China's Economic Conditions

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Summary

Since the initiation of economic reforms and trade liberalization 30 years ago, China has been one of the world's fastest-growing economies and has emerged as a major economic and trade power. China's rapid economic growth has sharply improved Chinese living standards and helped raise hundreds of millions of people out of extreme poverty. Trade and foreign investment flows have been major factors in China's booming economy. In 2008 China, was the world's second largest merchandise exporter and third largest importer. Over half of China's trade is conducted by foreign-invested firms in China. In 2008, foreign direct investment (FDI) in China totaled $92 billion, making it the destination for FDI among developing economies. The combination of large trade surpluses, FDI flows, and large-scale purchases of foreign currency (especially dollars) has helped make China the world's largest holder of foreign exchange reserves at $2.3 trillion.

The global economic crisis began to impact China's economy in late 2008. After growing by 13% in 2007, China's real GDP slowed to 9.0% in 2008 and to 7.1% in the first half of 2009 (year-on-year basis). China's trade and inflows of FDI diminished sharply, and millions of workers reportedly lost their jobs. The Chinese government has sought to boost the economy by implementing a $586 billion economic stimulus package (largely aimed at infrastructure projects), establishing easy money policies to boost banking lending, and providing assistance to various industries. Such policies have helped stabilize China's economy; real GDP is expected to grow by over 8% in 2009—far higher than the expected growth of any other major economy.

Despite the relatively positive outlook for its economy, China faces a number of difficult challenges that, if not addressed, could undermine its future economic growth and stability. These include pervasive government corruption, an inefficient banking system, over-dependence on exports and fixed investment for growth, the lack of rule of law, severe pollution, and widening income disparities. The Chinese government has indicated that it intends to create a "harmonious society" over the coming years that would promote more balanced economic growth and address a number of economic and social ills.

China's economy and economic policies are of major concern to many U.S. policymakers. On the one hand, U.S. consumers, exporters, and investors have generally benefitted from China's rapid economic and trade growth. China's large holdings of U.S. securities have helped keep U.S. interest rates relatively low. Some contend that China has a large stake in ensuring the continuance of a liberalized global trading system. On the other hand, the surge in U.S. imports of Chinese products has put competitive pressures on various U.S. industries. Many U.S. policymakers have argued that China maintains a number of economic policies that violate its commitments in the World Trade Organization (WTO) and/or are harmful to U.S. economic interests, such as its currency policy. Concerns have also been raised over China's rising demand for energy and raw materials in terms of the impact that demand may have on world prices, Chinese efforts to purchase energy and raw materials assets around the world, and the growing level of pollution and greenhouse gases that has resulted from China's growing energy needs. China has been pursuing free trade agreements around the world, especially in Asia. This has raised concerns that China might try to promote a greater Asian trading area that would exclude the United States, and thus possibly diminish U.S. economic power and influence in the region.

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The rapid rise of China as a major economic power within a time span of about 30 years is often described by analysts as one of the greatest economic success stories in modern times. From 1979 (when economic reforms began) to 2008, China's real gross domestic product (GDP) grew at an average annual rate of nearly 10%. From 1980 to 2008, China's economy grew14-fold in real terms, real per capita GDP (a common measurement of living standards) grew over 11-fold, and hundreds of millions of people were raised out of extreme poverty. By some measurements, China is now the world's second largest economy and some analysts predict it could become the largest within a few decades. Yet, on a per capita basis, China remains a relatively poor country.

China's economic rise has led to a substantial increase in U.S.-China economic ties. Total trade between the two countries surged from $5 billion in 1980 to $409 billion in 2008 (U.S. data). In 2008, China was the United States' second largest trading partner, its third largest export market, and its largest source of imports. Many U.S. companies have extensive operations in China in order to sell their products in the booming Chinese market and to take advantage of low-cost labor for export-oriented manufacturing.[1] These operations have helped some U.S. firms to remain internationally competitive and have supplied U.S. consumers with a variety of low-cost goods. China's large-scale purchases of U.S. Treasury securities have enabled the federal government to fund its budget deficits, which helps to keep U.S. interest rates relatively low.

However, the emergence of China as a major economic superpower has raised concern among many U.S. policymakers. Some express concern over the large and growing U.S. trade deficits with China, which rose from $10 billion in 1990 to $266 billion in 2008, and are viewed by many Members of Congress as an indicator that U.S.-Chinese commercial relations are imbalanced or unfair. Others claim that China uses unfair trade practices (such as an undervalued currency and subsidies to domestic producers) to flood U.S. markets with low-cost goods, and that such practices threaten American jobs, wages, and living standards. Other concerns relating to China's economic growth include its growing demand for energy and raw materials, its status as the world's largest emitter of greenhouse gasses, its large holdings of U.S. securities, and its growing economic ties (and hence influence) with numerous countries around the world, including traditional U.S. allies, as well as countries in which the United States has major foreign policy concerns (such as North Korea, Sudan, and Iran).

China faces a number of major economic challenges, including the fallout from the global financial crisis (which has sharply slowed foreign demand for its exports and diminished FDI flows to China), a weak banking system, widening income gaps, growing pollution, unbalanced economic growth (through over-reliance on exports and fixed investment), widespread economic efficiencies resulting from non-market policies, government corruption, and the lack of the rule of law. The Chinese government views a growing economy as vital to maintaining social stability.

This report provides background on China's economic rise and current economic structure and the challenges China faces to keep its economy growing strong, and describes Chinese economic policies that are of concern to U.S. policymakers.

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[1] Some companies use China as part of their global supply chain for manufactured parts, which are then exported and assembled elsewhere. Other firms have shifted the production of finished products from other countries (mainly in Asia) to China; they import parts and materials into China for final assembly.

Most Recent Developments

- On November 9, 2009, China announced that it would provide $10 billion in concessional loans to African countries, help set up a $1 billion loan program for African small and medium-sized businesses, and forgive certain African debt due in 2009. China also pledged to lower tariffs for African products and to boost cooperation on climate change, science and technology, medical care and health, agriculture, human resources development and education, and cultural exchanges.
- On October 22, 2009, the Chinese government announced that third quarter GDP had risen by 8.9% on a year-on-year basis.
- On October 21, 2009, a Chinese banking official warned that easy money policies could cause property and stock bubbles.
- On October 15, 2009, the Chinese government announced that FDI in China in September had risen by 18.9% year-on-year, the second straight month of FDI growth. The government also reported that foreign exchange reserves had risen to $2.27 trillion as of September 2009, up $358 billion since February 2009.
- On October 15, 2009, the U.S. Treasury Department released its semi-annual report on exchange rates. The report stated that "although China's overall policies played an important role in anchoring the global economy in 2009 and promoting a reduction in its current account surplus, the recent lack of flexibility of the renminbi exchange rate and China's renewed accumulation of foreign exchange reserves risk unwinding some of the progress made in reducing imbalances as stimulus policies are eventually withdrawn and demand by China's trading partners recovers."
- On October 13, 2009, China and Russia reportedly signed 40 trade deals worth an estimated at $3.5 billion. On the same day, the New York Times reported that government officials in Guinea had announced that a Chinese company had agreed to invest up to $7 billion in the country's electricity and aviation infrastructure in return for certain mining and oil rights.
- A report by Hurun Research issued on October 13, 2009, estimated that China had 130 billionaires (U.S. dollars).
- China's Xinhua News Agency report on October 13, 2009, that 968 children living near three smelters in Jiyuan City (in Henan province), were found to have excessive amounts of lead in their blood. China Daily reported on August 25, 2009, that more than 1,350 children in Wenping (Hunan province) and 851 children in Fengxiang (Shaanxi province) had also tested positive for excessive lead. The government stated that it would close down a number of lead plants.
- On August 19, 2009, China reached an agreement with Australia to purchase $41billion worth of Australian natural gas.
- On June 29, 2009, a Chinese government agency estimated that 20% of new bank credit was going into China's stock markets.

- At a press conference during her visit to China on February 21, 2009, Secretary of State Hillary Rodham Clinton stated that she appreciated "greatly the Chinese government's continuing confidence in the United States treasuries."
- On February 1, 2009, the Chinese government announced that 20 million migrant workers (15.4% out of an estimated 130 million migrants) had lost their jobs due to the global financial crisis.
- On November 15, 2008, Chinese President Hu Jintao attended the summit meeting of the Group of 20 (G-20) countries in Washington, D.C. to discuss the current global financial crisis. Hu stated that "steady and relatively fast growth in China is in itself an important contribution to international financial stability and world economic growth."
- On November 9, 2008, the Chinese government announced it would implement a two-year, $586 billion stimulus package, mainly dedicated to infrastructure projects.
- On June 13, 2008, the Netherlands Environmental Assessment Agency announced that, according to its estimates, China in 2007 became the world's largest emitter of CO_2, surpassing the United States by 14%, and accounting for two-thirds of last year's global carbon dioxide increase.

An Overview of China's Economic Development

China's Economy Prior to Reforms

Prior to 1979, China, under the leadership of Chairman Mao Zedong, maintained a centrally planned, or command, economy. A large share of the country's economic output was directed and controlled by the state, which set production goals, controlled prices, and allocated resources throughout most of the economy. During the 1950s, all of China's individual household farms were collectivized into large communes. To support rapid industrialization, the central government undertook large-scale investments in physical and human capital during the 1960s and 1970s. As a result, by 1978 nearly three-fourths of industrial production was produced by centrally controlled state-owned enterprises according to centrally planned output targets. Private enterprises and foreign-invested firms were nearly nonexistent. A central goal of the Chinese government was to make China's economy relatively self-sufficient. Foreign trade was generally limited to obtaining only those goods that could not be made or obtained in China.

Government policies kept the Chinese economy relatively stagnant and inefficient, mainly because most aspects of the economy were managed and run by the central government (and thus there were few profit incentives for firms, workers, and farmers), competition was virtually nonexistent, foreign trade and investment flows were mainly limited to Soviet bloc countries, and price and production controls caused widespread distortions in the economy. Chinese living standards were substantially lower than those of many other developing countries. The Chinese government in 1978 (shortly after the death of Chairman Mao in 1976) decided to break with its Soviet-style economic policies by gradually reforming the economy according to free market principles and opening up trade and investment with the West, in the hope that this would significantly increase economic growth and raise living standards. As Chinese leader Deng

Xioping, the architect of China's economic reforms, put it: "Black cat, white cat, what does it matter what color the cat is as long as it catches mice?"

The Introduction of Economic Reforms

Beginning in 1979, China launched several economic reforms. The central government initiated price and ownership incentives for farmers, which enabled them to sell a portion of their crops on the free market. In addition, the government established four special economic zones along the coast for the purpose of attracting foreign investment, boosting exports, and importing high technology products into China. Additional reforms, which followed in stages, sought to decentralize economic policymaking in several sectors, especially trade. Economic control of various enterprises was given to provincial and local governments, which were generally allowed to operate and compete on free market principles, rather than under the direction and guidance of state planning. In addition, citizens were encouraged to start their own businesses. Additional coastal regions and cities were designated as open cities and development zones, which allowed them to experiment with free market reforms and to offer tax and trade incentives to attract foreign investment. In addition, state price controls on a wide range of products were gradually eliminated. Trade liberalization was also a major key to China's economic success. Removing trade barriers encouraged greater competition and boosted foreign direct investment (FDI) flows.[2]

China's Economic Growth Since Reforms: 1979-2008

Since the introduction of economic reforms, China's economy has grown substantially faster than during the pre-reform period (see **Table 1**). From 1960 to 1978, real annual GDP growth was estimated at 5.3% (a figure many analysts claim is overestimated, based on several economic disasters that befell the country during this time, such as the Great Leap Forward from 1958-1960 and the Cultural Revolution from 1966-1976). During the reform period (1979-present), China's average annual real GDP grew by nearly 9.90%; it grew by 13.0% in 2007, but slowed to 9.0% in 2008. Since 1980, economic reforms helped to produce a 14-fold increase in the size of the economy in real terms and a 11-fold increase in real per capita GDP (a common measurement of living standards). The impact of the current global economic crisis on China's economy is discussed later in this report.

[2] For example, China's accession to the World Trade Organization in December 2001, which required it to reduce a wide range of trade and investment barriers, helped to accelerate GDP growth and led to a sharp increase in FDI flows to China.

Table 1. China's Average Annual Real GDP Growth: 1960-2008

Time Period	Average Annual Growth (%)
1960-1978 (pre-reform)	5.3
1979-2008 (post-reform)	9.9
1990	3.8
1991	9.3
1992	14.2
1993	14.0
1994	13.1
1995	10.9
1996	10.0
1997	9.3
1998	7.8
1999	7.6
2000	8.4
2001	8.3
2002	9.1
2003	10.0
2004	10.1
2005	9.9
2006	11.1
2007	13.0
2008	9.0

Source: Official Chinese government data and the Economist Intelligence Unit.

Causes of China's Economic Growth

Economists generally attribute much of China's rapid economic growth to two main factors: large-scale capital investment (financed by large domestic savings and foreign investment) and rapid productivity growth. These two factors appear to have gone together hand in hand. Economic reforms led to higher efficiency in the economy, which boosted output and increased resources for additional investment in the economy.

China has historically maintained a high rate of savings. When reforms were initiated in 1979, domestic savings as a percentage of GDP stood at 32%. However, most Chinese savings during this period were generated by the profits of state-owned enterprises (SOEs), which were used by the central government for domestic investment. Economic reforms, which included the decentralization of economic production, led to substantial growth in Chinese household savings (these now account for half of Chinese domestic savings). As a result, China's gross savings as a percentage of GDP has steadily risen, reaching 52% in 2008 (compared to a U.S. rate of 8%), among the world's highest savings rates.[3]

Several economists have concluded that productivity gains (i.e., increases in efficiency in which inputs are used) were another major factor in China's rapid economic growth. The improvements to productivity were caused largely by a reallocation of resources to more productive uses, especially in sectors that were formerly heavily controlled by the central government, such as agriculture, trade, and services. For example, agricultural reforms boosted production, freeing workers to pursue employment in the more productive manufacturing sector. China's decentralization of the economy led to the rise of non-state enterprises, which tended to pursue more productive activities than the centrally controlled SOEs. Additionally, a greater share of the economy (mainly the export sector) was exposed to competitive forces. Local and provincial governments were allowed to establish and operate various enterprises on market principles, without interference from the central government. In addition, foreign direct investment (FDI) in China brought with it new technology and processes that boosted efficiency.[4]

Despite these widespread economic reforms, Chinese officials contend that China is a "socialist-market economy," a term that appears to indicate that the government accepts and allows the use of free market forces in a number of areas to help grow the economy, but where the government still plays a major role in the country's economic development. For example, the banking sector in China is largely state-controlled. In addition, although the number of SOEs has declined sharply, they continue to dominate a number of sectors (such as petroleum); are shielded from competition; are generally the only companies that are allowed to invest overseas; and dominate the listings on China's two stock indexes. The government continues to issue five-year and ten-year development plans for the of the economy, and also promotes the development of industries deemed vital for future economic growth. Direct ownership of private property continues to be prohibited by the government (all land is owned by the State), although the government provides rights to individuals and firms to lease and transfer property and offers some legal protection from government seizures.

Measuring the Size of China's Economy

The rapid growth of the Chinese economy has led many analysts to speculate if and when China will overtake the United States as the "world's largest economic power." The "actual" size of China's economy has been a subject of extensive debate among economists. Measured in U.S. dollars using nominal exchange rates, China's GDP in 2008 was $4.2 trillion; its per capita GDP (a commonly used living-standards measurement) was $3,190. Such data would indicate that China's economy and living standards are significantly lower than those of the United States and Japan, respectively considered to be the number-one and number-two largest economies on a nominal dollar basis (see **Table 2**).

[3] Source: EIU Database.

[4] According to the Economist, China's total factor productivity (efficiency gains from such factors as capital and labor) has grown at an average annual rate of about 4% from 1990 to 2008, compared to about 1% growth for the United States. See, the Economist, "Secret sauce: China's rapid growth is due not just to heavy investment, but also to the world's fastest productivity gains." November 12, 2009.

Many economists, however, contend that using nominal exchange rates to convert Chinese data into U.S. dollars substantially underestimates the size of China's economy. This is because prices in China for many goods and services are significantly lower than those in the United States and other developed countries. Economists have attempted to factor in these price differentials by using a purchasing power parity (PPP) measurement, which attempts to convert foreign currencies into U.S. dollars on the basis of the actual purchasing power of such currency (based on surveys of the prices of various goods and services) in each respective country. This PPP exchange rate is then used to convert foreign economic data in national currencies into U.S. dollars.

Because prices for many goods and services are significantly lower in China than in the United States (and other developed countries), the PPP exchange rate nearly doubles the size of the Chinese economy from $4.4 trillion (nominal dollars) to $8.2 trillion (PPP dollars), significantly larger than Japan's GDP in PPPs ($4.3 trillion), and about half the size of the U.S. economy. PPP data also raise China's per capita GDP from $3,325 (nominal) to $6,150.[5] The PPP figures indicate that, while the size of China's economy is substantial, its living standards (though rising) remain far below those of the United States and Japan. China's 2008 per capita GDP on a PPP basis was only 12.9% of U.S. levels.

There are a number of international economic forecasts that project that China's economy on a PPP basis will surpass the U.S. economy (although long-term economic projections should be viewed with caution). The Economist Intelligence Unit projects that China will overtake the U.S. economy in 10 years (2019), and by the year 2030, China's economy will be 18.3% larger than the U.S. economy (see **Figure 1**). However, on a per capita GDP (PPP) basis, China's living standards in 2030 will be less than one-third of U.S. levels (see **Figure 2**).

Table 2. Comparisons of U.S., Japanese, and Chinese GDP and Per Capita GDP in Nominal U.S. Dollars and PPP, 2008

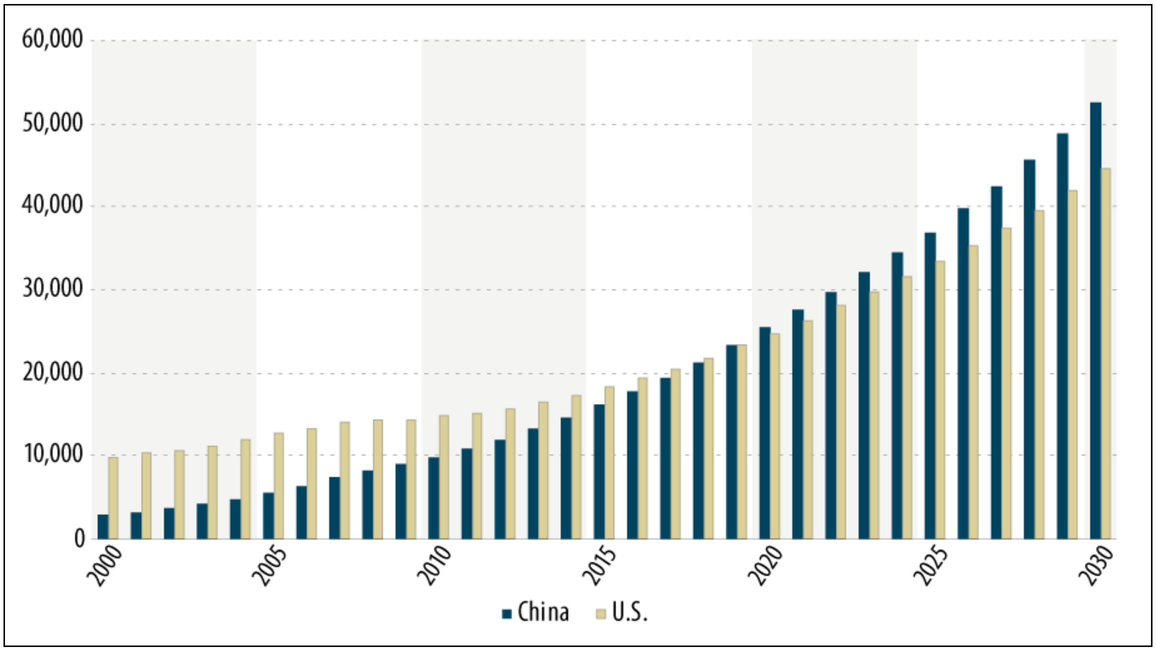
Country	Nominal GDP ($ billions)	GDP in PPP ($ billions)	Nominal Per Capita GDP	Per Capita GDP in PPP
United States	14,441	14,441	47,496	47,496
Japan	4,909	4,333	38,566	34,040
China	4,416	8,161	3,325	6,150

Source: Economist Intelligence Unit.

[5] These figures represent country averages and do not reflect the growing level of income disparity in China, especially between rural areas and cities along the coast.

Figure 1. GDP on a PPP Basis for China and the United States, 2000-2008 and Projections Through 2030

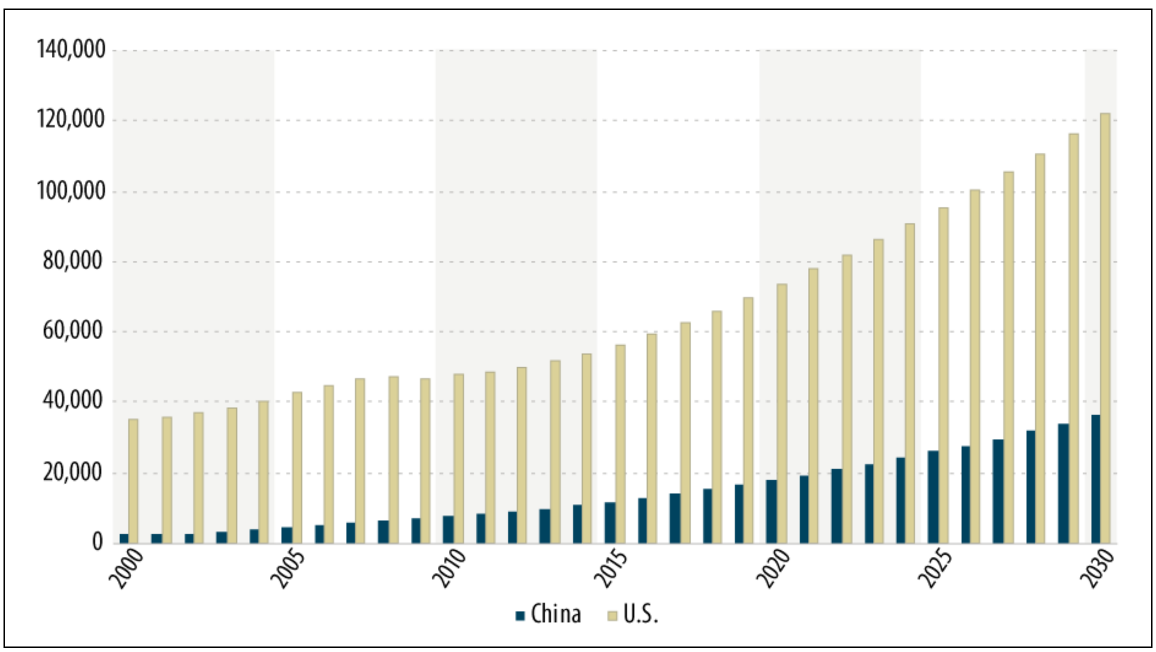
$Billions



Source: Economist Intelligence Unit.

Figure 2. Per Capita GDP on a PPP Basis for China and the United States: 2000-2008 and Projections Through 2030

$Billions



Source: Economist Intelligence Unit.

Foreign Direct Investment in China

China's trade and investment reforms and incentives led to a surge in FDI, which has been a major source of China's productivity and economic growth. The Chinese government estimates that as of 2007 there were 286,200 approved foreign-invested companies in China, and that such firms employed more than 42 million people and accounted for 31.5% of gross industrial output value.[6] Annual utilized FDI in China grew from $2 billion in 1985 to $92 billion in 2008. The cumulative level of FDI in China at the end of 2008 is estimated at $883 billion, making China one of the world's largest destinations of FDI.

In terms of cumulative FDI in China for 1979-2008, the Chinese government reports that 39.6% came from Hong Kong, 10.2% from the British Virgin Islands, 7.4% from Japan, and 6.8% from the United States (see **Table 3**).[7] In terms of annual data, Hong Kong was reported as the largest investor in China in 2008, while the United States ranked 7th. Annual U.S. FDI flows to China peaked at $5.4 billion in 2002, declined annually through 2007, before increasing by 12.5% (to $2.9 billion) in 2008 (see **Figure 3**). The U.S. share of annual FDI flows to China fell from 10.2% in 2002 to 3.2% in 2008.[8]

Table 3. Major Foreign Investors in China: 1979-2008

($ billions and % of total)

Country	Estimated Cumulative Utilized FDI: 1979-2008		Utilized FDI in 2008		
	Amount	% of Total	Amount	% of Total	% Change over 2007
Total	883.1	100.0	92.4	100.0	23.6
Hong Kong	349.6	39.6	41.0	44.4	48.1
British Virgin Islands	90.1	10.2	16.0	17.3	-3.6
Japan	65.4	7.4	3.7	4.0	1.8
United States	59.7	6.8	2.9	3.2	12.5
Taiwan	47.7	5.4	1.9	2.1	–0.3
South Korea	41.9	4.7	3.1	3.4	–14.8
Singapore	37.8	4.3	4.4	4.8	39.3

Source: Chinese Ministry of Commerce.

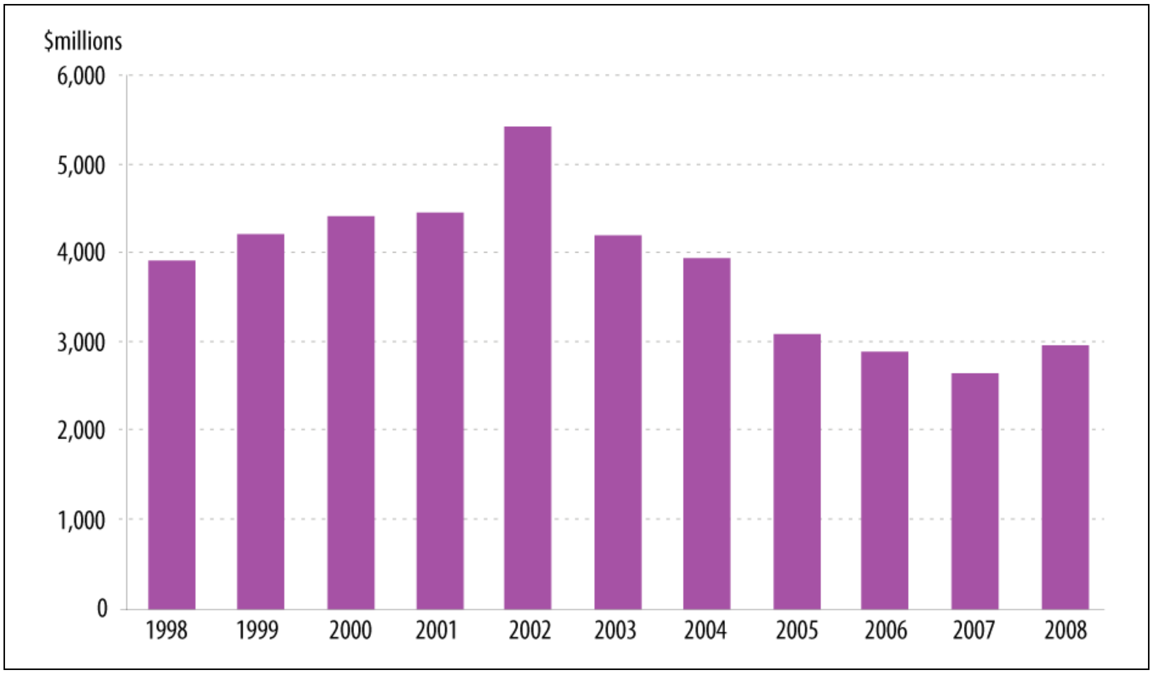
Note: Ranked by cumulative top seven investors through 2008. Excludes FDI in the financial sector

[6] Gross industrial output value is the total volume of final industrial products produced and industrial services provided during a given period. Source: China 2008 Statistical Yearbook.

[7] Much of the FDI originating from the British Virgin Islands and Hong Kong may originate from other foreign investors. For example, Taiwanese businesses are believed to invest in China through other countries or territories (such as Hong Kong) in order to circumvent government restrictions. In addition, some Chinese investors might be using these locations to shift funds overseas in order to re-invest in China to take advantage of preferential investment policies (this practice is often referred to as "round-tipping"). Thus, the actual level of FDI in China may be overstated.

[8] Note, U.S. data on bilateral FDI flows with China differ significantly with Chinese data.

Figure 3. Annual U.S. FDI Flows to China: 1998-2008



Source: Chinese Ministry of Commerce and Chinese Yearbook, various years.

Note: Chinese and U.S. data on bilateral FDI flows differ sharply.

China's Trade Patterns

Economic reforms and trade and investment liberalization have helped transform China into a major trading power. Chinese exports rose from $14 billion in 1979 to $1,429 billion in 2008, while imports over this period grew from $16 billion to $1,132 billion (see **Table 4** and **Figure 4**). China's trade growth has been particularly rapid over the past six or so years. From 2002 to 2008, China's exports grew by 339%, a compound annual growth rate of 23.5%; while imports increased by 283%, a compound annual growth rate of 21.2%.

In 2007, China surpassed the United States as the world's second largest merchandise exporter, after Germany. China was the world's second largest exporter in 2008 (and was close to overtaking Germany), and was the third largest importer, after the United States and Germany (see **Figure 5** and **Figure 6).** China's trade surplus, which totaled $32 billion in 2004, surged to $297 billion in 2008.

Merchandise trade surpluses, large-scale foreign investment, and large purchases of foreign currencies to maintain its exchange rate with the dollar and other currencies have enabled China to accumulate the world's largest foreign exchange reserves at $2.3 trillion at the end of September 2009, making it the world's largest holder of such reserves.

Table 4. China's Merchandise World Trade: 1979-2008

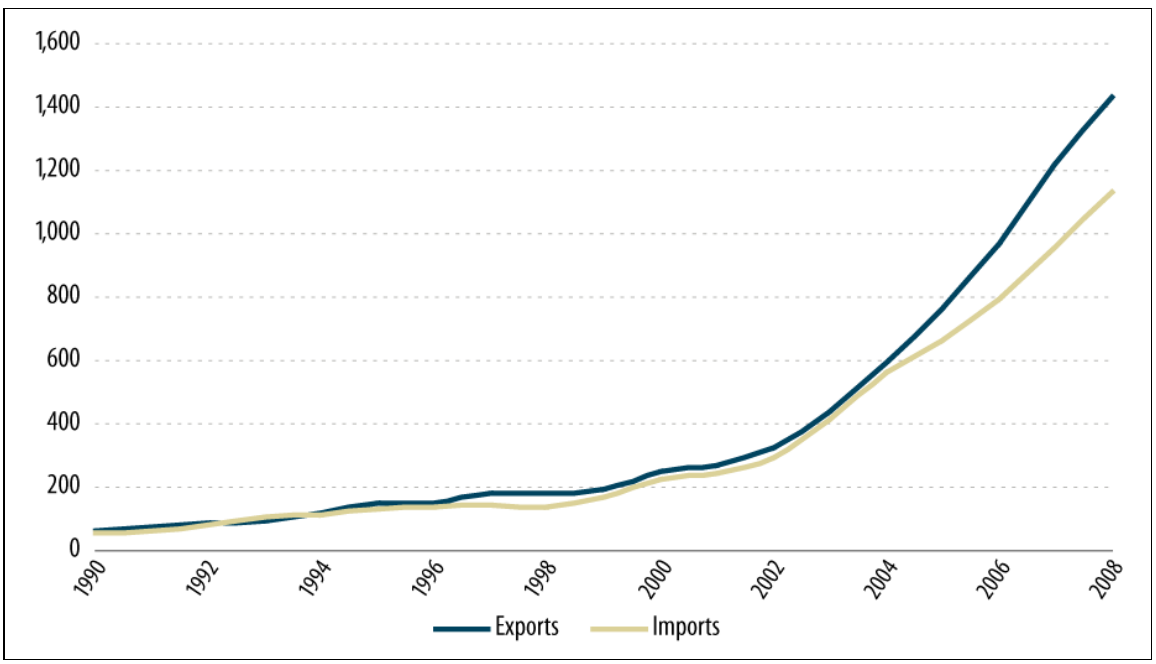
($ billions)

Year	Exports	Imports	Trade Balance
1979	13.7	15.7	–2.0
1980	18.1	19.5	–1.4
1985	27.3	42.5	–15.3
1990	62.9	53.9	9.0
1995	148.8	132.1	16.7
2000	249.2	225.1	24.1
2001	266.2	243.6	22.6
2002	325.6	295.2	30.4
2003	438.4	412.8	25.6
2004	593.4	561.4	32.0
2005	762.0	660.1	101.9
2006	969.1	791.5	177.6
2007	1,218.0	955.8	262.2
2008	1,428.9	1,131.5	297.4

Source: *Global Trade Atlas*.

Figure 4. China's Merchandise Trade: 1990-2008

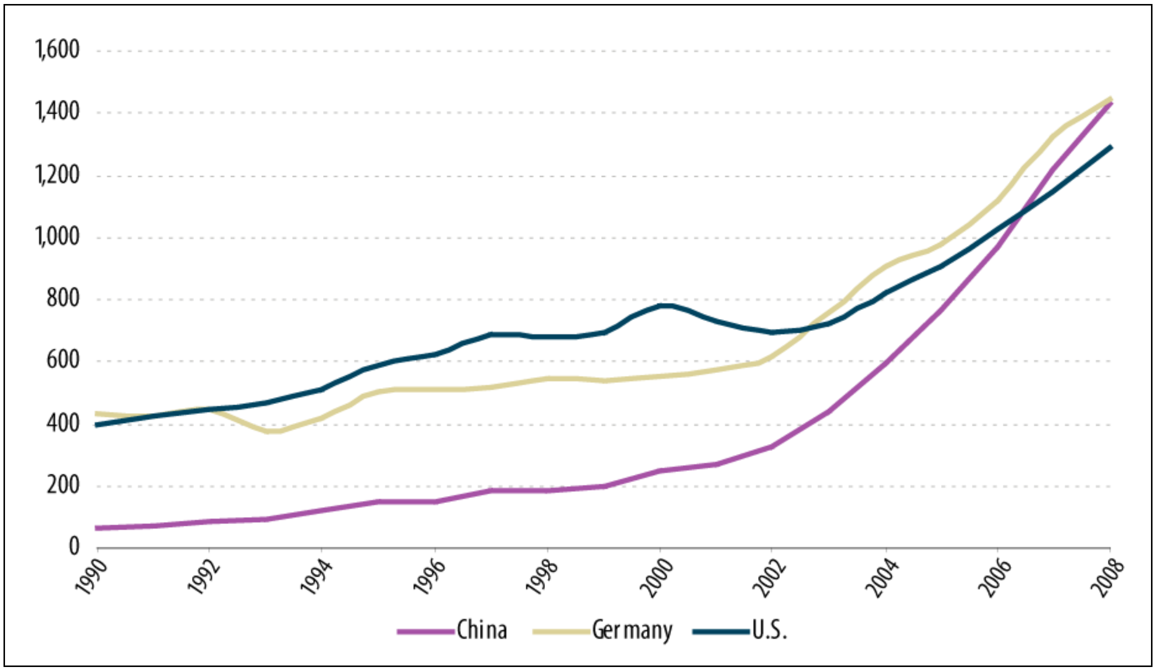
$Billions



Source: Economist Intelligence Unit.

Figure 5. Merchandise Exports by China, Germany and the United States: 1990-2008

$Billions

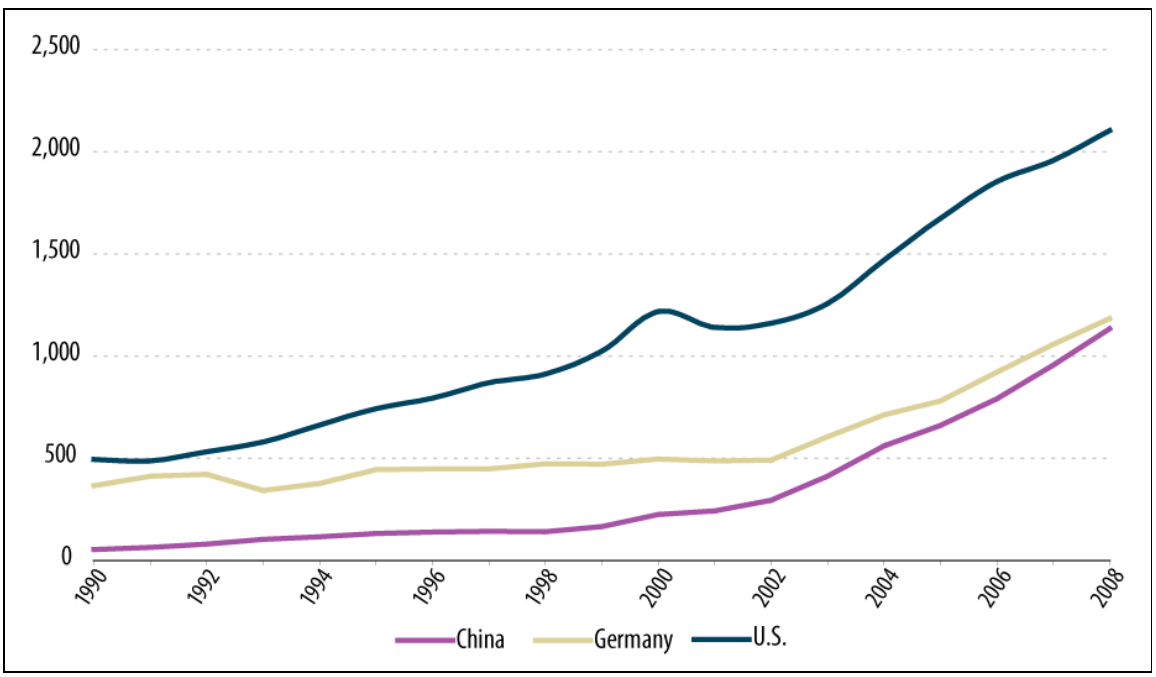


Source: Economist Intelligence Unit

Notes: These countries represented the top three global exporters in 2008.

Figure 6. Merchandise Imports by China, Germany, and the United States: 1990-2008

$Billions



Source: Economist Intelligence Unit

Notes: These represent the top three global importers in 2008. Import data are listed on a cost, insurance, and freight (c.i.f.) basis.

China's Major Trading Partners

China's trade data often differ significantly from those of its major trading partners, including the United States. This is largely due to the large share of China's trade (both exports and imports) that pass through Hong Kong (which reverted back to Chinese rule in July 1997 but is treated as a separate customs area by most countries, including China and the United States). China treats a large share of its exports through Hong Kong as Chinese exports to Hong Kong for statistical purposes, while many countries that import Chinese products through Hong Kong generally attribute their origin to China for statistical purposes.

According to Chinese trade data, its top five trading partners in 2008 were the 27 countries that make up the European Union (EU), the United States, Japan, the 10 nations that constitute the Association of Southeast Asian Nations (ASEAN), and Hong Kong. China's largest export markets in 2008 were the EU, the United States, and Japan, while its top sources for imports were Japan, the EU, and ASEAN (the United States ranked sixth). China maintained substantial trade surpluses with the United States, the EU, and Hong Kong, but reported deficits with Japan and ASEAN. China reported that it had a $171 billion trade surplus with the United States, but U.S. data show that it had a $266 billion deficit with China. These trade imbalance data disparities occur with many of China's other major trading partners as well (see **Table 5**).

Chinese data indicated that 18% of its exports went to the United States in 2008. However, many analysts contend that the United States is a much more significant market for China than its trade data indicate, and they attempt to show this by taking U.S. data on its imports from China ($338 billion in 2008) and dividing it by China's official data on its total exports ($1,429 billion), which yields about 24% (i.e., the percent of Chinese exports that go to the United States).[9]

A growing level of Chinese exports is from foreign-funded enterprises (FFEs) in China. According to Chinese data, FFEs were responsible for 55% of Chinese exports in 2008 compared with 41% in 1996. A large share of these FFEs are owned by Hong Kong and Taiwan investors, many of whom have shifted their labor-intensive, export-oriented, firms to China to take advantage of low-cost labor. Many of the products made by such firms are likely exported to the United States. Additional information on China's trade with other countries and regions, including Africa, Iran, and North Korea, can be found in the **Appendix**.

[9] Such calculations represent a very rough estimate and should be interpreted with caution.

Table 5. China's Major Trading Partners: 2008
($ billions)

Country	Total Trade	Chinese Exports	Chinese Imports	China's Trade Balance	Trading Partner's Reported Trade Balance With China
European Union	425.9	293.0	132.9	160.1	-247.6
United States	333.8	252.3	81.5	170.8	-266.2
Japan	266.8	116.2	150.6	–34.5	-18.6
ASEAN	231.0	114.1	116.9	–2.8	-21.6
Hong Kong	203.7	190.8	12.9	177.8	-3.1
Total Chinese Trade	2,560.4	1,428.9	1,131.5	297.4	—

Source: *Global Trade Atlas* and *World Trade Atlas* using official Chinese data.

Major Chinese Trade Commodities

China's abundance of cheap labor (the average hourly labor wage in China's manufacturing sector in 2008 was $1.64, compared to about $18 in the United States) has made it internationally competitive in many low-cost, labor-intensive manufactures.[10] As a result, manufactured products constitute a significant share of China's trade. A substantial amount of China's imports is comprised of parts and components that are assembled in Chinese factories (such as consumer electronic products and computers), then exported. China's top 10 exports and imports in 2008 are listed in **Table 6** and **Table 7**, respectively, using the harmonized tariff system (HTS) on a two-digit level.

[10] China's hourly average wage in 2008 was equal (in dollar terms) to about 26% of the U.S. minimum wage. Source: Global Insight. Note, that China's hourly wage would rise to $3.19 if measured on a purchasing power parity level.

Table 6. Major Chinese Exports: 2008

HS	Description	$millions	Percent of Total	2008/2007 % Change
	—World—	1,428,869	100.0	17.3
85	Electrical machinery (such as computers and parts)	342,082	23.9	13.9
84	Machinery	268,740	18.8	17.5
61	Knit apparel	60,590	4.2	-1.2
72	Iron and steel	53,494	3.7	33.9
62	Woven apparel	52,430	3.7	10.8
73	Iron and steel products	48,344	3.4	31.7
90	Optical, photographic, cinematographic, measuring checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof	43,385	3.0	17.2
94	Furniture and bedding	42,786	3.0	19.0
87	Vehicles, except railway (mainly auto parts, motorcycles, trucks, and bicycles)	39,316	2.8	23.4
95	Toys and sports equipment	32,695	2.3	20.8

Source: *World Trade Atlas*, using official Chinese statistics.

Notes: Top 10 exports, 2-digit level, harmonized tariff system.

Table 7. Major Chinese Imports: 2008

HS	Description	$millions	Percent of Total	2008/2007 % change
	World	1,131,469	100	18.3
85	Electrical machinery	266,639	23.6	3.5
27	Mineral fuel, oil etc	168,643	14.9	61.1
84	Machinery	138,707	12.3	11.5
26	Ores, slag, and ash	85,236	7.5	58.1
90	Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof	77,696	6.9	12.0
39	Plastic	48,841	4.3	7.8
29	Organic chemicals	39,301	3.5	2.4
87	Vehicles, not railway (mainly autos and parts)	26,941	2.4	21.8
74	Copper and articles thereof	26,085	2.3	-4.0
72	Iron And Steel	24,520	2.2	6.6

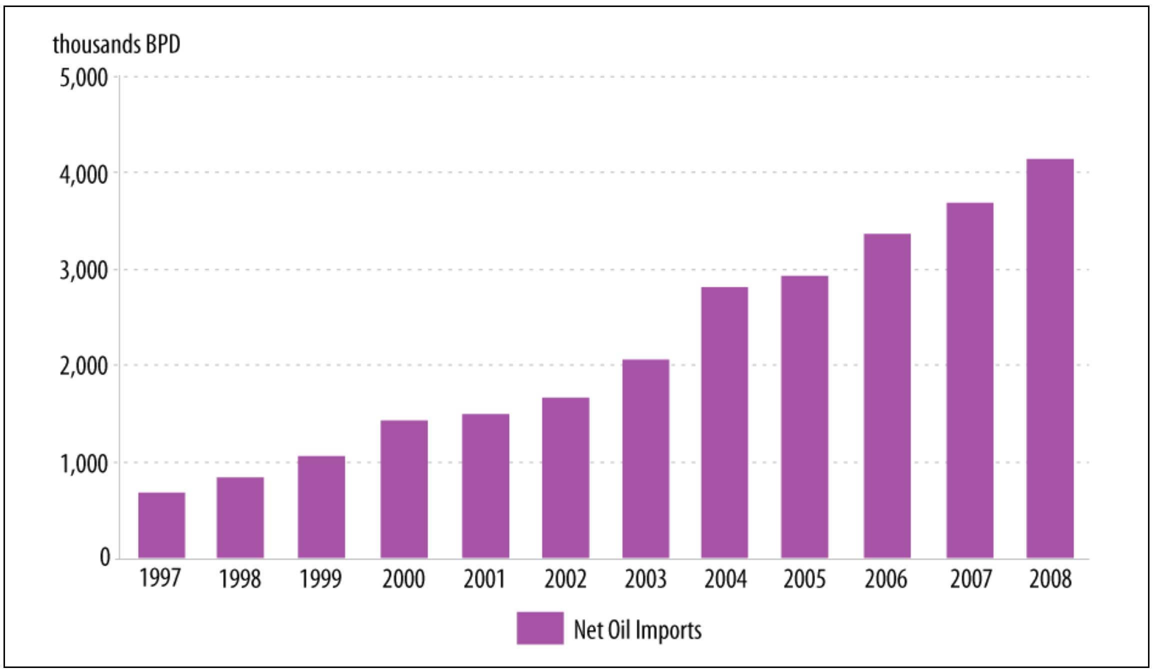
Source: *World Trade Atlas*, using official Chinese statistics.

Notes: Top 10 imports in 2008, two-digit level, harmonized tariff schedule.

China's Growing Appetite for Imported Oil

China's rapid economic growth has fueled a growing demand for energy, such as petroleum, and that demand is becoming an increasingly important factor in determining world oil prices. China is the world's second largest consumer of oil products (after the United States) at 7.6 million barrels per day (bpd) in 2007 (compared to 3.9 million in 1997), and that level is projected to increase to13.6 million bpd by 2030 (depending on China's future growth and energy policies).[11] China became a net oil importer (i.e., imports minus exports) in 1993. Net oil imports grew from 632 thousand bpd in 1997 to about 4.1 million bpd in 2008. China's net oil imports doubled from 2003 to 2008 (see **Figure 7**), and making it the world's third largest net oil importer (after the United States and Japan). China's net oil imports are projected to rise to 13.1 million bpd by 2030, a level that would be comparable to the EU in that year. China's dependence on imported oil could rise from about the current level of about 50% to 80% by 2030.[12]

Figure 7. China's Net Oil Imports: 1997-2008



Source: U.S. Energy Administration and China Energy Newswire.

China's Regional and Bilateral Free Trade Agreements

The Chinese government has maintained an active policy of boosting trade and investment ties around the world, especially countries in Asia. To that end, China has entered into a number of regional and bilateral trade agreements, or is in the process of doing so. China currently has FTAs that include the following trading partners: the 10 nations that make up ASEAN, Bangladesh,

[11] Global Insight, *Global Petroleum Outlook Forecast Tables (Long-Term)*, August 2008.

[12] International Energy Agency, *2007 World Energy Outlook*, p. 168. Estimates are based on Reference Scenario projections, which assume no new government policies and measures or technological breakthroughs.

India, South Korea, Sri Lanka, Chile, Hong Kong, Macau, New Zealand, Singapore, Pakistan, and Peru. These activities are summarized in **Table 8.**

Table 8. China's Free Trade Agreements

Agreement	Implementing Year	Brief Description of the Agreement
Asia Pacific Trade Agreement (originally founded in 1976). Current members are China, Bangladesh, India, S. Korea, Laos, and Sri Lanka	China joined the agreement in 2002.	Preferential tariff arrangement that aims at promoting intra-regional trade through exchange of mutually agreed concessions by member countries.
Mainland and Hong Kong Closer Economic Partnership Arrangement	2004	Free trade and economic integration agreement covering goods & services.
Mainland and Macao Closer Economic Partnership Arrangement	2004	Free trade and economic integration agreement covering goods & services
Framework Agreement on Comprehensive Economic Co-Operation Between ASEAN and the People's Republic of China. Three separate agreements covering goods, services, and investment	Goods agreement entered into force in 2005. ASEAN 6 countries (Brunei Darussalam, Indonesia, Malaysia, Philippines, Singapore and Thailand) to implement most tariff cuts by 2010, and the remaining countries to implement most cuts by 2015 (longer phase-ins and/ remaining tariffs for certain "sensitive" and "highly sensitive" products.. Services agreement effective 2007. Investment agreement effective 2009	Establishes the ASEAN-China Free Trade Area (ACFTA), which would constitute the world's largest free trade area in terms of population (1.9 billion people).
China-Chile FTA	2006	China agreed to immediately reduce tariffs on 92% of Chilean exports to China.
China-Pakistan FTA (separate agreements on goods and services	2007 for goods and 2009 for services	China agreed to eliminate tariffs on 35.5% of tariff lines within three years and reduce tariffs on another 48.5% within five years.
China-New Zealand FTA	2008	China agreed to remove tariffs on 96% of New Zealand exports by 2019.
China-Singapore FTA	2009	China agreed to remove tariffs on 85% of Singapore's exports to China by 2010.
China-Peru FTA	2009	Will eliminate tariffs on 90% of all trade items within 16 years.

Source: WTO Regional Trade Agreements Information System and Chinese Ministry of Commerce.

China is also in the process of negotiating FTAs with the following countries and entities: Australia, Norway, South Africa, Iceland, Costa Rica, the Cooperation Council for the Arab States of the Gulf (which includes Saudi Arabia, Kuwait, the United Arab Emirates, Qatar, and Bahrain), and the Southern African Customs Union (which includes Botswana, Lesotho, Namibia, and Swaziland). China also claims that it currently is negotiating with a number of trading partners to begin individual FTA negotiations with India, South Korea, and Taiwan. China has been active in a number of regional dialogue forums that could eventually lead to regional FTAs or free trade areas. These include the *Japan-China-Republic of Korea trilateral Summit*, the *ASEAN Plus Three Summit* (which includes ASEAN, China, South Korea, and Japan), and *the East Asian Summit,* which includes the ASEAN plus three countries, as well as India, Australia, and New Zealand (together referred to as ASEAN Plus Six).

China's Growing Overseas Direct Investment

A key aspect of China's economic growth strategy has been to attract foreign investment into China. However, in 2000, China's leaders initiated a new "go global" strategy, which sought to encourage firms (especially state-owned enterprises) to invest overseas. The Chinese government generally refers to these activities as overseas direct investment (ODI). There appear to be several factors driving this investment.

- China's massive accumulation of foreign exchange reserves has led government officials to seek more profitable ways of investing these holdings (which traditionally have mainly been put into relatively safe, low yield assets, such as U.S. Treasury securities). On September 29, 2007, the Chinese government officially launched the China Investment Corporation (under the direction of the State Council) in an effort to better manage its foreign exchange reserves. It was originally funded at $200 billion, making it one of the world's largest sovereign wealth funds.[13] Some analysts believe that China will increasingly use its reserves to purchase foreign firms, or shares of foreign firms, that are perceived to be profitable in order to diversify its use of foreign exchange holdings.
- As a developing country, China has traditionally sought to attract FDI into the country in order to, through joint ventures, gain access to foreign technology and management skills to help domestic firms become more efficient and internationally competitive. Now the Chinese government is attempting to promote the development of internationally recognized Chinese brands. One strategy has been to purchase (or attempt to purchase) existing companies and their internationally-recognized brand names (as well as to obtain technology and management skills). For example, in April 2005 Lenovo Group Limited, a Chinese computer company, purchased IBM Corporation's personal computer division for $1.75 billion.[14] On June 20, 2005, Haier Group, a major Chinese home appliances manufacturer, made a $1.28 billion bid to take over Maytag Corporation, although the bid was later withdrawn.
- Acquisition of energy and raw materials has been a major priority of China's overseas investment strategy. As such, China has sought to either purchase or invest in foreign energy and raw material companies, infrastructure projects (such as oil and gas pipelines, oil refineries, and mines), and joint ventures. For example, in June 2005, the China National Offshore Oil Corporation (CNOOC), through its Hong Kong subsidiary (CNOOC Ltd.), made a bid to buy a U.S. energy company, UNOCAL, for $18.5 billion, although CNOOC later withdrew its bid due to opposition by several congressional Members. In August 2005, the

[13] See, CRS Report RL34337, *China's Sovereign Wealth Fund*, by Michael F. Martin.

[14] The Chinese government is believed to be the largest shareholder in the company.

> China National Petroleum Corporation (CNPC), China's largest oil company, purchased PetroKazakhstan Inc., a Canadian-registered company, for $4.2 billion.[15] According to the Eurasia Group, since the 1990s CNPC has signed energy deals with Sudan worth $10 billion, with $4 billion in actual investment.[16] In June 2009, China's Sinopec Group acquired Addax Petroleum Corporation (a Swiss company) for $7.2 billion.

China appears to be a relatively small, but growing, global investor. According to Chinese data, its annual ODI increased from $2.9 billion in 2003 to $55.9 billion in 2008; its ODI in 2008 was more than double 2007 levels ($26.5 billion).[17] China's cumulative ODI through 2008 was reported at $184.0 billion.[18] China's state-owned enterprises accounted for 64% of ODI in 2008.[19]

Broken down by country, China's ODI data are somewhat misleading because the three top ODI destinations on a cumulative basis (as of 2008) were Hong Kong, the Cayman Islands, and the British Virgin Islands. It is likely that these were not the final destination for most of these investment funds. Some analysts contend that a large share of ODI going to Hong Kong and Caribbean islands represents "round-tipping," that is, Chinese capital that is sent overseas but then re-invested elsewhere (some of which may come back to China in the form of "foreign investment") to take advantage of favorable treatment afforded to foreign investment. Some of that capital could be also going into tax havens.

Table 9 lists the top 10 destinations for China's cumulative ODI through 2008. Hong Kong was by far the major destination (accounting for 63% of total), followed by the Cayman Island (14%), the British Virgin Islands (6%), and the United States (2%).[20] China has sharply increased its investment in Africa over the past few years; annual ODI there rose from $75 million in 2003 to $5.5 billion in 2008 (cumulative ODI through 2008 was $7.8 billion). China's increased level of overseas investment has raised some concerns among U.S. policymakers, in large part because it is often unclear to what extent such investments are being made for economic reasons and to what extent the central government is attempting to guide such investments.

[15] *Asia Times*, August 24, 2005.

[16] Eurasia Group, *China's Overseas Investments in Oil and Gas Production*, October 16, 2006, p. 20.

[17] However, the Chinese government reported that ODI during the first quarter of 2009 was down 60% over the same period in 2008, due largely to the effects of the global economic slowdown.

[18] In comparison, U.S. FDI (as reported by the U.S. Bureau of Economic Analysis) was $311.8 billion and cumulative FDI through 2008 was $3,162.0 billion (on a historical cost basis).

[19] *China Daily*, September 19, 2009.

[20] In terms of regions, Asia accounted for 77.9% of China's cumulative ODI, followed by Africa (9.8%) Latin America (6.6%), Oceania (3.5%).Europe (1.6%), and North America (0.7%).

Table 9. Top 10 Destinations for China's Overseas Direct Investment: 2008

($ millions)

Country	ODI in 2008	Cumulative ODI Through 2008
Hong Kong	38,640	115,845
Cayman Islands	1,524	20,327
British Virgin Islands	2,104	10,477
Singapore	1,551	3,335
Australia	1,952	3,255
South Africa	4,808	3,049
United States	462	2,390
Russian Federation	395	1,838
Macau	643	1,561
Pakistan	265	1,328
Total Chinese ODI	**55,907**	**183,970**

Source: China Ministry of Commerce, 2008 Statistical Bulletin of China's Outward Foreign Investment, 2009.

Major Long-Term Challenges Facing the Chinese Economy

China's economy has shown remarkable growth over the past several years, and many economists project that it will enjoy fairly healthy growth in the near future. However, economists caution that these projections are likely to occur only if China continues to make major reforms to its economy. Failure to implement such reforms could endanger future growth.

- **Uneven economic growth**. The global economic crisis has demonstrated to the Chinese government the dangers of relying too heavily on foreign trade and investment for economic growth. That dependency made China's economy particularly vulnerable to the effects of the global economic downturn (discussed in more detail below).
- **An inflexible currency policy**. China does not allow its currency to float and therefore must make large-scale purchases of dollars to keep the exchange rate within certain target levels. Although the renminbi (or yuan) has appreciated somewhat since reforms were introduced in July 2005, analysts contend that it remains highly undervalued against the dollar.[21] Economists warn that China's currency policy has made the economy overly dependent on exports and fixed investment for growth and has promoted easy credit policies by the banks. These policies may undermine long-term economic stability by causing overproduction

[21] The renminbi appreciated by about 18% against the dollar from July 2005 to July 2008, but since then the Chinese government has halted any further appreciation.

in various sectors, increasing the level of non-performing loans held by the banks and boosting inflationary pressures.[22]

- **State-owned enterprises (SOEs)**, which account for a significant amount of Chinese industrial production, put a heavy strain on China's economy. By some estimates, over half lose money and must be supported by subsidies, mainly through state banks. Government support of unprofitable SOEs diverts resources away from potentially more efficient and profitable enterprises. In addition, the poor financial condition of many SOEs makes it difficult for the government to reduce trade barriers out of fear that doing so would lead to widespread bankruptcies among many SOEs and unemployment.

- **The banking system** faces several major difficulties due to its financial support of SOEs and its failure to operate solely on market-based principles. China's banking system is regulated and controlled by the central government, which sets interest rates and attempts to allocate credit to certain Chinese firms. The central government has used the banking system to keep afloat money-losing SOEs by pressuring state banks to provide low-interest loans, without which a large number of the SOEs would likely go bankrupt. According to some estimates, over 50% of state-owned bank loans go to the SOEs, even though a large share of loans are not likely to be repaid. The precarious financial state of the Chinese banking system has made Chinese reformers reluctant to open the banking sector to foreign competition. Corruption poses another problem for China's banking system because loans are often made on the basis of political connections. This system promotes widespread inefficiency in the economy because savings are generally not allocated on the basis of obtaining the highest possible returns. Many private companies in China find it difficult to borrow from state banks.

- **Public unrest.** The Chinese government acknowledged that there were over 87,000 protests (many of which were violent) in 2005 (compared with 53,000 protests in 2003) over such issues as pollution, government corruption, and land seizures.[23] A number of protests in China have stemmed in part from frustrations among many Chinese (especially peasants) that they are not benefitting from China's economic reforms and rapid growth, and perceptions that those who are getting rich are doing so because they have connections with government officials. Protests have broken out over government land seizures and plant shutdowns in large part due to perceptions that these actions benefitted a select group with connections. A 2005 United Nations report stated that the income gap between the urban and rural areas was among the highest in the world and warned that this gap threatens social stability. The report urged China to take greater steps to improve conditions for the rural poor, and bolster education, health care, and the social safety net.[24] It is estimated that 300 million people in China (mainly in rural areas) lack health insurance, and many that do have basic

[22] For further information on the economic consequences of China's currency policy, see CRS Report RL32165, *China's Currency: Economic Issues and Options for U.S. Trade Policy*, by Wayne M. Morrison and Marc Labonte.

[23] See CRS Report RL33416, *Social Unrest in China*, by Thomas Lum.

[24] *China's Human Development Report 2005.*

insurance must pay a significant amount of medical expenses out of their own pocket.[25]

- **The lack of the rule of law** in China has led to widespread government corruption, financial speculation, and misallocation of investment funds. In many cases, government "connections," not market forces, are the main determinant of successful firms in China. Many U.S. firms find it difficult to do business in China because rules and regulations are generally not consistent or transparent, contracts are not easily enforced, and intellectual property rights are not protected (due to the lack of an independent judicial system). The lack of the rule of law in China limits competition and undermines the efficient allocation of goods and services in the economy.
- **Poor government regulatory environment**. China maintains a weak and relatively decentralized government structure to regulate economic activity in China. Laws and regulations often go unenforced or are ignored by local government officials. As a result, many firms cut corners in order to maximize profits. This has lead to a proliferation of unsafe food and consumer products being sold in China or exported abroad.[26] Lack of government enforcement of food safety laws led to a massive recall of melamine-tainted infant milk formula that reportedly killed at least four children and sickened 53,000 others in 2008. Growing concerns over the health and safety of Chinese products (such as fish, pet food, tires, and toys) in the United States and other countries could lead consumers to reduce their purchases of Chinese products and could undermine China's efforts to develop and promote internationally recognized Chinese brands.
- **Growing pollution.** The level of pollution in China continues to worsen, posing series health risks to the population. The Chinese government often disregards its own environmental laws in order to promote rapid economic growth. According to the World Bank, 20 out of 30 of the world's most polluted cities are in China, with significant costs to the economy (such as health problems, crop failures and water shortages). According to one government estimate, environmental damage costs the country $226 billion, or 10% of the country's GDP, each year. The Chinese government estimates that there are over 300 million people living in rural areas that drink unsafe water (caused by chemicals and other contaminants). Toxic spills in 2005 and 2006 threatened the water supply of millions of people. China is the largest producer and consumer of coal, which accounts for about 70% of China's energy use. In October 2009, China's media reported that thousands of children living near smelters had been found to have excessive amounts of lead in their blood. Although growing environmental degradation has been recognized as a serious problem by China's central government, it has found it difficult to induce local governments to comply with environmental laws, especially when such officials feel doing so will come at the expense of economic growth. According to a study by ExxonMobil, China's, energy demand for power generation will more than double by 2030, surpassing U.S. demand by

[25] Washington Post, October 29, 2009.

[26] See CRS Report RS22713, *Health and Safety Concerns Over U.S. Imports of Chinese Products: An Overview.*

more than one third. In addition, by 2030, China's CO2 emissions are expected to be comparable to those in the United States and EU combined.[27]

The Chinese government is attempting to address several of these areas. In October 2006, the Chinese government formally outlined its goal of building a "harmonious socialist society" by taking steps (by 2020) to lessen income inequality, improve the rule of law, enhance environmental protection, reduce corruption, and improve the country's social safety net (such as expanding health care and pension coverage to rural areas). In March 2007, the Chinese National People's Congress (NPC) passed a law to strengthen property laws to help prevent local governments from unfairly seizing land from farmers, and in June 2007, it passed a new labor contract law to enhance labor rights. In addition, the government has scrambled to improve health and safety laws and regulations. The government has also pledged to boost energy efficiency, crack down on polluting industries, and to promote the development of and use of green technology (such as solar power, wind power, biomass). For example, it has set a target of deriving 20% of energy from renewable sources by 2020. In April 2009, the government pledged to implement a three-year, $124.4 billion, plan to begin the establishment of universal health care plan, expected to be in place by 2020.

Fallout From the Current Global Financial Crisis[28]

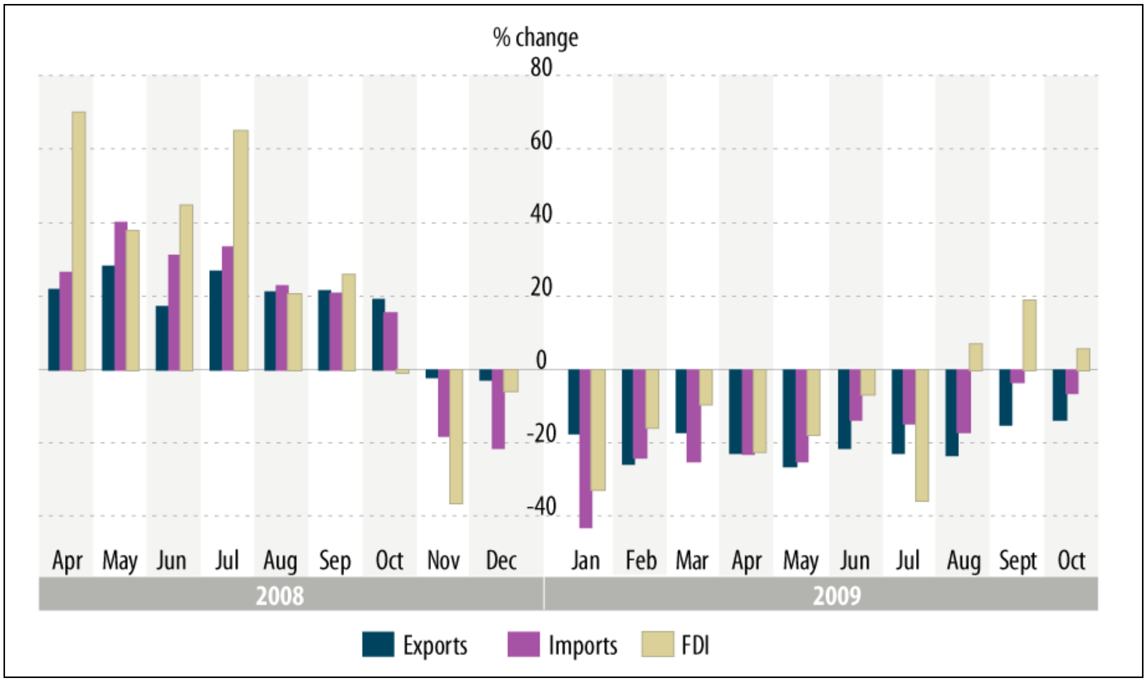
China's economy suffered a sharp slow-down as a result of the global financial crisis, largely due to a decline in foreign demand for Chinese imports and a drop-off in FDI in China. From January to September 2008, China enjoyed nearly double-digit growth in monthly exports and FDI on a year-on-year basis. However, from November 2008 to October 2009, China's monthly exports (and imports) on a year-on-year basis declined. FDI flows dropped during the months of October 2008 through July 2009, (see **Figure 8**). From January-October 2009, China's total exports, imports, and FDI were down by 20.5%, 19.9%, and 12.6%, respectively over the same period in 2008. China's trade with its major trading partners has declined sharply in 2009 (through September 2009) over 2008 levels, as indicated in **Figure 9**.

[27] ExxonMobil, *The Outlook for Energy*, A View to 2030, p. 4.

[28] For additional information, see CRS Report RS22984, *China and the Global Financial Crisis: Implications for the United States*, by Wayne M. Morrison.

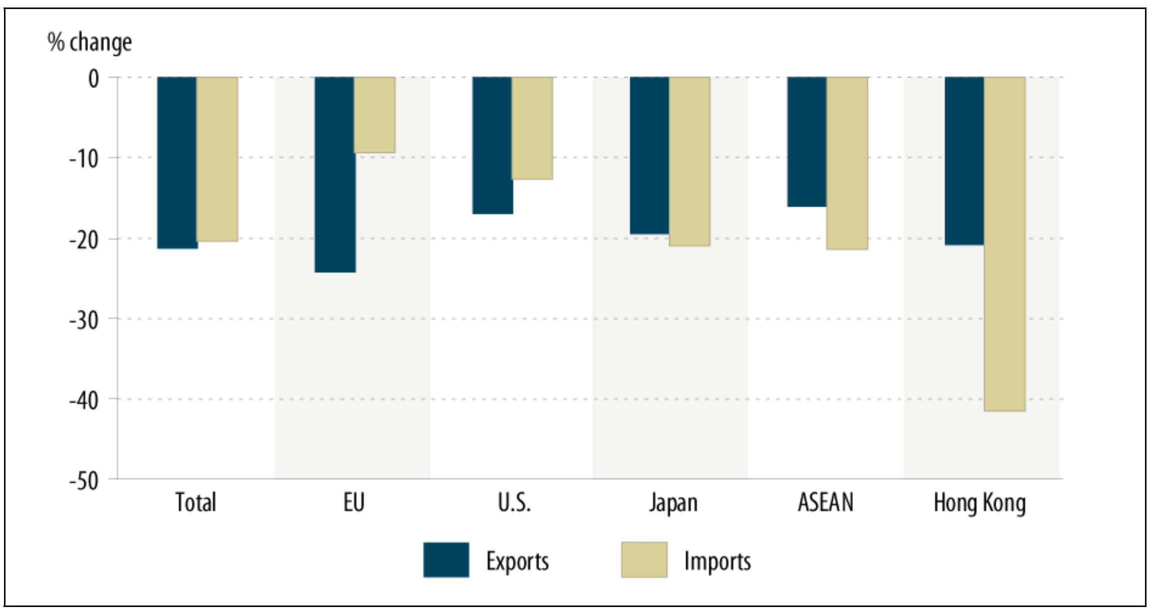
Figure 8. Monthly Percentage Change in China's Trade and FDI: April 2008-October 2009

Year-on-Year Basis



Source: China's Customs Administration.

Figure 9. Change in China's Trade With its Major Trading Partner: January-September 2009 Over the Same Period in 2008



Source: China's Customs Administration.

China's quarterly real GDP growth on a year-on-year basis dropped from 10.1% in the second quarter of 2008 to 6.1% in the first quarter of 2009. In January 2009, the Chinese government reported that 20 million migrant workers had lost their jobs due to the global financial crisis. The real estate market in several Chinese cities exhibited signs of a bursting bubble, including a slow down in construction, falling prices, and growing levels of unoccupied buildings.

China took a number of steps to stimulate its economy. On November 9, 2008, it announced that it would implement a two-year $586 billion stimulus package, mainly dedicated to infrastructure projects. Interest rates and taxes were cut, and a number of subsidies were offered to consumers to purchase various products, such as cars. In addition, the government directed banks to loosen credit requirements, which resulted in a sharp increase in bank lending. It is estimated that Chinese banks made $1.27 trillion in new loans during the first nine months of 2009.[29]

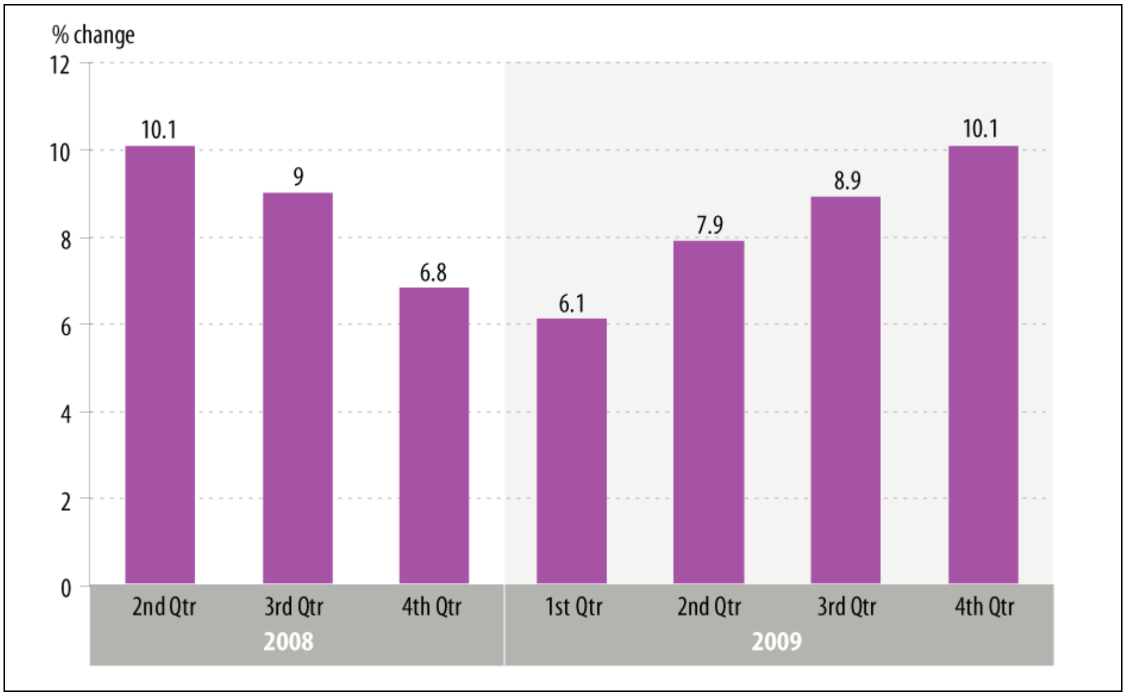
These measures appear to have been effective. China's real quarterly GDP on a year-on-year basis rose by 7.9% in the 2nd quarter of 2009 and by 8.9% in the 3rd quarter of 2009. The IMF predicts 4th quarter growth at 10.1% (see **Figure 10**). Although China's trade in 2009 has not rebounded to 2008 growth levels, it has shown gradual growth since around February 2009 (see **Figure 11)**. In addition, FDI growth in China for the months of August, September, and October 2009 were higher than in the same months in 2008. The IMF in October 2009 projected China's real GDP would rise by 8.5% in 2009 (and by 9.0% in 2010), a level significantly higher than what has been projected for most of the other major world economies (see **Figure 12**).

Despite these positive growth projections, some economists warn that long-term economic growth will depend largely on the ability of the government to rebalance the economy away from trade and FDI to domestic consumption. Many have also raised concerns that easy money policies could lead to overproduction in some industries and create asset bubbles in certain sectors, such as in real estate and the stock market. In June 2009, a Chinese government agency estimated that 20% of new bank credit was going into China's stock markets.

[29] Global Insight, Country Intelligence, China, October 15, 2009.

Figure 10. Change in China's Quarterly Real GDP Growth: Second Quarter 2008 to Third Quarter 2009 and Projection for Fourth Quarter 2009

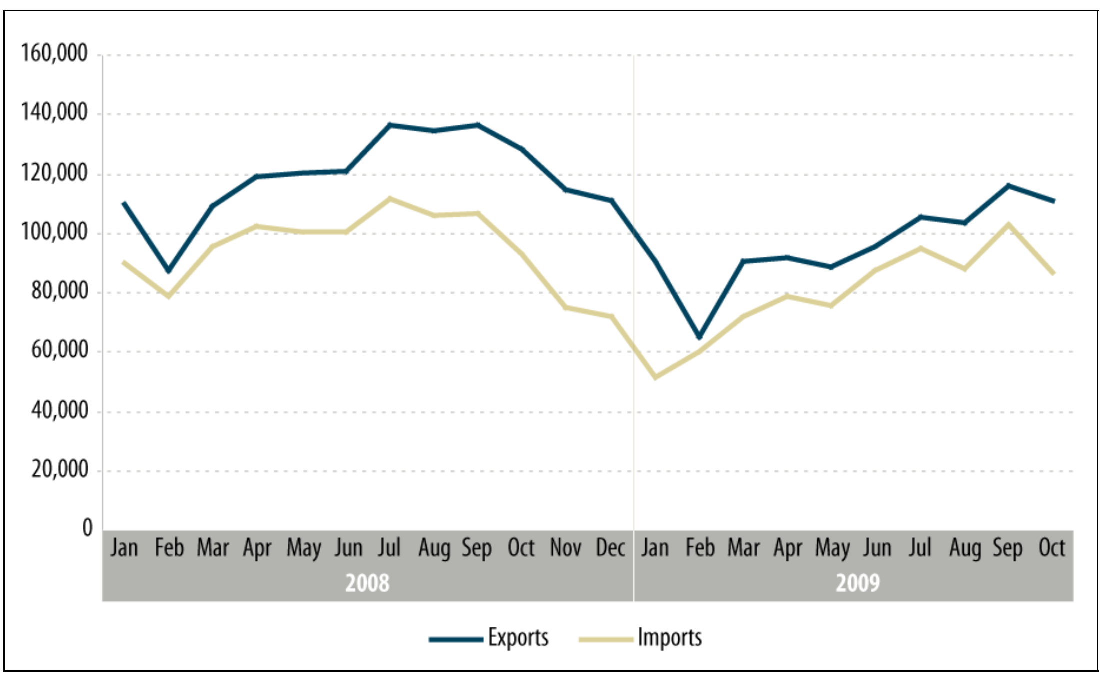
Year-On-Year Change



Source: Actual data from Global Insight. Fourth Quarter 2009 projection from IMF.

Figure 11. China's Monthly Trade Data in Dollars: January 2008-October 2009

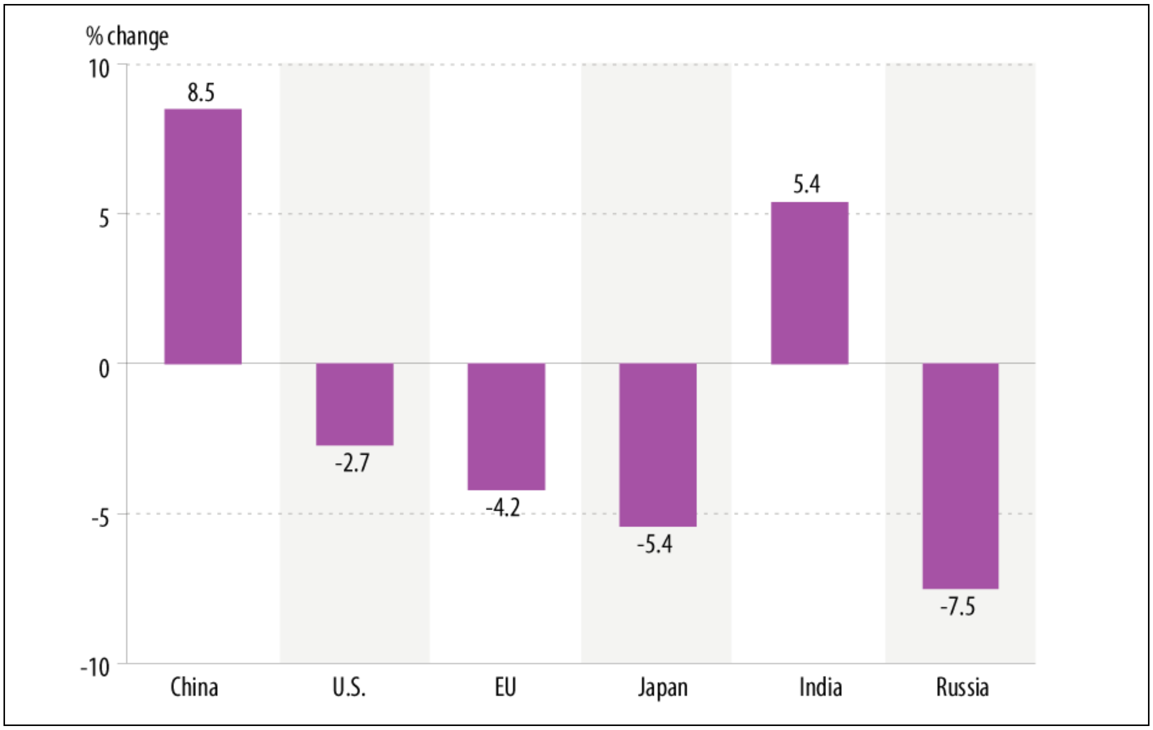
$ millions



Source: China Customs Administration.

Figure 12. Projected Real GDP of Major Economies in 2009

% growth over 2008 levels



Source: International Monetary Fund, World Economic Outlook, October 2009.

Appendix. China's Growing Economic Ties with Africa, North Korea, and Iran

China has sought to expand its trade with countries around the world, especially those that possess energy and raw materials China needs to sustain its rapid economic growth, such as those in Africa. Although China's trade with these countries is relatively small (compared with its major trading partners), it is growing rapidly. China is also a major trading partner of various countries that pose challenges to U.S. foreign policy, such as Iran, Sudan, and North Korea.[30]

China-Africa Trade

China's Imports From Africa

China's imports from Africa as a percent of its total imports grew from 2.8% in 2004 to 5.2% in 2008 (to $46.7 billion).[31] If taken as a whole, Africa would have been China's seventh largest source of imports in 2008. From 2004-2008, China's imports from Africa grew by 192%. Mineral fuels were by far China's largest import from Africa, accounting for 71% of total imports. Angola was China's largest source of imports from Africa, accounting for 41% of those imports in 2008, followed by South Africa, Sudan, the Congo, and Libya. China's imports from Sudan were up 199% from 2004 to 2008 (see **Table A-1** and **Table A-2**). It is estimated that China is Sudan's largest trading partner, accounting for 56% of its exports, and 25% of its imports, in 2008.[32]

Table A-1. Top Five African Sources of Chinese Imports: 2004-2008

($ millions)

	2004	2005	2006	2007	2008	2004-2008 % Change
Africa Total	**15,641**	**21,114**	**28,768**	**36,330**	**45,672**	**192.0**
Angola	4,718	6,581	10,931	12,885	18,721	296.8
South Africa	2,955	3,444	4,095	6,608	6,976	136.1
Sudan	1,706	2,615	1,941	4,114	5,108	199.4
Congo	1,569	2,278	2,785	2,828	3,724	137.3
Libya	417	942	1,694	1,548	2,577	518.0

Source: *World Trade Atlas*. Official Chinese statistics.

[30] For additional information on policy challenges posed by North Korea, see CRS Report RL33590, *North Korea's Nuclear Weapons Development and Diplomacy*; and CRS Report RL32493, *North Korea: Economic Leverage and Policy Analysis*. For information on policy challenges posed by Sudan, see CRS Report RL33574, *Sudan: The Crisis in Darfur and Status of the North-South Peace Agreement*.

[31] In comparison, U.S. imports from Africa in 2008 were $85.0 billion (or 5.9% of total). Note, the United States reports import trade data on a customs basis, while China reports imports on a cost, insurance, and freight (C.I.F.) basis. The C.I.F. basis differs from the customs basis in that the former includes the cost of insurance and freight and thus raises the value of imports (which the customs basis does not), by about 10%. Both U.S. and Chinese imports from Africa have declined sharply in 2009.

[32] CIA, *The World Factbook*, 2009.

Table A-2. Major Chinese Imports from Africa: 2004-2008

($ millions and %)

HS 2 Commodity Description	2004	2005	2006	2007	2008	% of Total 2008	2004-2008 % Change
Mineral fuel, oil, etc.	10,135	14,676	21,083	25,997	38,489	70.7	279.8
Ores, slag, ash	1,393	1,577	2,116	3,298	7,254	13.0	402.7
Precious stones and metals (mainly platinum and diamonds)	742	967	1,196	1,358	1,772	3.2	138.8

Source: *World Trade Atlas*. Official Chinese statistics.

China's Mineral Fuel Imports From Africa

Africa has become an important source of China's surging energy needs. In 2008, 71% of China's imports from Africa were mineral fuels.[33] China's fuel imports from Africa rose from $10.1 billion in 2004 to $38.5 billion in 2008, up 280%. In 2008, Africa supplied 27.8% of China's imported mineral fuels (compared with 9.1% in 1997). Angola was China's second largest overall mineral fuel supplier and its largest African supplier. Other major African suppliers (and the world rank) of mineral fuel to China were Sudan (7th), the Congo (16th), and Libya (18th) (see **Table A-3**).

Table A-3. Top Five African Suppliers of Mineral Fuel to China: 2008

Country	Imports ($ millions)	Rank as a Supplier of Mineral Fuel to China
Angola	22,347	2
Sudan	6,267	7
Congo	3,085	16
Libya	2,540	18
Equatorial Guinea	2,190	19
Africa Total	38,489	—

Source: *Global Trade Atlas*.

China's Exports to Africa

The share of Chinese exports going to Africa rose from 2.3% in 2004 to 3.6% in 2008 ($50.9 billion).[34] If Africa were treated as a single trading partner, it would rank as China's sixth largest export market (2008).[35] Exports to Africa grew by 268% from 2004 to 2008. Major Chinese exports to Africa in 2008 included electrical machinery, machinery (such as computers and

[33] If Africa were treated as a single trading bloc, it would be the largest source of Chinese mineral fuel imports.

[34] In comparison, total U.S. exports to Africa in 2008 were $28.4 billion (2.2% of total U.S. exports).

[35] Chinese and U.S. exports to Africa have declined sharply in 2009.

components), and vehicles (mainly motorcycles and trucks). The top five African destinations of Chinese exports in 2008 were South Africa, Nigeria, Egypt, Algeria, and Angola (see **Table A-4** and **Table A-5**).

Table A-4. China's Top Five African Export Markets: 2004-2008

($ millions)

Country	2004	2005	2006	2007	2008	2004-2008 % Change
Africa Total	**13,815**	**18,687**	**26,705**	**37,314**	**50,869**	**268.2**
South Africa	2,952	3,826	5,769	7,429	8,596	191.2
Nigeria	1,719	2,305	2,856	3,800	6,758	293.1
Egypt	1,389	1,935	2,976	4,432	5,817	318.8
Algeria	981	1,405	1,952	2,709	3,685	275.6
Angola	193	373	894	1,241	2,931	1,418.7

Source: *World Trade Atlas*. Official Chinese statistics.

Table A-5. Major Chinese Exports to Africa: 2004-2008

($ millions)

HS 2 Commodity Description	2004	2005	2006	2007	2008	% of Total 2008	2004-2008 % Change
Electrical machinery and parts[a]	1,905	2,799	4,122	5,806	8,882	17.5	366.2
Machinery, mechanical appliances, and parts	1,374	2,141	3,220	4,517	7,292	14.3	430.7
Vehicles (excluding railway) and parts	936	1,448	2,023	3,165	4,730	9.3	405.3

Source: *World Trade Atlas*. Official Chinese statistics.

a. Includes electrical machinery and equipment and parts thereof; sound recorders and reproducers; television image and sound recorders and reproducers; and parts and accessories of such articles.

China's Trade with North Korea

Chinese trade with North Korea is of concern to Congress due to North Korea's nuclear program, its violations of human rights, and the military threat it poses to South Korea.[36] China is North Korea's largest trading partner and is believed to be a major provider of foreign aid to North

[36] See CRS Report RL33590, *North Korea's Nuclear Weapons Development and Diplomacy*; CRS Report RL31785, *Foreign Assistance to North Korea*; and CRS Report RL32493, *North Korea: Economic Leverage and Policy Analysis.*

Korea, largely in the form of food and fuel.[37] Many U.S. policymakers have urged China to make greater use of its "economic leverage" with North Korea, especially on the nuclear issue.

North Korea is a relatively minor trading partner for China. In 2008, Chinese exports to, and imports from, North Korea totaled $2,033 million and $754 million, respectively.

North Korea was China's 70th largest source of imports (0.07% of total) and its 64th largest export market (0.14% of total).[38]

Chinese exports to North Korea rose by 13.0% and imports were up 24.3%, over 2006 levels. China accounted for 37.3% of North Korea's exports and 39.8% of its imports (2005 data).[39] According to Chinese data, its top five exports to North Korea (2007) were oil, machinery, electrical machinery (such as TVs), plastics, and vehicles (see **Table A-6**), while its top imports from North Korea were ores, coal, woven apparel, fish, and iron and steel (see **Table A-7**).

Table A-6. Major Chinese Exports to North Korea: 2004-2008

($ millions and % change)

	2004	2005	2006	2007	2008	2006-2007 % Change
Total Exports	**795**	**1,085**	**1,232**	**1,392**	**2,003**	**151.9**
Mineral fuel, oil, etc. (mainly oil)	204	286	348	402	586	187.3
Machinery	40	77	83	104	145	262.5
Electrical machinery (such as TVs)	46	57	98	69	101	119.6
Knit apparel	5	6	10	24	87	1,640.0
Plastics	32	52	52	55	80	150.0

Source: *World Trade Atlas*, which uses official Chinese statistics.

Table A-7. Major Chinese Imports from North Korea: 2004-2008

($ millions and % change)

	2004	2005	2006	2007	2008	2004-2008 % Change
Total Imports	**582**	**497**	**468**	**582**	**754**	**29.6**
Ores, slag, and ash	59	92	118	164	213	261.0
Mineral fuel, oil, etc. (mainly coal)	53	112	102	170	208	292.5
Iron and steel	75	72	35	45	78	4.0
Woven apparel	49	58	63	60	77	57.1
Fish and seafood	261	92	43	30	40	-84.7

Source: *World Trade Atlas*, which uses official Chinese statistics.

[37] See CRS Report R40095, *Foreign Assistance to North Korea.*

[38] *World Trade Atlas.*

[39] Economist Intelligence Unit, *Country Report, North Korea*, February 2008, p. 5.

China's Trade With Iran

Chinese economic ties with Iran are of concern to Congress because of Iran's nuclear program and because of Iranian threats to U.S. foreign policy interests.[40] China is Iran's largest trading partner, accounting for 18.5% of Iran's exports and 13.0% of its imports (2008).[41] Iran was China's 16th largest source of imports ($19.6 billion) and 32nd largest export market ($8.0 billion), according to Chinese trade data (see **Table A-8**). Mineral fuels accounted for 86% of China's imports from Iran;[42] other major imports included ores and organic chemicals. China's main exports to Iran were machinery, electrical machinery, and vehicles (excluding railroad).

Table A-8. China's Trade With Iran: 2004-2008

($ billions and % change)

	2004	2005	2006	2007	2008	2004-2008 % Change
Exports	2,555	3,298	4,479	7,288	8,047	215.0
Imports	4,484	6,796	9,946	13,300	19,581	336.7

Source: Global Trade Atlas.

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[40] See CRS Report RL32048, *Iran: U.S. Concerns and Policy Responses*; and CRS Report RL34525, *Iran's Economic Conditions: U.S. Policy Issues*.

[41] CIA, *The World Factbook*, 2009.

[42] Iran was China's third largest source of mineral fuels.