yuan after readjustment from the initial amount of 40 billion Yuan. However, on the Second Session of the 11th National People's Congress (NPC) held in March 2009, Premier Wen Jiabao announced a series of major actions for the reform of China's public healthcare system in his Report on the Work of the Government. Urban residents will be covered by basic medical insurance for urban workers or basic medical insurance for non-working urban residents, and rural residents will be covered by the new type of rural cooperative medical care system. These programs will cover over 90% of those eligible within three years. In 2009, the government will formulate and promulgate a unified national basic drugs catalog and adopt policies concerning their production, distribution, pricing, use and insurance reimbursement in order to ease the burden on patients for the cost of basic drugs. In the coming three years, the central government will allocate funds to support the building of another 5,000 health clinics in central villages and towns, 2,000 county-level hospitals and 2,400 community health service centers in urban areas. The government will steadily promote equal access for all to basic public health services and will expand the scope of free public health services. Governments at all levels will allocate an additional 850 billion Yuan in the next three years, including 331.8 billion Yuan from the central government, to ensure smooth progress in the reform of the system of medical and health care.

As regards education system, Premier Wen announced that the government will increase public expenditures on rural compulsory education to 300 Yuan per primary school student and 500 Yuan per junior high school student. He promises the government will progressively ensure that children of rural migrant workers have access to free compulsory education in their parents' working places.

Apart from the medical and health care service system and the culture and education fields, China will also further increase the investment in social security. Premier Wen also claimed in his report that the government will improve the basic endowment insurance system and comprehensively extend the approach of "planning as a whole at the provincial level". The pilot projects for establishing a new type of endowment insurance system for rural residents will cover approximately 10% of the counties and county-level cities in the country. The government will introduce a method for transferring pension accounts for workers moving from one region to another, expand coverage of social security programs and increase social security benefits. The government will continue to raise the amount of basic pensions for enterprise retirees by an annual average of about 10% per person for the next two years. The government will continue to increase unemployment insurance benefits and workers' compensation. The government will extend greater financial support to both urban and rural recipients of cost of living allowances and to childless and infirm rural residents who receive subsidies for food, clothing, medical care, housing and burial expenses."

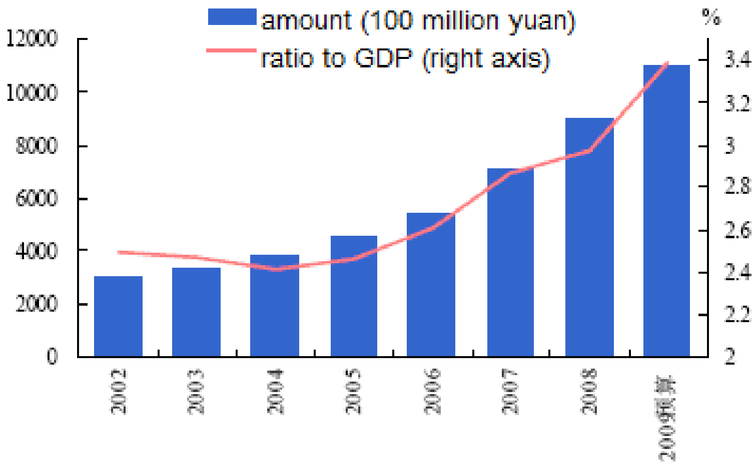
The investment in the medical service system, education and social security in China's financial budget for 2009 will reach 341.56 billion Yuan, 1094.66 billion Yuan and 833.07 billion Yuan respectively, increasing by 25.5%, 22.5% and 23.1% respectively, which increased much faster than the average speed of 2003-2008 (see figure 3~5). This fully indicated that China is increasing, not decreasing, her efforts to expand domestic consumption demand.

Figure 3 National public finance expenditure on medical and healthcare service



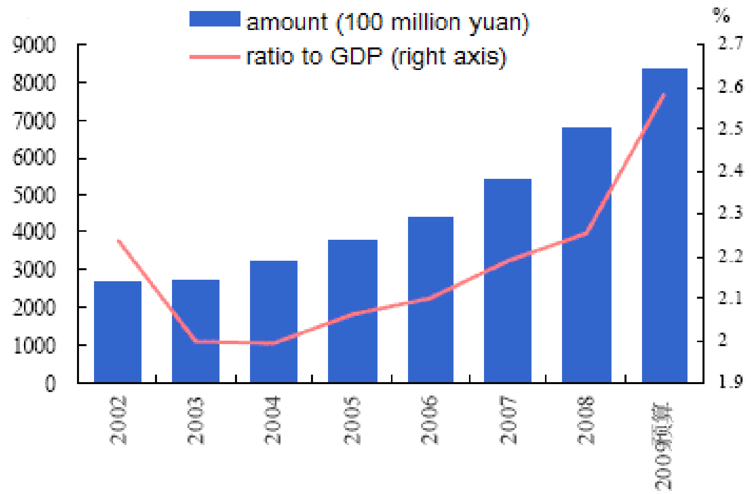
Source: Ministry of Finance of China.
Note: Figure for 2009 refers to 2009 budget.

Figure 4 National public finance expenditure on education



Source: Ministry of Finance of China.
Note: Figure for 2009 refers to 2009 budget.

Figure 5 National public finance expenditure on social security and employment



Source: Ministry of Finance of China.
Note: Figure for 2009 refers to 2009 budget.

■ Against the backdrop of the crisis, other reforms to expand domestic consumption are also being promoted.

In this regard, a good example is the notification made by the People's Bank of China in March 2009, which vows to "promote consumer credit and expand and preserve the consumer credit market". The regulator for China's financial market will "collectively boost the credit consumption in such industries closely related with the wellbeing of the people as autos, houses, household appliances, education and tourism", "guide the financial institutions to introduce new consumer credit products", "encourage to set up consumption finance companies in areas where conditions are ripe", encourage and support the commercial banks and auto finance companies conduct business cooperation from various aspects", "support qualified auto finance companies to issue finance bonds", and "expand the scale of auto loan securitization and broaden the auto finance companies' access to financial resources".

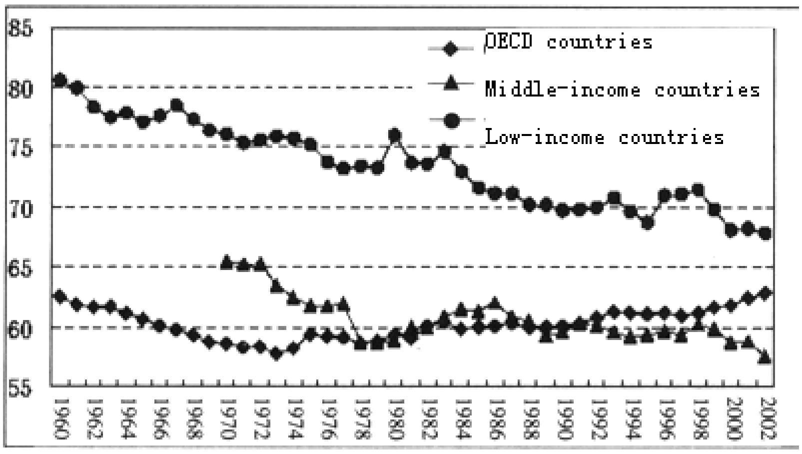
Question 2: China has enhanced its effort to expand domestic demand. Does this mean that a rebalancing between the economies of the US and China can be achieved in the near term?

Answer: It is unrealistic to expect China to complete the mission of shifting its economic development mode in three or five years.

- Basically, consumption is decided by peoples' income level. China's per capita income is still low although it has increased a lot since 1978.

A research group from the Development Research Center (DRC) has found that a country's consumption rate usually follows a "down-up-level off" pattern, with the development of industrialization and the increase of personal income. For example, the consumption rate of OECD countries kept decreasing during the period of 1960-1973 and then kept going up in 1974-1986.

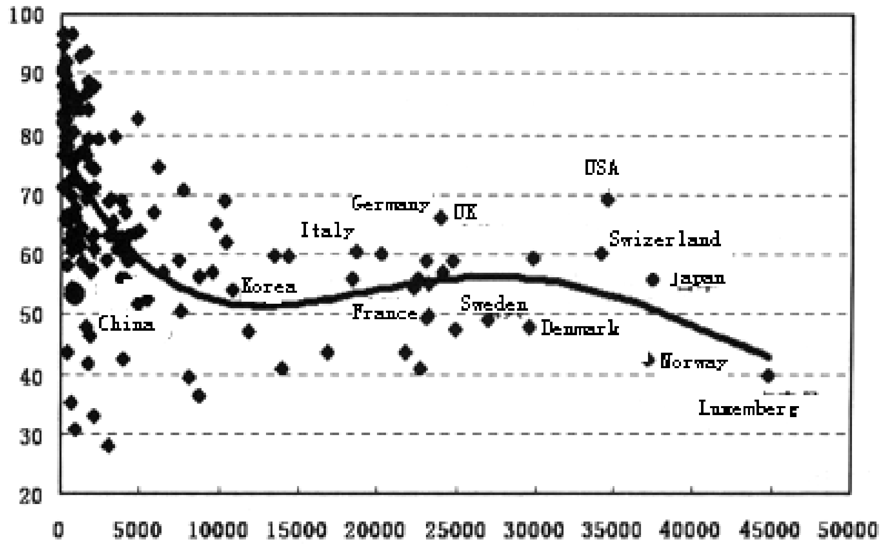
Figure 6　Characteristic of the changing patter of consumption rate



Source: "China: Looking for new breakthroughs in fighting the crisis", DRC research group, *Management World*, Issue 6, 2009.

By a comparison of 168 countries data for the year of 2000, the research group of DRC has also found that low-income countries tend to have the highest consumption rate and middle-income countries tend to have the lowest consumption rate. High-income countries' consumption rate tends to be between the former two groups of countries.

Figure 7 Relationship between per capita GDP and consumption rate



Source: "China: Looking for new breakthroughs in fighting the crisis", DRC research group, *Management World*, Issue 6, 2009.

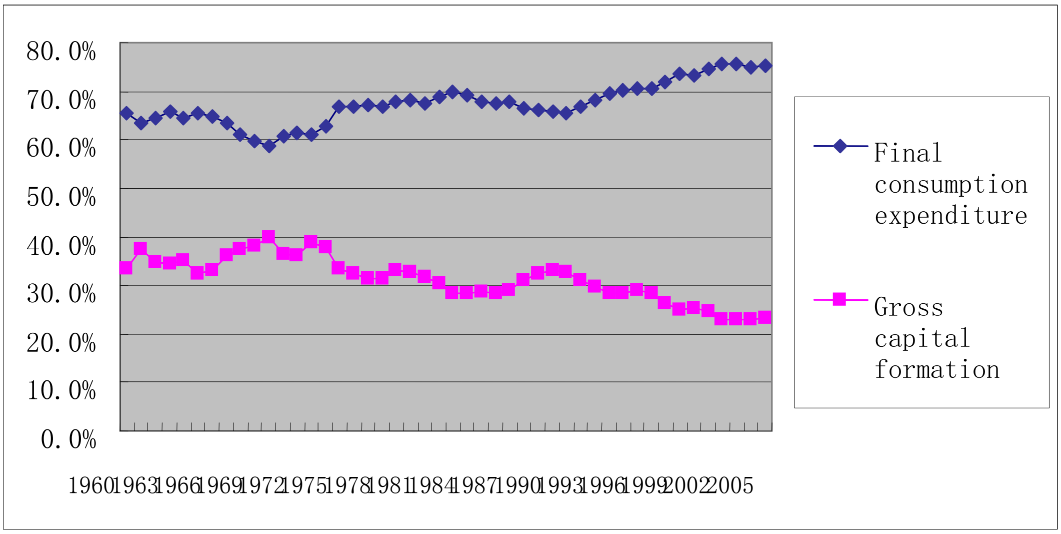
Even if calculated by PPP standards, China's per capita GDP in 2008 is only 5962 USD, ranking 101st in 182 economies in the world[1]. Therefore, China is currently only a middle-income country and is at a stage of low consumption rate.

■ It is a common phenomenon that investment rate goes up and hence drags consumption rate down during the process of industrialization. The process of industrialization has not been completed in China.

Since industrialization needs huge amount of investment, a country's investment rate tend to be high when it is trying to become an industrialized economy. From the experience of East Asian economies such as Japan, Korea and Singapore, we can easily find this rule.

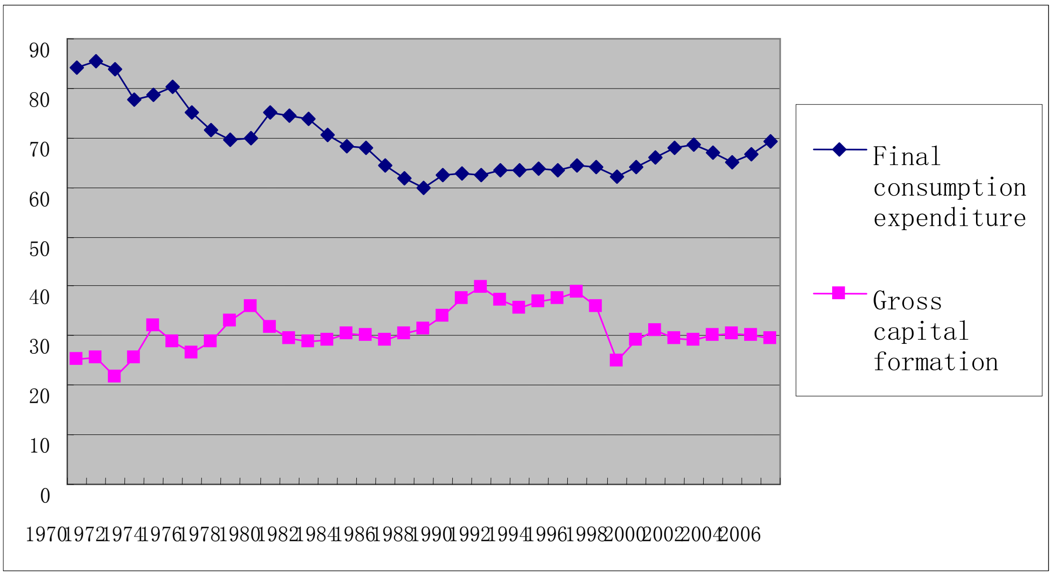
[1] CHINA ECONOMIC WORLD RANKING REPORT, Issue 2, August 2009.

Figure 8 Investment rate and consumption rate of Japan



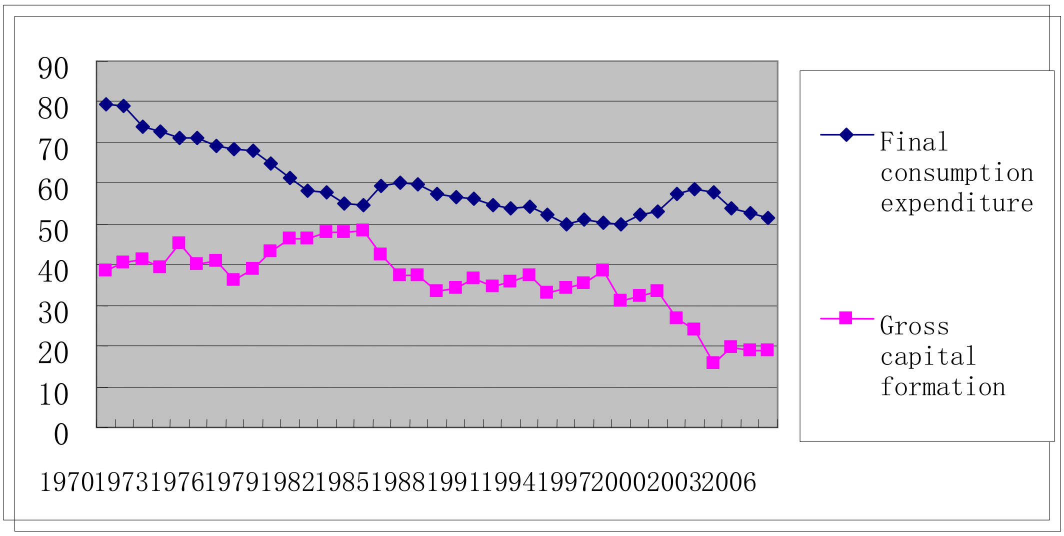
Source: World Bank.

Figure 9 Investment rate and consumption rate of Korea



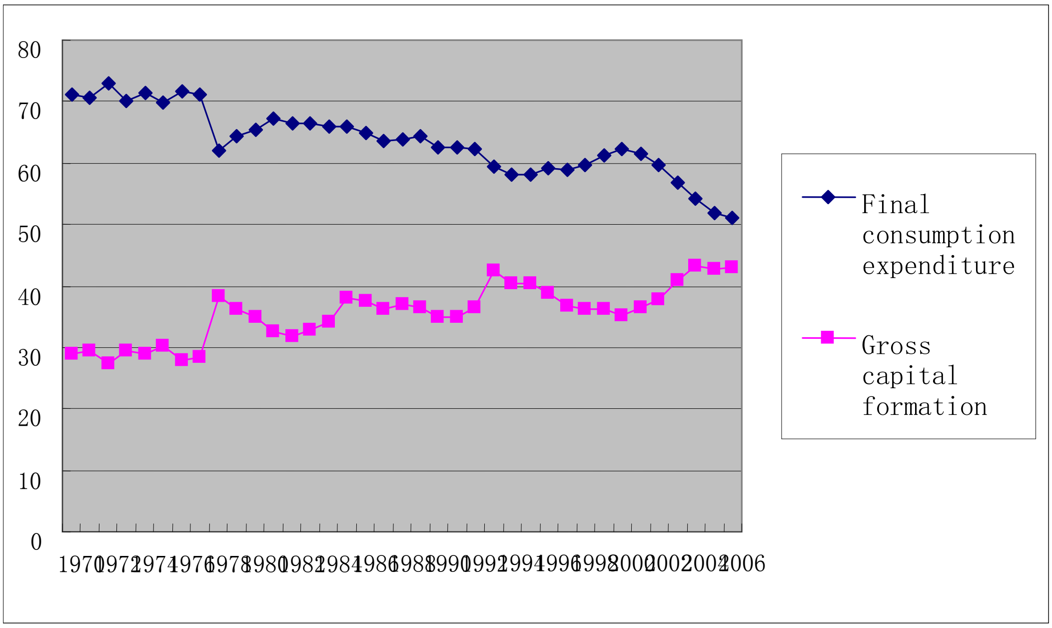
Source： UNCTAD.

Figure 10 Investment rate and consumption rate of Singapore



Source: UNCTAD.

Figure 11 Investment rate and consumption rate of China



Source: UNCTAD.

Judging by the share of industry in GDP, it seems that China's industrialization is already at a very high level. In 2007, industry accounted for 43.5% of China's GDP. This ratio is almost the highest when compared with the historical high levels of many industrialized or newly industrialized countries.

Table 1 Highest level of the share of industry in GDP

	Share（%）	Year
UK	36.3	1970
Germany	39.1	1970
Australia	30.1	1970
Japan	38.8	1970
Sweden	30.9	1974
Italy	32	1976
France	28.4	1978
Canada	30.5	1979
Switzerland	26.1	1980
South Africa	45.2	1980
USA	29.3	1981
Hungary	37.9	1982
New Zealand	27.2	1982
Brazil	35.5	1984
Israel	24.7	1984
Taiwan Province of China	43.4	1986
Mexico	31.4	1987
Korea	34.5	1987
Singapore	32.2	1988
Poland	43.4	1990
Russia	39.7	1991
India	22.7	1995
Malaysia	45.9	2006
Thailand	41.4	2006
China	**43.5**	**2007**

Source：Research report, Galaxy Securities.

However, from the perspective of technology level, there is still a big gap between China's industry and advanced countries. As can be seen from Table 1, China's exports of electronic and IT products are mainly in the form of the processing trade which accounted for 87% in 2005. Although electronic and IT industry itself is capital-intensive and can raise labor productivity, limited values are created in processing and assembling activities, which are no more than a labor-intensive link in the global value chain, since a great quantity of technology-intensive manufacturing equipments and key parts and components come from abroad. This judgment can be substantiated by examining foreign-invested enterprises (FIEs)2 in China as most of them are engaged in processing trade production. According to China Statistics Yearbook, the overall labor productivity, or the industrial value added per capita of FIEs in China's manufacturing sector of electronic and telecommunication equipment in 2005 is RMB 143,000, against RMB 38,000 for those FIEs in the manufacturing sector of textile, apparel, footwear and caps. However, the ratio of value added to gross industrial output value for the first group of enterprises (20.1%) is remarkably lower than the second group of enterprises (29.4%). Therefore, although the electronic and IT products China exported are indeed technology-intensive, the value added through processing trade production is still limited. China is still at the low end of TNCs' global production chain, which includes R& D, design, key parts manufacturing, processing and assembling.

Table 2 Comparison of China's export structure with developed countries

	China				**Korea**	**Germany**	**Japan**	**US**
			2005					
Technology Level	1996	2001		in which processing trade	2004	2004	2004	2004
Primary products	10%	7%	4%	1%	2%	5%	1%	9%
Resource-based products	11%	9%	8%	3%	10%	12%	7%	14%
Agro-based	5%	4%	3%	1%	3%	6%	2%	6%
Other	6%	5%	5%	1%	8%	6%	5%	8%
Low technology manufactures	45%	40%	31%	11%	10%	12%	6%	10%
Textiles, garment & footwear	30%	25%	18%	6%	5%	3%	1%	3%
Other	15%	15%	13%	5%	4%	8%	5%	7%
Medium technology manufactures	19%	20%	23%	12%	41%	51%	59%	39%
Automotive	1%	2%	2%	1%	13%	18%	22%	9%
Process	6%	5%	6%	2%	12%	11%	11%	10%
Engineering	11%	13%	14%	9%	17%	22%	27%	20%
High technology manufactures	15%	24%	33%	28%	37%	20%	27%	29%
Electronic and electrical	13%	22%	31%	27%	35%	12%	22%	16%
Other	2%	2%	3%	2%	2%	9%	5%	13%

Source: "Improving export structure must be based on upgrading industrial structure", Lu Gang, http://www.drcnet.com.cn/.
Note: For the purpose of calculation, China Customs data have been used for China and UN COMTRADE data used for the developed countries.

Another structural change in Chinese export during the last decade is that

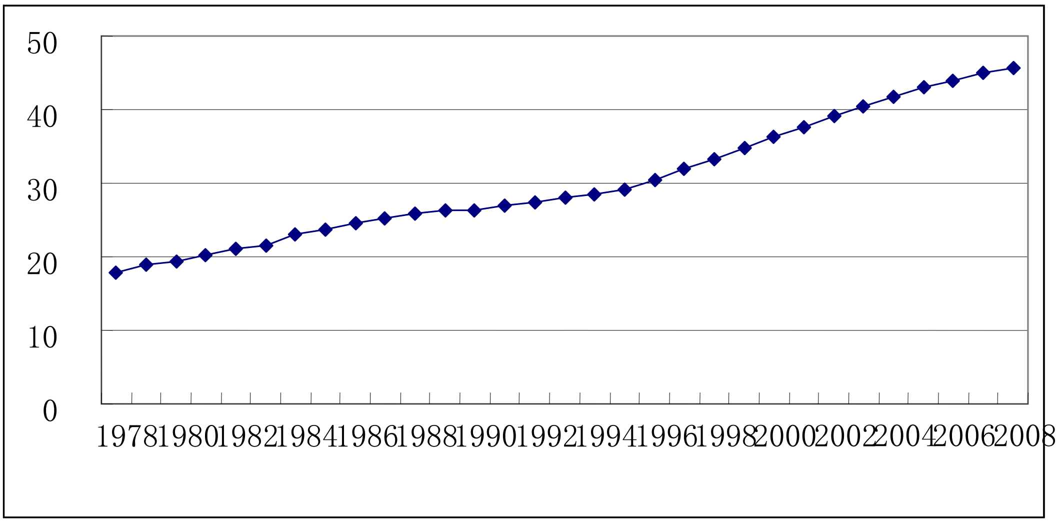
[2]They include Chinese-foreign joint ventures, Chinese-foreign cooperative enterprises and solely foreign-funded enterprises.

the share of medium-tech products, mainly including iron and steel products, chemical products, automobiles and machinery, has risen only slightly from 19% in 1996 to 23% in 2005, while the corresponding figures for Korea, Germany, Japan and the United States in 2004 were 41%, 51%, 59%, 39% respectively. Again, this shows that there still exists a big gap between China and developed countries in terms of industrial technology level. This is why independent innovation has been recently set by China's leadership as a national development focus.

- Due to the fact that China's urbanization process is far from complete, and the reform of China's housing allocation regime, Chinese people will have to save a large portion of their income in order to buy houses. Therefore, the savings rate of the country will remain at a high level in the coming years.

A report by China's Renmin University has found that there exist a positive correlation relationship between urbanization and investment rate and a negative correlation relationship between urbanization and consumption rate. Investment rate tends to rise and consumption rate tends to drop before urbanization rate reaches 60%[3].

Figure 12 Ratio of China's urban population to total population



Source: China Statistical Yearbook 2009.

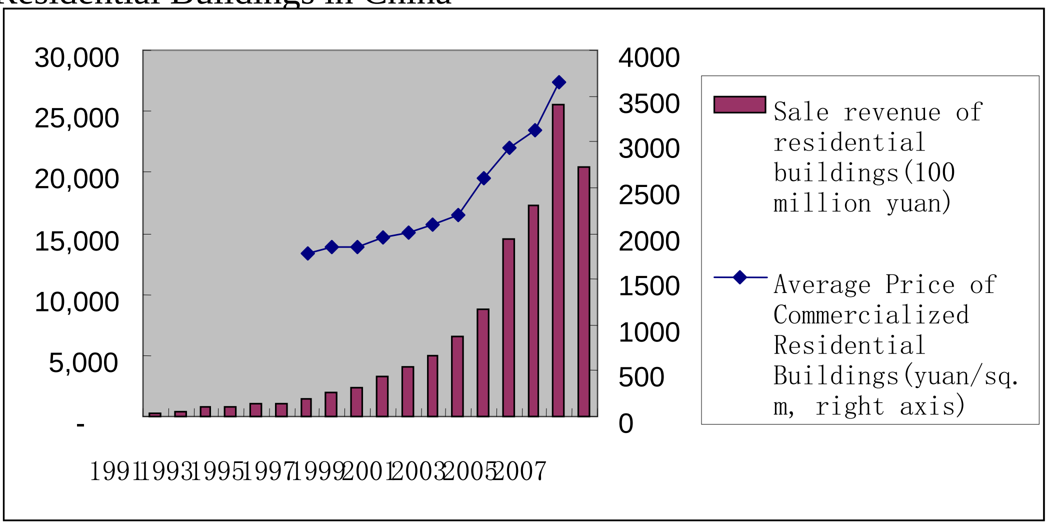
[3] *Report on China's Macroeconomic Situation: Analysis and Forecast 2009Q3*, Macroeconomic forum held by China Renmin University.

It took China 15 years (1981-1996) for its urbanization rate to go up from 20% to 30%, and 7 years (1996-2003) for its urbanization rate to gain another 10 percentage points. In 2008, China's urbanization rate stands at 45.7%, still about 15 percentage points lower than the 60% threshold.

During the process of urbanization, new migrants rushing into cities, including university graduates and migrant workers, would have to save a huge portion of their income in order to have their own house in cities, or at least rent a decent flat. This would considerably restrict their consumption ability on other goods and services.

Aside from the factor of urbanization, the reform of China's housing allocation regime is another important factor which needs to be taken into account if one wants to evaluate the country's consumption potential. For urban residents, they used to receive their houses for free from the government. But after the reform of this allocation reform starting in 1998, they can no longer enjoy this benefit and have to buy their own houses instead. This has created a soaring real estate market ever since. At the same time, urban residents are faced with a heavy economic burden if they want to own a decent house.

Figure 13 Sales revenue and average price of Commercialized Residential Buildings in China



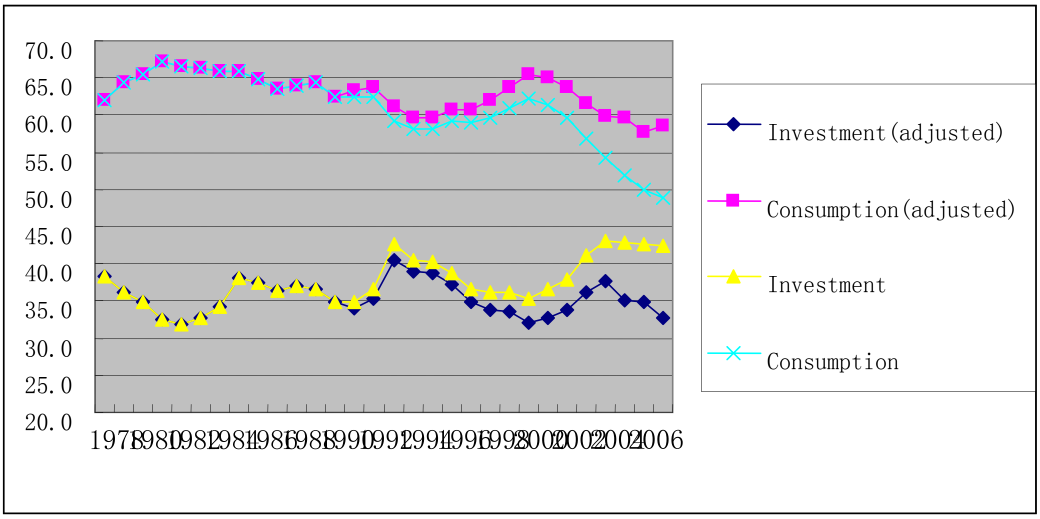
Source: China Statistical Yearbook 2009.

At present, there are still a significant proportion of urban residents in

China who have not bought a commercialized house yet. According to a questionnaire survey conducted by the Anhui branch of China's Statistical bureau in 2006, 92.4% of urban families in Anhui Province have had their own houses, but only 26.3% have purchased commercialized houses, i.e. at market price. 48.4% of urban families live in the flat they bought at a subsidized price from the government during the housing allocation reform and 17.7% of families built their own houses. Since the quality of the latter two types of houses (subsidized flats and own-built houses) is usually inferior to commercialized buildings, there still exists huge potential demand for people to buy new houses at market price. Besides, even for those who have bought a flat at a subsidized price, their offspring can no longer enjoy such treatment and have to buy their houses from the market.

To find out how much impediments the factor of urbanization and housing allocation regime reform have become for China's consumption rate, we can make the following experiment. If we deduct the sales revenue of commercialized residential buildings in China from the countries investment and add it to consumption, the consumption rate of China would be 58.5%, 10 percentage points higher then the actual level.

Figure 14 Experimental Adjustment of consumption and investment rate of China



Source: China Statistical Yearbook 2009 and author's calculation.

■ Besides, China will continue to promote the development of its export sector due to the heavy dependence of its employment on exports. This means net exports will continue to be a major contributor to GDP growth in the coming years, although its relative importance would be decreasing.

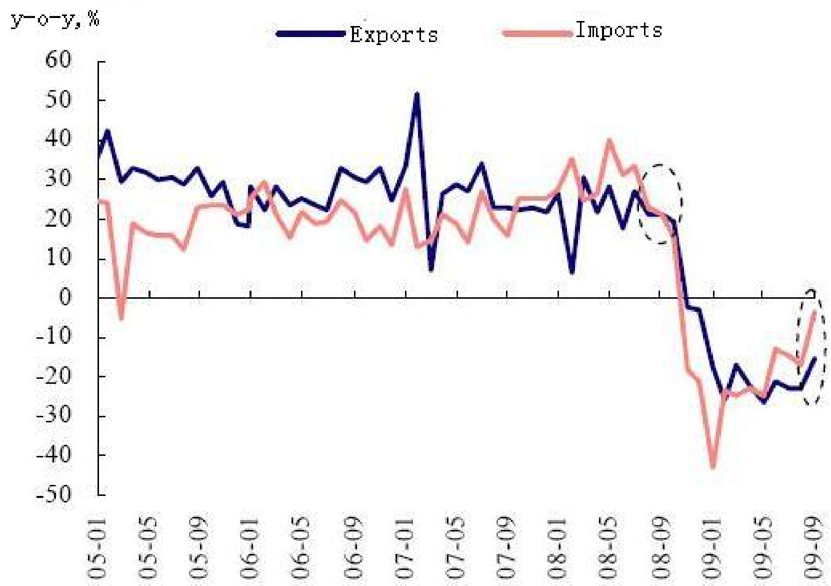
The employment in China is highly dependent on exports and the contribution of exports to employment is irreplaceable in the short term. According to estimates of the Ministry of Commerce of China (MOFCOM), China's foreign trade directly brought job opportunities for about 80 million people, 60% of which are rural migrant workers. Such traditional labor-intensive export industries as agriculture, light industry and textile industry directly employs about 50 million people. There are great difficulties for the huge number of labor force to swiftly change to other industries when the export is shrinking sharply. First of all, the people employed in such traditional labor-intensive export sector as light industry and textile industry are mainly poorly educated migrant workers with low technical skills. It is hard for them to switch to other industries after retraining.

Secondly, China is currently increasing the investments mainly in capital-intensive sectors aiming at domestic market. On the other hand, a large part of the export sectors are labor-intensive. Since the two types of sectors have different employment effect, the internal sales sector is not able to fully absorb the unemployed personnel transferred from the export sector.

Thirdly, the unemployed migrant workers are not willing to go back to rural areas. Their lands in rural areas might have been rented to others and they would have no land to work on even if they go back to their villages. Many young migrant workers come to work in cities when they are still young and have not learned the systematic agricultural production techniques like their parents. Moreover, many of them have already become accustomed to the modern life styles in cities and are not fit for rural life from the psychological perspective.

Under these circumstances, if no actions were taken to alleviate the shock caused by plummeting of exports, many unemployed migrant workers will be stranded in the cities, which may severely undermine the social stability. Undoubtedly, this is politically unacceptable. Therefore, the Chinese government has indeed taken several important measures to protect its exports. For example, China increased the coverage of export credit insurance, decided to arrange short-term export credit insurance of 84 billion USD in 2009. The government has also increased the export rebate rate of a large number of products. With the recovery of US and EU economy, and with the help of the above-mentioned measures, China's exports have showed a clear sign of recovery since May 2009.

Figure 15 Growth rate of China's exports and imports



Source: CEIC, China Customs.

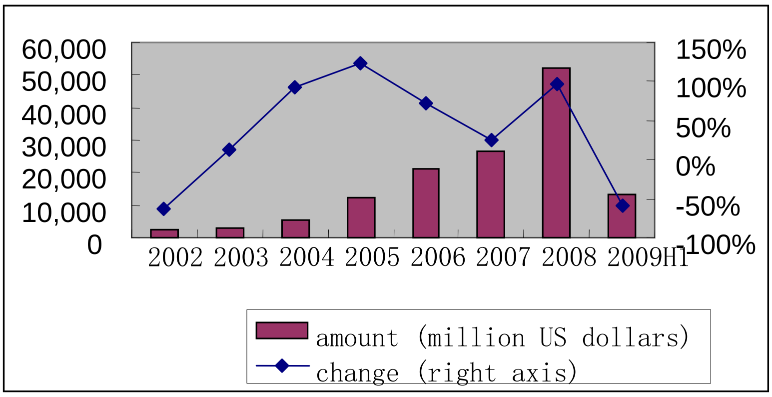
Question 3: Globally, there seems to be an upward trend of investment protectionism against the background of financial crisis. Will China change its policy of promoting outward FDI due to the need to expanding domestic demand?

Answer: The Chinese government will continue to actively promote its "go global" strategy.

- The abrupt drop of China's FDI outflows in the first half year of 2009 was mainly a result of the market factors, i.e. the sluggish global economy leading to enhanced risks of external market, which made the Chinese enterprises more prudent when trying to invest abroad. There is no change in Chinese government's policy to encourage enterprises to invest overseas.

In the first half year of 2009, China's outbound FDI flow recorded 13.3 billion USD, dropping by 60% as compared with the same period of the previous year, which constitutes a strong contrast with the high-speed increase over the last five years. However, this mainly resulted from the market factors, i.e. the sluggish global economy leading to enhanced risks of external market, which made the Chinese enterprises interested in investing overseas more prudent. There is no change in Chinese government's policy to encourage enterprises to invest overseas.

Figure 16 China's FDI outflows



Source: Ministry of Commerce of China, National Bureau of Statistics of China, State Administration of Foreign Exchange of China.

■ It is the objective requirement of economic development rules for Chinese enterprises to increase overseas investment.

As the theory of international investment development path goes, when the per capita GDP of a country reaches 2000～4750 USD, the overseas investment will increase by a large margin. China's per capita GDP exceeded 3300 USD in 2008. As a matter of fact, the development of China's outbound FDI during the first three years of the 11^{th} five-year economic and social development plan period has obviously accelerated. The investment flow for the three years from 2006～2008 totaled nearly 100 billion USD, 1.87 times of the total flow of the fifteen years from

1991～2005. The share of China's outbound FDI flow in the world total hit a record high of 3.6% in 2008, which will probably make China one of the world's top ten investors for the first time.

While the scale of investment is being expanded, the structure, regions and modes of China's overseas investment have also become diversified. The major investment fields have expanded from import/export trade and transportation to finance, mining, manufacturing, telecom and R&D. Since technology, brands, human resources and marketing networks of the enterprises in developed countries have increasingly become the major investment targets of Chinese enterprises, the focus of China's overseas investment is turning from developing countries to both developing counties and developed counties. As a response to this, China's foreign investment has more and more adopted the M&A modes and the proportion of traditional greenfield investment has declined accordingly.

■ Accelerating China's outbound FDI is an important approach for China to switch its economic growth mode and an inevitable choice for China to realize sustainable development.

Firstly, the future 10 years will be the crucial period for China to turn from a large industrialized country to an industrial power. While enhancing independent innovation capacity has been recognized as a national strategy, overseas investment is a shortcut to achieve this goal. Secondly, the huge gap between supply and demand of energy and mineral resources has pressured China to look for resource in overseas regions. Thirdly, the further development of China's manufacturing industry requires the extension of industrial chain and expands to the upstream design and R&D and downstream distribution sections, while directly purchasing overseas brands, patents, marketing network and after-sale service networks is a shot-cut to realize this target. Fourthly, expanding overseas development can open up a path for a part of the foreign exchanges of China to go overseas, which is an important way to help solve the problem of long-term imbalance in China's international payments.

- Supporting the enterprises to invest overseas and thus pulling up exports is also an important part of China’s counter-crisis measures.

In the policy measures to stabilize external demands issued by the Standing Committee Conference of the State Council presided over by Premier Wen Jiabao on May 27, 2009, an important part is to support the enterprises of various ownership to “go global” in order to promote export. The measures specifically include arranging preferential export buyer's credit of 10 billion USD in 2009 and simplifying the examination and approval procedures for preferential purchase and preferential loans projects and funds.

- China’s reform to promote overseas investment management mechanism has not stopped. On the contrary, it has picked up speed. Several key deregulation policies are promulgated in 2009.

The Ministry of Commerce of China (MOFCOM) issued the *Management Measures for Overseas Investment* on March 16, 2009, further reforming the overseas investment management mechanism, promoting the facilitation of overseas investment and greatly supporting Chinese enterprises to “go global”. Compared with the existing regulations, the new *Measures* mainly have the following three characteristics: first, the power of examination and approval is decentralized to provincial departments of commerce. The *Measures* stipulates that MOFCOM only reserves the power of examination and approval on a few major sensitive overseas investment projects, i.e. overseas investment projects of over 100 million USD and outbound investment projects in specific countries. Estimated by the number of applications examined and approved in 2008, about 85% of overseas investment applications will be handled by provincial level authorities. Second, the examination and approval procedures are simplified. The *Measures* stipulates that most enterprises engaged in overseas investment will obtain a Certificate of Outbound Investment by Domestic Institutions within three working days after submitting an application form. Third, the key points of management are stressed. The *Measures* stipulates that the commerce administration authority shall mainly examine the outbound investment on whether it harms the political and economic and trade relations between the PRC and relevant countries (or regions), whether it jeopardizes the national economic security, whether it may contravene the international treaties to which China has acceded and whether it involves vicious competition. The authority no longer examines the economic and technical feasibility of outbound investment projects.

On June 9, 2009, the State Administration of Foreign Exchange (SAFE) of China issued the *Circular on Foreign Exchange Control Issues Relevant to Overseas Loans Extended by Enterprises in China*. The *Notice* mainly includes the following contents: first, the scope of entities that are entitled to provide loans overseas are extended. Compared with the current rules that allow only qualified multinational corporations to provide funds overseas, the new rules extend the scope to include qualified enterprises of all types of ownership. Second, the scope of funds sources is expanded, allowing domestic enterprises to provide loans overseas with their own foreign currencies or by purchasing foreign currencies using RMB within a certain quota. Third, approval procedures for providing loans overseas are also simplified. The opening of the special foreign exchange accounts for providing funds overseas, the transfer of the funds within China and purchasing foreign currencies will also be directly handled by authorized banks.

On July 13, 2009, SAFE also issued the *Provisions on the Foreign Exchange Administration of the Overseas Direct Investment of Domestic Institutions* offering facilitation to outbound FDI by domestic institutions. First, it expands the scope of source of foreign exchange for outbound investment to include self-owned foreign exchange, qualified foreign exchange loans from domestic banks, foreign exchange converted with RMB funds, tangible or intangible assets, and overseas retained profits. Second, it changes the method of reviewing foreign exchange sources for outbound investment from former examination to afterward registration. Third, it changes SAFE’s administration method of the capital outward remittance by domestic institutions for outbound investment from approval to registration. Fourth, upon the approval of local SAFE, the *Provisions* allow domestic institutions to remit in advance the initial expenses according to certain proportion of the total amount of investment for outbound investment before the overseas projects are formally established.

Conclusions

Against the backdrop of global financial crisis, China has actively stimulated investment, but the current rise of investment rate caused by such actions is only temporary. Policy makers have not changed the strategic decision to transform the country's economic development mode from investment and export-led to a more balanced growth path that relies more on domestic consumption. Actually, the Chinese government is exerting as much effort to promote consumption as to boost investment in its anti-crisis policy package. More importantly, the financial crisis has actually promoted reforms in such key fields as medical care system, education system and social security system, which will decrease China's savings rate and promote consumption in the longer term.

At the same time, it is unrealistic to expect China to complete the mission of shifting its economic development mode in the near term. First, its per capita income, which is the crucial factor in deciding consumption rate, is still low. Second, as China's industrialization has not been completed yet, investment will continue to play a key role in the country's economic growth. Third, the unfinished urbanization process of China, together with the factor of housing allocation regime reform, means that a big portion of people's income will have to be saved to buy houses, which is counted as investment rather than consumption in GDP statistics. Fourth, net exports will continue to be a major contributor to China's GDP growth in the coming years, as the country's heavy dependence of employment on exports cannot be changed overnight.

As far as outbound FDI is concerned, the Chinese government will continue to actively promote its "go global" strategy. China will not change its policy of promoting outward FDI due to the need to expanding domestic demand, although there seems to be an upward trend of investment protectionism against the background of financial crisis.

Reference

"China: Looking for new breakthroughs in fighting the crisis", DRC research group, *Management World*, Issue 6, 2009.

"China Economic World Ranking Report", Issue 2, August 2009.

China Statistical Yearbook 2009.

"Improving export structure must be based on upgrading industrial structure", Lu Gang, http://www.drcnet.com.cn/.

Report on the Work of the Government, Chinese Premier Wen Jiabao, March 2009, the Second Session of the 11th National People's Congress (NPC).

"To Deeply Understand the Contribution of Foreign Trade to the Development of National Economy", Zhong Shan, Vice Minister of MOFCOM, June 22, 2009, *Economic Daily*.

"Urban residents' housing quality improving year by year", Anhui branch of China's Statistical bureau, 2006, Issue 82, *Anhui Survey*.

UNCTAD, *Handbook of Statistics online*, http://stats.unctad.org/handbook/.

World Bank, *Key Development Data & Statistics*, http://web.worldbank.org/.