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of Xiamen University

China's Macroeconomic Outlook

Quarterly Forecast and Analysis Report, September 2012

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Preface I

The Center for Macroeconomic Research (CMR), one of the Key Research Institutes of Humanities and Social Sciences sponsored by the Ministry of Education of China, has been focusing on studying China's economic growth and policies. Led by Professor Li Wenpu, Director of CMR, and cooperated with the Asia Research Center in Nanyang Technology University, Singapore, CMR started to develop the CQMM (China's Quarterly Macroeconomic Model) for the purpose of short-term forecasting, policy analysis and simulation since 2005.

Based on the CQMM, CMR and its partners hold press conferences to release forecast results on major macroeconomic variables for the next eight quarters. Since August 2006, 12 quarterly reports on China's macroeconomic outlook have been presented and six annual reports have been published.

As the 13th quarterly report, this is a summary of the studies presented at the Forum on China's Macroeconomic Prospects and Press Conference of China Quarterly Macroeconomic Model in September 2, 2012. This conference was jointly held by the CMR, Economic Information Daily and Xinhua News Agency. Financial aid from the Ministry of Education of China National Social Science Foundation and National Science Foundation is acknowledged. We deeply thank all key note speakers for their valuable comments, based on which we revised the report. We also appreciate the media for reporting the conference.

We take responsibility for any errors in this report.

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Preface II

The growth rate of gross domestic product (GDP) of China continued to decline in the first half of 2012. The economic slowdown was due to external and domestic factors, including the sovereign debt crisis in the euro area, weak economic recovery in the US and domestic macroeconomic management, such as the new regulations on the real estate market. More importantly, in addition to sluggish export markets, excess capacity in some industries has undermined enterprise investment, especially investment of the small or micro-businesses. As a result, the prudent or tight monetary policy had failed to boost investment. Therefore, the authority has switched from tight monetary policy to loose monetary policy in the second quarter of 2012.

Owing to the decline of domestic investment and trade with the rest of the world, China's real GDP was lower than expected, though the increase in residential income has promoted the contribution of final consumption to economic growth. Therefore, in order to create a good environment for further reforms and economic structural adjustments and the sustainability of development, as well as to maintain steady growth, it is crucial to adopt new economic policies.

The research team assumes that the euro area will continue to slump in the second half of 2012, resulting in a significant fall in the growth rates of China's exports, and China will adopt a loose monetary policy to reboot growth. Very likely, interest rates could be cut by 0.25 percentage point in the fourth quarter of 2012. With the growth rate of M2 in 2012 is 13.8 % and with the moderately expansionary fiscal policy, the forecast results include: the actual GDP grow at 7.8 % in 2012 and then rebound to 8.29 % in 2013; the actual CPI would be 2.6 % in 2012 and then would pick up to 3.27 % in 2013.

Because of the bleak perspective of external demand in 2013, China's investment growth is forecast to slowdown in 2012, but should remain at a high level, as a result of loose monetary policy. On the other hand, growth rate of residential consumption is expected to remain at moderate level because residential income is increasing. Hence, final consumption as a share in GDP would rise, while the share of fixed asset investment in GDP would shrink compared with previous year. The research team suggests that, with China's economic growth slowing down due to shrinking investment and bleak perspective of exports, a constant expansion in residential

consumption would contribute to growth of GDP. Therefore, it is crucial to continue to increase residential income and to boost residential consumption through structural adjustments and deepening reform, such as reshape the income distribution pattern.

In conclusion, due to bleak perspective in euro area and less robust growth in the US in 2013, China's economy should continue a downward trend. However, the slowdown of the growth rate would be moderate as a result of the modestly proactive macrocontrol policy.

A crucial question is whether China's economy would plummet if the sovereign debt crisis in the euro area would worsen, which is highly likely, and the U.S. economic recovery would be weak. Under this circumstance, should China launch a new massive investment stimulus package?

Based on the first scenario assumed in CQMM, in the second half of 2012 and 2013, the sovereign debt crisis in the euro area would worsen, the economic growth of euro area would significantly decline and the growth rate of the U.S. economy would drop significantly. The value of Euro against the U.S dollar would depreciate further compared with the conclusions of the baseline model; the exchange rate between RMB and the U.S. dollar, and the monetary policy would be the same as those of the baseline model. The simulation results suggest that: (1). China's growth rates of imports and exports would decline considerably. (2). In 2012 and 2013, the setback in China's exports should further undermine its economic growth. Real GDP is forecast at 7.71 % and 7.5 %, lower than forecast in the baseline model decreases of 0.31 and 0.79 percentage point, respectively. (3). A more severe recession in the euro area is expected to bring down China's inflation rate. In this scenario, CPI is expected to increase by 2.69 % in 2012, followed by a further decrease of 1.84 % in 2013. (4). The investment demand is expected to maintain a relative high growth rate due to deflation of investment goods, caused by the plunge in the price index of investment in fixed assets. To some extent, expansion in investment should offset the negative impact of the sluggish external market and then help to stabilize GDP growth at the level of 7.5 % in 2013.

The second scenario assumes that China will implement a new massive investment expansion by launching a "2 trillion Yuan stimulus package" and adopt a loose money supply (M2) with growth rates of 16 % and 17 % in 2012 and 2013, respectively.

The simulation shows that, under the assumptions on external economic environment as in the baseline model, launching a "2 trillion Yuan stimulus package" would not boost the growth rate of GDP significantly. As a result of expansion in credit and money, inflation would rebound considerably. Moreover, the existent imbalance in the economic structure would worsen.

Simulations based on the above two distinguished scenarios show that even if the external economic environment becomes worse, China's growth is expected to stay at above 7.5 %, which might be a steady growth rate for the near future. In other words, the growth trend for China's economy is characterized by "stability with slight slowdown". Although economic risk in the euro area will put downside pressure on China's economy in the short term, with a modest expansionary macropolicy, the economy could maintain a relative low but steady growth rate. The growth rate of 7.5 % might be the lower bound for the coming years. If China plans to achieve a

higher growth rate by launching the "2 trillion massive investment package," the growth rate could be increased to 8.25 % and 8.86 % in 2012 and 2013 with a risk of inflation and worsening economic structure. With domestic demand expansion (consumption plus investment), a growth rate around 8 % should be feasible. In one way, 8 % may be the normal or potential growth rate, as China ends its first period of two-digit growth rate and begins the second growth period.

As shown above, the cost of any policies pursuing a higher growth rate would be very expensive, for it might delay economic structural adjustments. Therefore, launching a new massive fiscal stimulus plan should not be an option. The policy implication from CQMM is: on one hand, the Chinese government should be able to maintain a growth rate around 8 % via timely fine-tuning of monetary policies; on the other hand, the emphases of the macrocontrol should be placed on structural adjustments through fiscal policies. In the long run, deepening economic, social and institutional reform will be crucial to remove the significant structural imbalance and institutional barriers to market competition, to accelerate the transformation of economic development pattern and finally to maintain a sustainable growth rate. During the period of the "Twelfth Five-Year Plan", the Chinese government should focus on improving the efficiency of resource use by letting markets determine the prices of production factors, on adjusting national income distribution to raise the residential income, on establishing a government with restricted administrative power, on reducing tax burden and the share of government revenue, on improving the people's wellbeing by adjusting fiscal expense structure, on eliminating monopoly and narrowing down income gap and on creating the conditions for transiting to China's economy to a new development stage, in which economic growth will mainly depend on domestic demand. A slight low economic growth rate should also be able to promote social progress and to ensure welfare improvement, as long as the economic structure is balanced and as long as there is more efficiency, more inclusivity and more attention to the people's well-being.

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Chapter 1
Review of Macroeconomic Performance in the First Half of 2012

In the first half of 2012, the quarterly growth rate of China's GDP continued to decline compared to the same period of last year. The cumulative growth rate of GDP for the first half was 7.8 %, which is the lowest level since 2010 (see Fig. 1.1). From the long term perspective, the slowdown of economic growth is the outcome of global economy rebalancing. It also is associated with the declining of China's potential economic growth rate, after China ended a development stage with two-digit growth rate over the past 30 years and stepped into a new development stage at a slight low growth rate as a middle income country. From the short term perspective, it was partly due to economic recession in the euro area. It also resulted from excess production capacity, structural imbalance in manufacturing industry caused by rapid domestic investment expansion in the past few years, and the new real estate market regulations. The declining economic growth in China, together with uncertainty of the EU and the US economy, has triggered concerns about the future economic outlook. Thus, it is highly important that China adopts proper measure to stabilize economic growth and create conditions for further social and economic reforms and transformation of economic development pattern.

1.1 Declining Economic Growth Rates and the Price Level

In the first half of 2012, due to the European sovereign debt crisis and the slow economic recovery in the United State, China's growth rate of exports decreased significantly. Because of the slow growth of exports, excess production capacity caused by investment expansion in the past 2 years, and the new real estate market regulations. China economy did not grow as fast as before. Although monetary policy has been appropriately eased since the beginning of the year, the cumulative growth rate of GDP was only 7.8 % in the first half year. Meanwhile, both Consumer Price Indices (CPI) and Producer Price Indices (PPI) kept going down.

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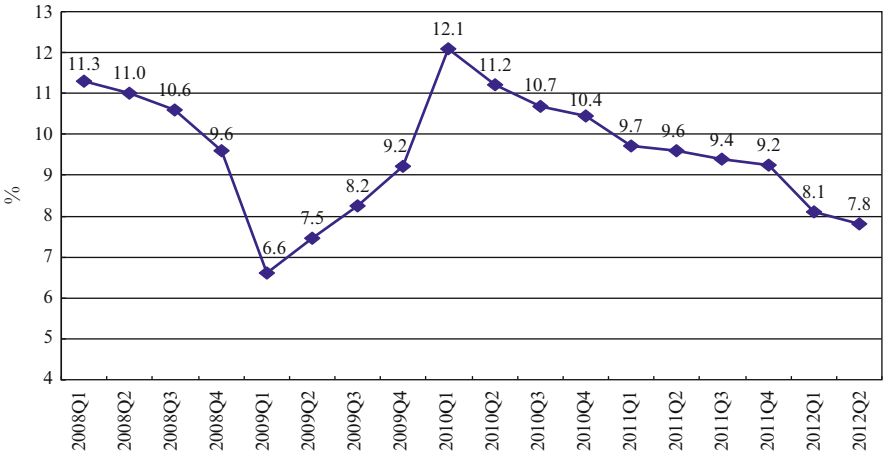

Fig. 1.1 Quarterly cumulative growth rate of gross domestic product (GDP) in 2008–2012 (Sources: CEIC)

The year-on-year growth rate of CPI was only 2.2 % in June,[1] which was the lowest level for 29 consecutive months; the core CPI (excluding food and energy) reached 1.3 %. PPI also had decreased for 11 consecutive months, from 7.5 to −2.1 %. The chained CPI in June was −0.6 %, and the chained core CPI became 0.1 %; the chained PPI was −0.7 % (see Fig. 1.2).[2]

1.2 Declining Growth Rate of Fixed Asset Investment, Industrial Added Value and Profit Rate

Despite the loose monetary policy adopted since February 2012, the excess production capacity, the sluggish external market and the new real estate market regulations had been retarded fixed asset investment, slowed down industrial added value and reduced profit rate. In the first half of 2012, expansion in gross capital formation accounted for 49.4 % in GDP growth, 9.7 and 3.8 percentage points down, respectively, compared with the same period of 2010 and 2011. The contribution of gross capital formation to GDP growth was only 3.9 percentage points, which was lower than the same periods of 2010 and 2011. At the same time, the cumulative growth rate of fixed asset investment was 20.4 %, a decrease of 5.2 percentage points over the previous year.

[1] In July, CPI further dropped to 1.8 %. If not specially noted, all growth rate below is Year-On-Year growth rate.

[2] From May 2012, the global price of food in the next half year or even in 2013 might be pulled up due to the draught in western and central of U.S., which indicates the pressure of imported inflation is still high.

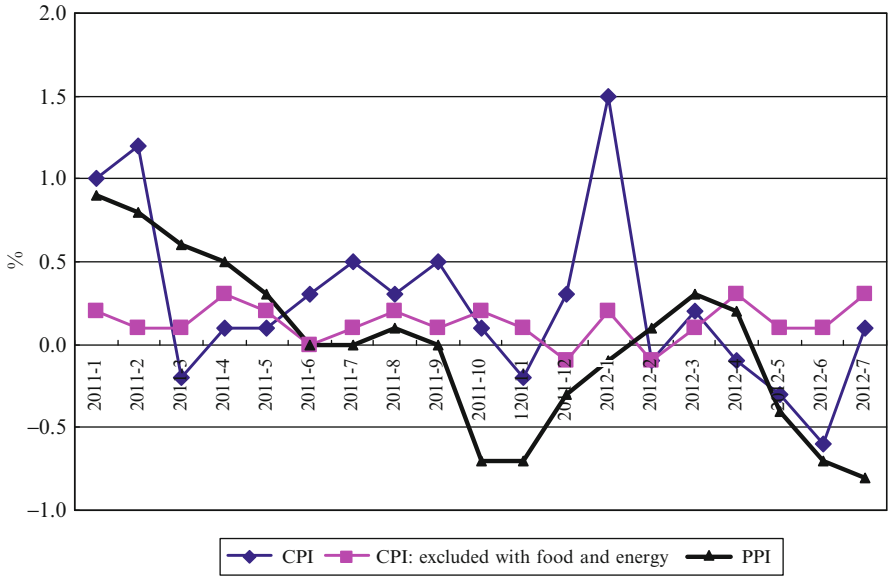

Fig. 1.2 Change in chained main price indexes (Sources: CEIC)

In the first half of 2012, the growth rate of central investment in newly increased fixed assets in urban area hadn't increased, while the growth rate of local investment decreased slightly but stayed at a high level of 22.1 %, playing a leading role in investment expansion. Looking at investments in fixed asset in urban area of each industry, investments in manufacturing industry increased by 24.5 %, a decrease of about 7.9 percentage points compared with the same period of 2011; investments in real estate grew by 22.1 %, a decrease of about 9.8 percentage points; the growth rate of investments in transport, storage and post was −2.0 %, a decrease of 18.3 percentage points (see Fig. 1.3). It is clear that investments in the real economy were experiencing overall downturn. Looking at investment in fixed asset in urban area by registration status, investment by the state-owned and state-holding enterprises increased by 13.8 %, a drop of about 0.8 percentage points; investments by the enterprises from Hong Kong, Macao, Taiwan province increased by 11.2 %, a drop of about 13.7 percentage points; foreign funded investments increased by 13.9 %, a drop of about 3.7 percentage points.

Turning to industrial production, the growth rate of total value added and total profits from large industrial enterprises slowed down. Among main indicators, electricity demand by industries declined greatly. Up to June 2012, the cumulative growth rate of industrial value added was 10.5 %, a fall of about 3.8 percentage points, which indicated a monthly by monthly downward trend. In the first half of 2012, the growth rate of value-added of the secondary industry was 8.3 %, dropped by about 5 and 2.6 percentage points, respectively, compared with the same period of 2010 and 2011. The cumulative growth rate of profit rate of the industrial

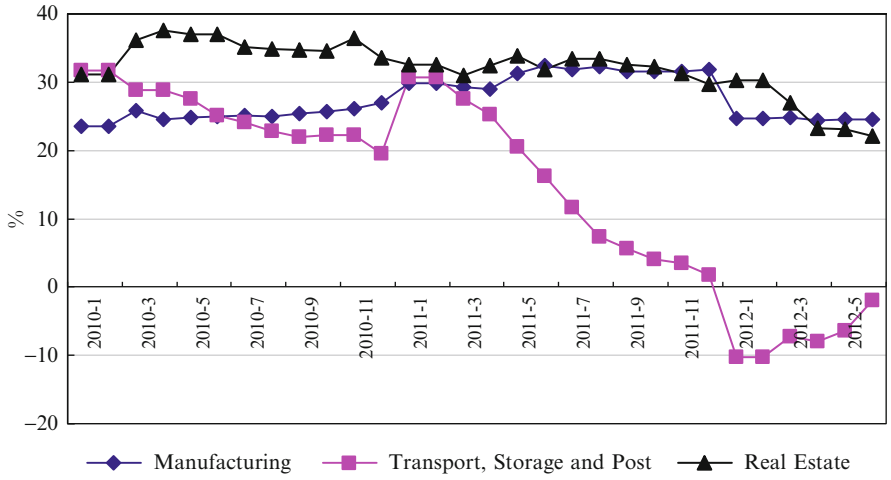

Fig. 1.3 Change in growth rates of investment in certain industries (Sources: CEIC)

enterprises was −2.2 %, substantially dropped by about 30.5 percentage points; looking at different types of enterprises, only the private enterprises achieved a positive profit growth, while all the rest of other enterprises experienced a negative profit growth. Moreover, the cumulative growth rate of electricity demand by industries in the first half of 2012 was 3.7 %, about 8 percentage points lower compared with the same period of last year; the growth rate of freight turnover was 10.1 %, dropped by about 4.3 percentage points. The manufacturing purchasing managers' index (PMI) experienced a change of up-and-down: suddenly rose in March due to loose monetary policy, followed by a slightly drop in April, and then sharply decline to nearly 50 % in May before further sliding down to 50.2 % in June.[3] Moreover, the PMI for new orders dropped dramatically to 49.8 % in May, and continued to reach 49.2 % in June (see Fig. 1.4). All of above indicated that the real industries were experiencing a downturn in the first half of 2012.

1.3 Declining Import and Export Growth and Robust Residential Consumption

Influenced by the weakening economic situation in the main trading partners, the cumulative growth rate of export reached 9.2 % in the first half year. With the price of the bulk commodity going down, the growth rate of import declined by 6.7 % and total value of import and export increased by 8 %. Total trade surplus was 68.92 billion dollars, an increase of 56.4 % over last year. Looking at components of total

[3]PMI dropped to 50.1 in July based on data published on Aug 2nd.

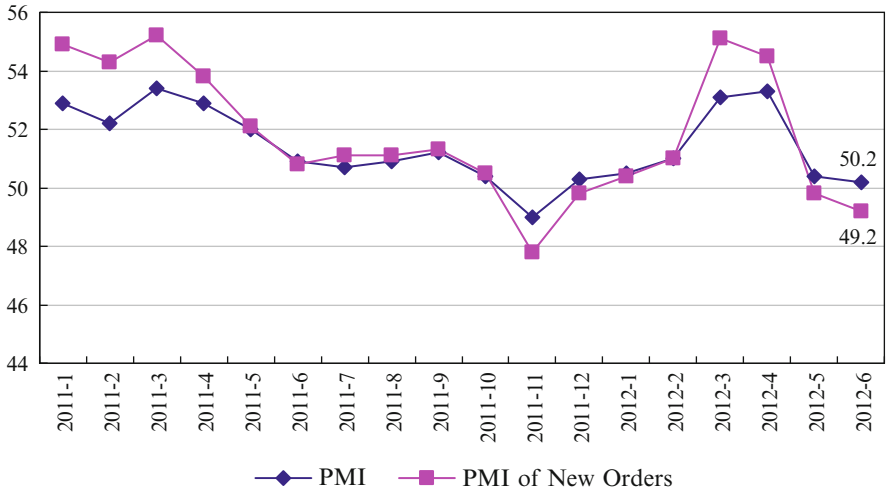

Fig. 1.4 Change in PMI (Sources: CEIC)

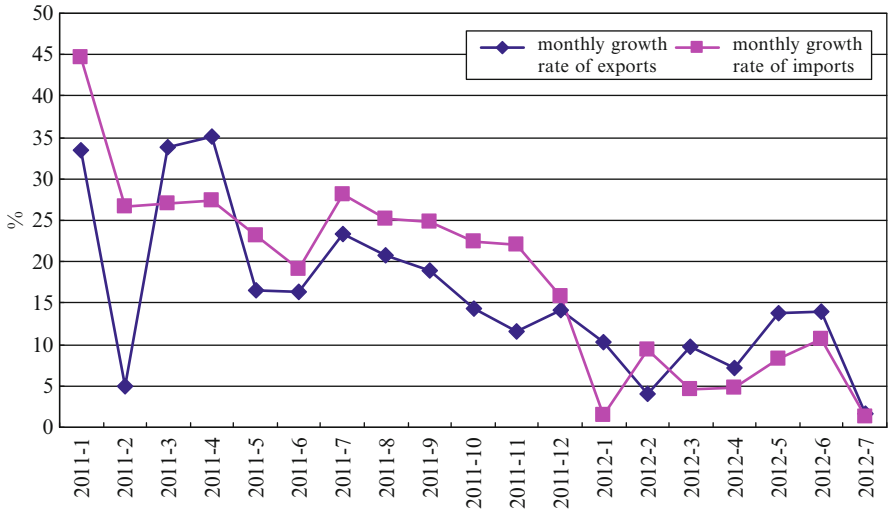

Fig. 1.5 Change of monthly growth rates of exports and imports after seasonally adjusted (year-on-year) (Sources: CEIC)

trade surplus, deficits from general trade decreased while surplus from processing trade increased. After seasonal adjustment, the growth rate of total value of import and export in the first 7 months of 2012 was far below the level for the same period of last year: the growth rates of export and import in June were 13.9 % and 10.6 %, respectively, while the total value of imports and exports growth rate was 12.4 % (see Fig. 1.5). In terms of monthly growth rate, exports increased by 4.3 % and

imports decreased by 0.6 %, while total value of exports and imports increased by 2 % in June.[4] The contribution share and contribution of net export from goods and service to GDP growth were –0.6 % and –7.1 %, respectively.

In the first half of 2012, disposable income of per urban resident was 12508.5 Yuan, which increased by 9.7 % (in real term), while cash income (or disposable income) for per rural resident was 4283.4 Yuan, which increased by 12.4 % (in real term). Owing to fast growth of income and the decline in the price level, together with structural tax cuts policies, total value of retail sales of consumption goods increased by a rate of 14.4 %, which dropped 2.4 percentage points compared with previous year. The contribution of final consumption expenditure to GDP growth was 4.5 percentage points, and the contribution share to GDP growth was 57.7 %, which increased by 22.6 percentage points and 10.2 percentage points, respectively, compared with the same period of 2010 and 2011.

1.4 Limited Effectiveness of Monetary Policy and Expected Active Fiscal Policy

In response to adverse effects of the slowdown of global economic growth in the first half of 2012, China began to adopt a loose monetary policy. Up to the end of July, the central bank had reduced deposit reserve rates and benchmark interest rates twice.[5] Looking at money supply, the growth of M1 remained at a low rate, while both M0 and M2 increased dramatically. Among them, the growth rate of M2 rebounded to 13.6 %, which dropped by 2.3 percentage points on a year-on-year basis. Accordingly, credit funds of financial institutes began to expand. Up to the end of June, the cumulative newly increased loans amounted to RMB 4.85 trillion, increased by 685.05 billion Yuan over last year. In terms of components of loan, however, short-term loans reached 3.14 trillion Yuan, while medium and long-term loans was only 1.57 trillion Yuan. As a result, the ratio of short-term loans to medium and long-term longs rose to 1.99 from 0.78 in the same period of last year (see Fig. 1.6). This fact indicated that less proportion of newly increased loans went to expanding production capacity or purchasing investment facilities, while large part of them ended up as the means of short-term investment or compensation of liquidity. Furthermore, this reflects that enterprises don't have a positive expectation about future economic outlook. Due to excess production capability, credit expansion could hardly stimulate investment in the real economy; more likely, would stimulate short-term speculation and inflate asset prices again.

[4] After seasonally adjusted, the growth rate for export, import and the total value of exports and imports were 1.6 %, 1.2 %, 1.4 % respectively. And on the month-on-month basis, the growth rate for export, import and the total value of exports and imports were –4.2 %, –5.8 %, –4.9 % respectively.

[5] Deposit reserve rate was sliced down twice in February and May, respectively, from 20.5 % at the end of 2011 to current 19.5 %. The 1-year interest rate of loan was reduced twice in June and July, by about 0.25 percentage point and 0.31 percentage point for each adjustment, respectively.

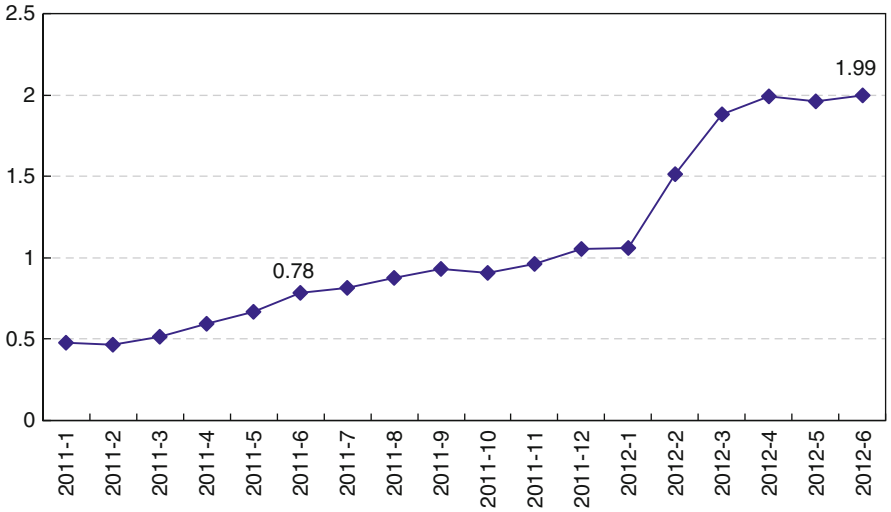

Fig. 1.6 Ratios of short-term loans to medium and long-terms in newly increased loans (Sources: CEIC)

On the side of fiscal policy, due to a decline in the growth rate of enterprises' income tax and value-added tax, which resulted from sharp reduction of the profit growth from industrial enterprises, government fiscal revenue increased by 12.2 % in the first half of the year, which largely dropped by about 19 percentage points. Fiscal expenditure increased by 21.3 %, which was much higher compared with same period of previous years. Looking at the components of fiscal expenditure, expenditure in transportation experienced the fastest growth with a rate of 44.1 %; expenditure in science, education, culture and health care that accounted for the largest share in total fiscal spending also maintained at a fast growth rate of 24.6 %, which dropped by about 6.6 percentage points; the growth rate of spending on social security and unemployment was only 14.4 %, which dropped sharply by about 26.1 percentage points; and the growth rate of expenditure in general public service, agriculture, forestry and water conservancy, and environment protection was 18.6 %, 23.7 % and 26.3 %, respectively, which dropped by about 5.2, 15.1 and 9.6 percentage points, respectively (see Fig. 1.7). This indicated that the growth rate of fiscal spending on transportation infrastructure grew considerably fast, while all the expenditure for people's wellbeing increased relatively slowly.

In summary, as a result of sluggish export markets related to economic recession in the euro area and less robust economic recovery in the U.S., combined with the slowdown of investment growth rate in manufacturing enterprises, as well as the new real estate market regulation, the growth rate of China's GDP fell into a downward trend in the first half of 2012. Moreover, due to the enterprises' adjustment to excess production capacity, the current loose monetary policy had failed to effectively stimulate long-term investment in the real economy. Although improvement of residential

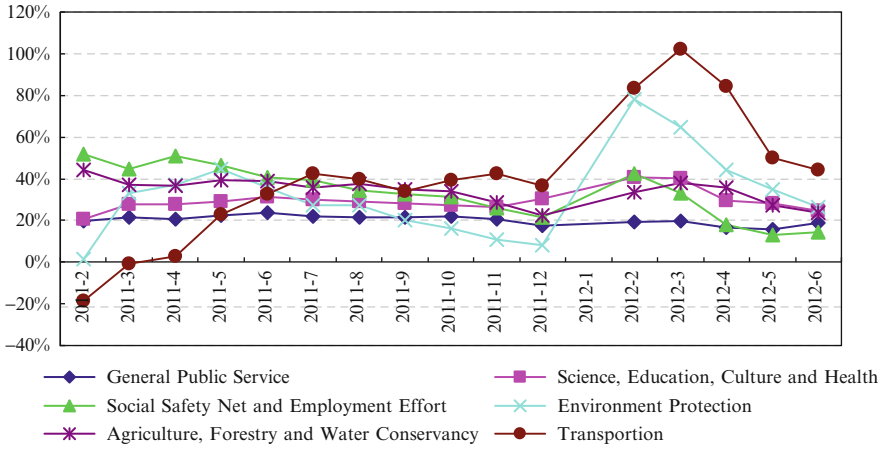

Fig. 1.7 Change in cumulative growth rates of main composition of fiscal expenditure (Sources: CEIC)

income has strengthened the contribution of final consumption to economic growth, it is not large enough to offset the negative effects of shrinking investment and foreign trade. Therefore, how to adopt appropriate macro control policies to stabilize economic growth, create conditions for further deepening reform and structural adjustment, has become an critical issue that is worthy of special attention.

Chapter 2
Forecast for 2012–2013

2.1 Assumptions on Exogenous Variables in a Baseline Model

2.1.1 Economic Outlook for the United State and the Euro Area

Uncertainties in external markets are still major sources of economic fluctuation in China for 2012–2013. In the first half of 2012, the euro area has involved into severe economic turmoil, ending up with a growth rate of −0.8 % in the second quarter, after an optimistic growth rate of 0.06 % in the first quarter (in terms of seasonally adjusted annualized rate). The outlook for the euro area in 2012 is forecast to grow by −0.3 %, according to *World Economic Outlook* (IMF, July 2012). On the other side, the U.S. economy has been on the road to a weak recovery without a rapid decline in unemployment rates. Meanwhile, depressed real estate market and "fiscal cliff" continue to put downward pressure on its recovery. As a result, economic growth is forecast to grow at 2.0 % in 2012 for the United State according to IMF. For 2013, the global economy is expected to rebound, with a growth rate of 0.7 % for the euro area, and 2.3 % for the United State. We assume in a baseline model that, in the context of relatively optimistic outlook for the world economy in the line with IMF's projections, in the second half of 2012, the economy in euro area is expected to show signs of recovery, and the U.S. economy is expected to continue its weak recovery. Specifically, in the third quarter of 2012, the 17 countries in the euro area are expected to suffer an economic contraction of 0.4 %, before picking up with a positive growth rate of 0.4 % in the fourth quarter (see Fig. 2.1).

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	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
USGDP_C	1.96	1.54	0.96	1.21	2.42	3.03	3.24	4.06
EU17GDPC	0.06	−0.80	−0.40	0.40	1.00	1.21	1.29	1.41

Fig. 2.1 Assumptions for economic outlook for the U.S. and the Euro area in 2012–2013 (percent; quarter on quarter, annualized) (Sources: By the authors. Note: EU17GDP_C denotes GDP growth rates of the euro area, USGDP_C denotes GDP growth rates of the U.S)

2.1.2 The Exchange Rates

According to forecast for the world economy above, the Euro is expected to depreciate against the US dollar due to economic contraction. By the end of the fourth quarter of 2012, the value of a Euro against a US Dollar is likely to fall to 1:1.5, and then, stay at the level of 1:1.1 through 2013 after the economy in the euro area starts to recover. For the exchange rate between RMB and the US Dollar, it's unlikely to stop rising in RMB's value against the US dollar from a long run point of view. Even so, it is more likely for RMB to float in a two-way in the short term. Moreover, with gloomy export perspective, shrinking trade surplus, as well as sluggish capital inflow, the value of RMB against the US dollar is expected to depreciate at a slow rate. By the end of 2012, the exchange rate of RMB against US Dollar is expected to appreciate to 6.34:1, and then decline to 6.28:1 in end of 2013 (see Fig. 2.2).

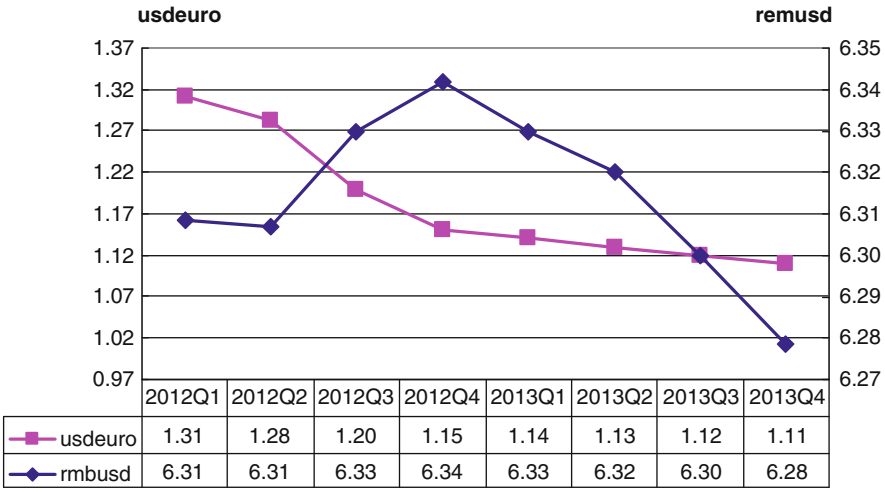
2.1.3 Growth Rate of the Broad Money Supply (M2)

The growth rate of the broad money supply (M2),[1] in the first half of 2012,is expected to grow at 13.8 and 14.2 % in the third and fourth quarter, respectively, and stay at the level of 14.3 % in 2013 (see Fig. 2.3).

2.1.4 Official Interest Rate of 1-Year Loans

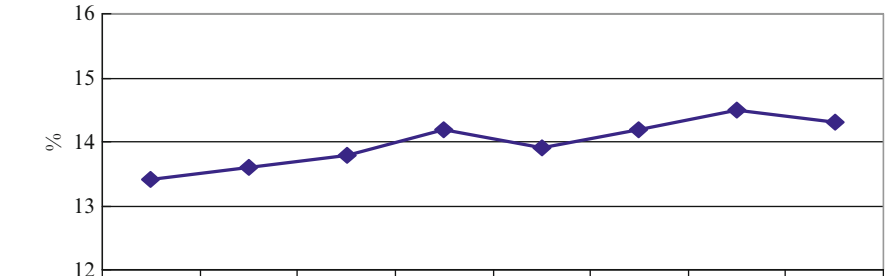
The interest rate of 1-year loans is expected to reach 5.75 % after a cut of 0.25 percentage point in the fourth quarter of 2012, and remains unchanged in 2013 (see Fig. 2.4).

[1] Data have been adjusted by the People's Bank of China in October 2011.



	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
usdeuro	1.31	1.28	1.20	1.15	1.14	1.13	1.12	1.11
rmbusd	6.31	6.31	6.33	6.34	6.33	6.32	6.30	6.28

Fig. 2.2 Assumptions of certain exchange rates for 2012–2013 (Sources: By the authors. Note: rmbusd refers to RMB/USD (*right hand axis*); usdeuro refers to EUR/USD (*left hand axis*))



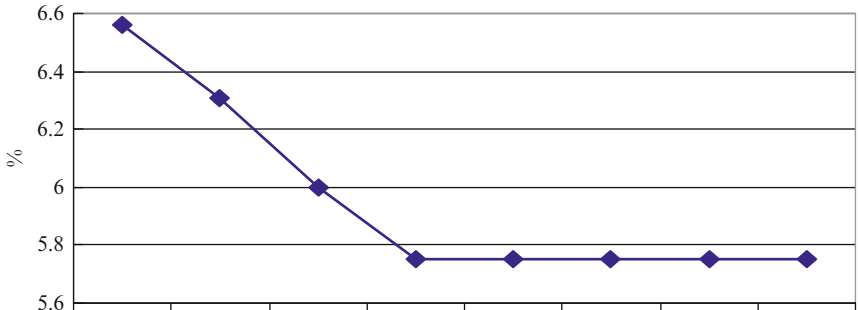
	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
M2	13.4	13.6	13.8	14.2	13.9	14.2	14.5	14.3

Fig. 2.3 Assumptions of trend of M2 growth rate (Sources: By the authors)

2.2 Forecast for China's Major Macroeconomic Indicators in 2012–2013

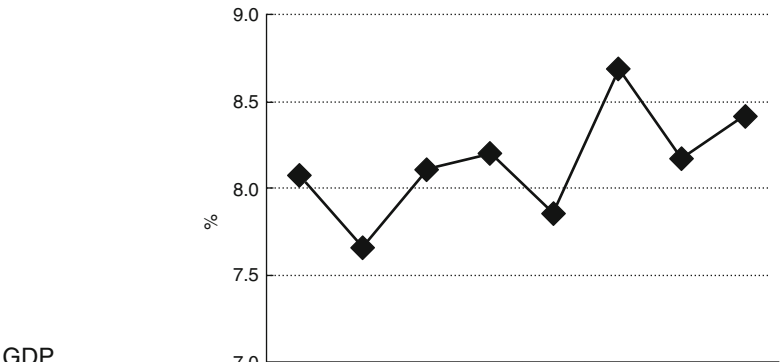
2.2.1 GDP Growth Rate

Based on the assumptions of exogenous variables made above, as a result of domestic and external factors, such as economic contraction in the euro area, China's GDP growth is forecast to decrease to only 8.01 % in 2012, and then rebound to 8.29 % in 2013. In terms of year-on-year quarterly growth rate (see Fig. 2.5), GDP is forecast to be



	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
RL	6.56	6.31	6	5.75	5.75	5.75	5.75	5.75

Fig. 2.4 Assumptions of trend of 1-year benchmark lending rate (Sources: Assumptions made by the Center for Macroeconomic Research (CMR-XMU))



	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
year-on-year growth rate	8.08	7.66	8.11	8.20	7.86	8.69	8.18	8.43

Fig. 2.5 Forecast results of GDP quarterly growth rate (quarterly year-on-year growth rate) (Sources: By the authors)

8.11 % and 8.20 % in the third and fourth quarter of 2012, respectively.[2] Forecast from CQMM suggests that: China's economy would maintain a moderate grow of above 8 % in the second half of the 2012, provided that the central bank would cut off the interest rate one more time, and keep the annually growth rate of M2 at 14 %, meanwhile, the central government would implement modest expansionary fiscal policy, in spite of less robust economic recovery in the U.S. and sever economic contraction in the euro area. In a word, China's economic growth rate would not decrease significantly.

[2]Note: Prediction are after seasonally adjusted.

2.2.2 Major Price Indices

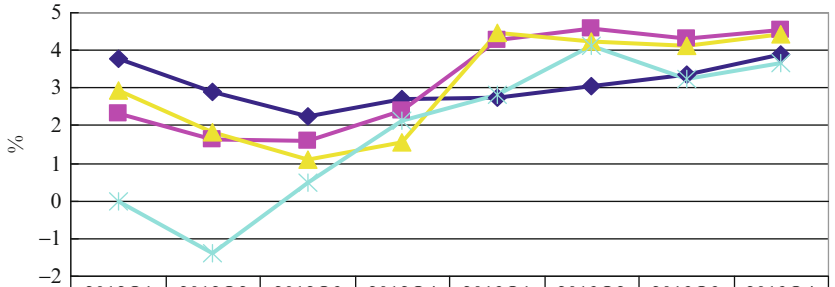
Due to sluggish external market demand and decelerated domestic economic growth, upward pressure on China's inflation rate would be released substantially.

First, CPI is expected to rise by only 2.9 % in 2012, a drop of 2.52 percentage points over last year, and then pick up to 3.27 % in 2013. In terms of year-on-year quarterly rates (see Fig. 2.6), by the third quarter of 2012, CPI is forecast to hit the bottom at 2.24 %; and then pick up gradually to 3.90 % at the end of 2013.

Second, PPI is forecast to fall to 0.3 % in 2012, and then go up to 3.45 % in 2013. To see year-on-year quarterly rates (see Fig. 2.6), PPI is likely to pick up to 0.48 % in the end of 2012, and then fluctuate within a small range and then finally rise to 3.66 % at the of 2013.

Third, the price index of investment in fixed assets is forecast to reach 1.98 % in 2012, a drop of 4.57 percentage points over the previous year, and then rises back to 3.27 % in 2013. In term of quarterly growth rate, it is forecast to decrease from 2.31 % in the first quarter of 2012 to 1.38 % in the third quarter, followed by an increase of 2.41 % in the fourth quarter compared with the same quarter of last year. It is expected to continue to rise and pick up to 4.55 % by the fourth quarter of 2013, which is likely to be a new peek (see Fig. 2.6).

Fourth, GDP deflator, it is expected to drop to 1.85 %, and then rises to 4.31 % in 2013. To see year-on-year quarterly rates, it is forecast to decrease from 2.95 % in the first quarter of 2012 to 1.09 % in the third quarter, and then, stay at the level of 1.56 % in the fourth quarter. It is expected to start going up, which would reach around 4.42 % by the fourth quarter of 2013 (see Fig. 2.6).



	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
CPI	3.77	2.88	2.24	2.72	2.75	3.05	3.35	3.90
P_I	2.31	1.62	1.58	2.41	4.27	4.58	4.29	4.55
P_GDP	2.95	1.84	1.09	1.56	4.45	4.25	4.12	4.42
PPI	−0.01	−1.40	0.48	2.13	2.81	4.12	3.23	3.66

Fig. 2.6 Forecasts of major price indices (annualized QoQ data) (Sources: By the authors. Note: CPI is Consumer Price Index, P_I denotes Price Index of Investment in Fixed Assets, P_GDP denotes GDP deflator, PPI denotes Producer Price Index)

In conclusion, if the euro area would not break down, and the situation in the Middle East would not deteriorate into a oil crisis, it is unlikely that the China's economy would suffer a severe slowdown, and inflation would unlikely rebound after cutting interest rates one more time in the fourth quarter of 2012.

2.2.3 Forecast for Growth Rates of Other Macroeconomic Indicators

2.2.3.1 Growth Rates of Imports, Exports and Foreign Exchange Reserve

Due to the euro area's economic setback through 2012, the value of exports, in term of the U.S. dollar at the current price, is forecast to rise 10.82 % in 2012, a decrease of 9.77 percentage points over the previous year. Meanwhile, the value of imports is forecast to decline to 5.76 % in 2012, a loss of 19.21 percentage points (see Table 2.1). In terms of the year-on-year quarterly growth rates of 2012, China's export is expected to grow 11.55 and 13.95 % in the third and fourth quarter, respectively. The import is expected to slow down to 6.63 % in the third quarter, a drop of 3.08 percentage points. As a result, China's trade surplus is expected to continue to increase, and foreign exchange reserve would remain at the growth rate of 3.98 % a drop of 17.45 % (see Fig. 2.7). By 2013, both China's imports and exports are expected to be on an upward path as global markets come back to stability. In 2013, exports, imports and foreign exchange reserve, is forecast to grow 15.93 %, 10.88 % and 10.75 %, respectively.

2.2.3.2 Growth Rates of Fixed Assets Investment

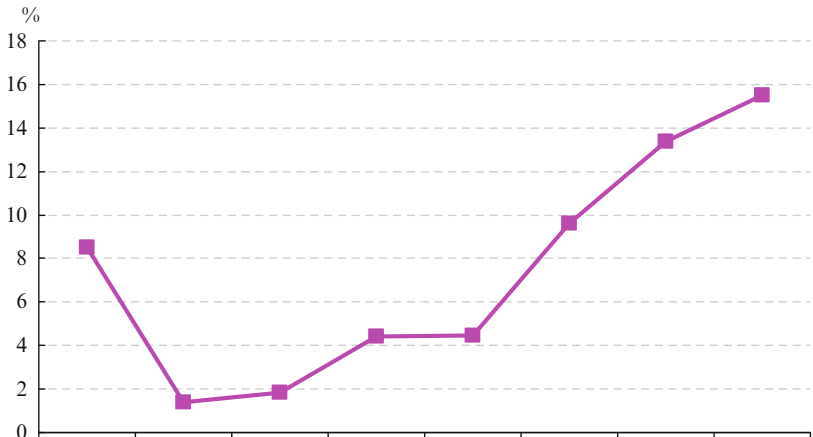
Though the external market is sluggish, China's investment is expected to grow as a result of loose monetary policy and moderately expansionary fiscal policy, but the growth rate of investment would decline sharply. The growth rate of gross fixed capital formation is forecast to grow at 8.97 % in 2012, a drop of 1.81 percentage points over last year. Investment in fixed assets in urban areas, is forecast to gain a growth rate of 20.4 %, shrinking by 5.41 percentage points from a year earlier. The reviving economy is forecast to boost investment demand in 2013. By that time, the growth rate of the gross fixed capital formation, is forecast to be 9.05, and 18.34 % for the urban investment in fixed assets (all variables are calculated at current price).

In terms of quarterly growth rates, after gross fixed capital formation, calculated at constant price, hit the bottom in the second quarter of 2012 with a rate of 6.95 %, it is forecast to bottom out and rise to 9.72 % in the third quarter, to pick up to 10.46 % in the fourth quarter. The growth rate of investment in fixed assets in urban area, is expected to hit the bottom in the third quarter of 2012, getting to 13.87 %, and then bottom out in the fourth quarter to 26.42 %. Due to base effects, the growth

Table 2.1 Forecast of growth rates of China's imports, exports and foreign exchange reserves in 2012–2013 (percent)

	Exports				Imports				Foreign exchange reserves
	Constant prices	Current prices	General trade (at current prices)	Processing trade (at current prices)	Constant prices	Current prices	General trade (at current prices)	Processing trade (at current prices)	Current price
Time	RMB	US dollars	US dollars	US dollars	RMB	US dollars	US dollars	US dollars	(US dollars 100 millions)
2012	**8.45**	**10.8**	**10.83**	**8.71**	**6.24**	**5.76**	**4.74**	**3.75**	**3.98**
Q1r	2.57	7.50	7.93	5.49	2.74	6.66	8.19	0.42	8.52
Q2 Quarter	6.43	10.10	11.28	6.56	7.57	6.85	7.97	0.61	1.41
Q3 Quarter	10.29	11.55	11.22	10.03	8.05	6.63	4.81	7.00	1.83
Q4 Quarter	14.53	13.95	12.66	12.78	6.63	3.08	−1.15	7.05	4.42
2013	**14.51**	**15.93**	**16.50**	**15.11**	**12.41**	**10.88**	**11.12**	**13.23**	**10.75**
1st Quarter	15.30	15.66	18.27	11.75	10.55	5.70	6.12	8.68	4.45
2nd Quarter	13.92	14.17	13.70	14.70	13.03	11.12	10.75	15.41	9.62
3rd Quarter	13.54	15.44	14.90	16.12	13.23	11.95	12.19	13.88	13.37
4th Quarter	15.31	18.34	19.19	17.67	12.75	14.57	15.17	14.86	15.51

Sources: By the authors



	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
FER	8.52	1.41	1.83	4.42	4.45	9.62	13.37	15.51

Fig. 2.7 Forecast of growth rates of foreign exchange reserves (annualized QoQ data) (Sources: Calculations of the Center for Macroeconomic Research (CMR-XMU))

	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
ti_c	8.69	6.95	9.72	10.46	6.50	11.07	9.23	9.42
fi_ur	20.62	21.01	13.87	26.42	14.62	16.96	20.38	21.01

Fig. 2.8 Forecast for growth rate of investment in fixed assets (annualized QoQ data) (Sources: By the authors. Note: ti_c denotes the growth rate of gross fixed capital formation in constant prices; fi_ur denotes the growth rate of urban investment in fixed assets at current price)

rate would be low at the first two quarters, and then climbs up in the second half of 2013 (see Fig. 2.8).[3]

In addition, total investment in fixed assets is forecast to grow at the rate of 20.13 %, a drop of 2.51 percentage points over previous year. In 2013, the growth rate would stay steady at 20.6 %. Classifying investment funds by sources, in 2012,

[3]Trends of the two indicators are different, due to a relatively low investment price index in the second half of 2012, and a relatively high one in the second half of 2013. The gross capital formation at constant prices is still likely to fall, when the urban investment in fixed assets, rise in the third quarter in 2013.

Table 2.2 Forecast of growth rates of investment in fixed assets by sources of funds in 2012–2013 (percent)

Time	From domestic loans	Self-raising funds	Other sources	Gross fixed capital investment
2012	17.67	23.02	10.12	20.13
1st Quarter	5.83	25.98	−3.84	17.35
2nd Quarter	6.47	20.93	5.48	17.01
3rd Quarter	19.52	18.24	13.48	16.21
4th Quarter	41.70	27.17	26.73	30.03
2013	24.96	18.62	29.08	20.60
1st Quarter	25.48	13.77	32.14	18.98
2nd Quarter	28.22	19.86	30.30	20.74
3rd Quarter	25.04	19.15	28.59	20.92
4th Quarter	21.65	21.32	25.92	21.57

Sources: By the authors
Note: Others = Gross fixed capital investment – (Budget + domestic Loans + Self-raising Funds + Foreign investment) at current price

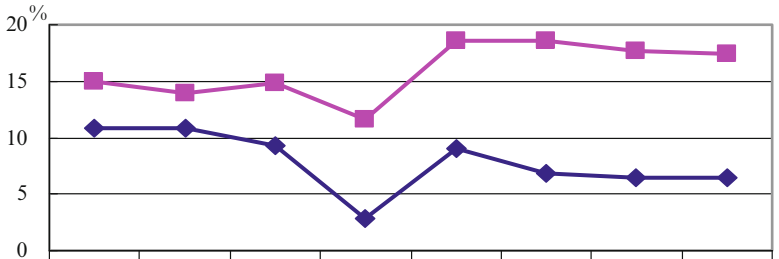
the growth rate of funds from domestic loans, influenced by the monetary policy, is expected to increase by 16.35 percentage points from a year earlier to reach 17.67 %, while, self-raising funds is expected to fall to 23.02 %, which would be a decrease of 9.5 percentage points from a year earlier. The growth rate of investment funded by other sources is forecast to be 10.12 %, decreasing by 2.2 percentage points year-on-year. The growth rate of investment funds both from domestic loans and other sources is forecast to get back on a sharp upturn through 2013 (see Table 2.2).

2.2.3.3 Growth Rates of Consumption

Based on CQMM, residential final consumption expenditure, is forecast to grow at 8.27 % in 2012, a drop of 0.88 percentage points over the previous year, and is forecast to drop to 7.18 % in 2013. Retail sales of consumption goods, would grow at 13.75 % in 2012, a fall of 5.19 percentage points, and would rebound to 18.05 % in 2013.

In terms of year-on-year quarterly growth rates, residential final consumption expenditure is forecast to grow at 9.26 and 2.87 % in the last two quarters of 2012. [4] The growth rates through 2013 is expected to stay around 6.7 %, and with some relatively mild changes. The growth rate of retail sales of consumption goods is forecast to be 14.79 and 11.6 % in the last quarters of 2012, respectively, and then to rise to 17.41 % in the fourth quarter of 2013 (see Fig. 2.9, all variables are calculated at constant price of 2011).

[4] The growth rate in the fourth quarter of 2012 is low due to a relatively high base in the last year.



	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4
con_d_c	10.82	10.82	9.26	2.87	9.01	6.87	6.44	6.51
ret ail	14.92	13.96	14.79	11.60	18.60	18.60	17.68	17.41

Fig. 2.9 Forecast of consumption growth rate (seasonally adjusted annual QoQ data) (Sources: By the authors. Note: CON_D_C denotes the growth rate of the residential final consumption expenditure at constant price; RETAIL denotes the growth rate of the retail sales of consumer goods at current price)

In conclusion, the research term suggests the following:

1. In the second half of 2012, due to the gloomy perspective of economic outlook in the euro area, the growth rate of China's imports and exports is expected to suffer significantly, which could put a downside pressure on the economy. However, if the interest rate would be cut off by 0.25 percentage point in the fourth quarter; meanwhile, if the growth rate of M2 would be kept at around 14 %, together with modestly expansionary fiscal policy, China's GDP is forecast to grow by 8.01 % in 2012. CPI is forecast to fall to a low level of 2.9 % in 2012. The economic growth is forecast to rise back to 8.29 %, a increase of 3.27 percentage points.
2. In the context of shrinking external demand, the growth rate of investment demand is expected to slow down considerably, but still at a relatively high level as a result of moderately loose monetary policy. In contrast, it is unlikely to significantly improve the slow growth trend of residential consumption. Therefore, final consumption expenditure as a share in GDP is expected to pick up, while gross fixed capital formation as a share in GDP is expected to decline. Nevertheless, residential consumption has been grown faster than GDP in the past 5 years, which continues to strengthen contribution of final consumption expenditure to GDP growth, especially when the growth rate slips down to its new low level of around 8 %. Therefore, it is necessary to boost residential consumption through improvement of people's wellbeing and promotion of economic structural adjustments. By doing so, China could switch its growth pattern away from an economy that heavily relies on investments and exports to one that more depends on domestic consumption and investments, as China enter a new development stage, at which the legend of two-digit growth will not longer come.

Based on forecast, the research team points out that, "stability in slowing down" would be the feature for the growth trend of in the China's economy in the next decade. Despite sever external economic situations, such as economic turmoil in the euro area as well as less robust economic recovery in the U.S., with moderately proactive macro control, which has been adopted since the first half of 2012, the China's economy could not suffer a sharp slump in the near future.

Chapter 3
Policy Simulation

Since the global financial crisis in 2008, the Chinese government has taken powerful anti-crisis measures. A "4 trillion Yuan stimulus package" was one of measures used to avoid the China's economy from plunging. After the China's economy picked up in the first quarter of 2010, the quarterly growth rate (cumulative year-on-year base) continued to decline as those anti-crisis measures faded out, more recently, as a result of high economic risks in the euro area and the U.S. (see Fig. 1.1). The growth rate of GDP in the second quarter of 2012 reached a new low level of 7.8 %. The perspective on the global economy is expected to be gloomy in short term. In the case where the euro area falls apart and turns into another deep recession, which would significantly undermine the U.S. economic recovery, how much would that affect the China's economy, and would the China's economy need a new stimulus package with massive investment expansion? Without answering these questions, the local governments have begun to call for and plan on some magnificent investment projects.

It is necessary to answer two questions before deciding whether to launch another massive investment stimulus plan.

1. Assuming that the euro area's economic turmoil turn into a severe recession, accordingly, slowing down the U.S. weak economic recovery, how much would that affect the China's economy? To what extent of the slowdown of the growth rate could be tolerated by the China's economy?
2. Assuming that it is necessary to launch a new massive investment stimulus plan, what should be its scale? And how much would that lift China's growth rate?

In order to answer the two questions, we analyze with two hypothetic scenarios.

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3.1 Scenario 1: More Severe Recession in the Euro Area

China's exports to the United State and the European account for more than 50 % of its total exports, though the share declined slightly in the past few years. Looking at the current economic situation in the euro area, an escalation of sovereign debt crisis associated with fiscal tightening, and high unemployment rates could make countries like Greece quit from the euro area, eventually leading the crisis to spread from the euro area periphery to the center, and to the whole euro area and also weakening the recovery of the U.S. economy. In this scenario, what would be the effects on China's economic growth?

This scenario assumes that the euro area will shrink by 1 % in 2012 as the sovereign debt crisis escalates a drop of 0.7 percentage point compared to the assumptions made in the baseline model in Sect. 2.1.1. For 2013, this scenario assumes that the growth rate of the euro area will contract by 3 %, which is 3.7 percentage points lower than the assumptions made in the baseline model. Accordingly, the growth rate of the U.S economy will drop to 1.0 % in 2012, a drop of 1 percentage point. For 2013, the U.S. economy is expected to grow only 0.6 %, 1.7 percentage points lower than the assumptions made in the baseline model. At the same time, the value of a Euro against the U.S. dollar, is expected to depreciate further to the level of 1.11, and then it maintains at 1.05 in 2013. The assumptions on the exchange rate of RMB against the U.S. dollar, as well as monetary policy are the same as those made in the baseline model.

Table 3.1 reports the simulation results based on CQMM:

1. The sovereign debt crisis in the euro area would cumber the China's growth rate of imports and exports. In 2012, the growth rate of China's export (calculated in U.S dollar at current price) is forecast to be only 6.42 %, 4.39 percentage points lower than that of the baseline model. For 2013, the growth rate is forecast to fall to 1.43 %, 14.5 percentage points lower than the predicted value in the baseline model. The import is forecast to grow at a rate of 3.94 % and 5.81 % in 2012 and 2013, respectively. The export is expected to grow at a rate of 4.33 % in 2012 and then turns to −38 % in 2013. Anyway, China could still maintain a trade surplus in 2013.
2. The setback in China's exports would further hamper its economic growth. GDP is forecast to grow at a rate of 7.71 % and 7.5 % in 2012 and 2013, respectively, 0.31 percentage point and 0.79 percentage point, respectively, lower than those of the baseline model.
3. A more severe recession in the euro area is expected to cool off China's inflation rate. In this scenario, CPI in 2012 is forecast to increase by 2.69 %, followed by a further decrease of 1.84 % in 2013. The price index of investment in fixed assets is expected to decline to 1.76 % and 2.86 % in 2012 and 2013. Similarly, GDP deflator would drop to 1.72 % and 3.17 %, respectively, in these 2 years. Therefore, compared to results of the baseline model, the price indices above would drop drastically.
4. To some extent, the growth rate of investment is expected to stay steady because a decrease in the price index of investment in fixed assets could stimulate investment. Owing to the sluggish demand, price index of investment in fixed assets is

Table 3.1 Impacts of the euro area's further recession on the China's economy (seasonally adjusted) (percent)

	GDP	Domestic consumption	Gross fixed capital formation	Export	Import	CPI	Price index of investment in fixed assets	GDP deflator
	(GDP)	At constant prices	At constant prices	In U.S. dollars at current price	In U.S. dollars at current price	(CPI)	(P_I)	(P_GDP)
2012Q1	8.08	10.82	8.69	7.50	6.66	3.77	2.31	2.95
2012Q2	7.66	10.82	6.95	10.10	6.85	2.88	1.62	1.84
2012Q3	7.48	9.23	9.84	3.41	3.19	1.95	1.30	0.97
2012Q4	7.63	2.84	10.84	4.80	−0.56	2.19	1.83	1.18
2013Q1	6.99	8.97	7.15	1.89	0.41	1.83	3.27	3.78
2013Q2	7.65	6.83	12.14	−2.89	4.32	1.70	3.10	3.21
2013Q3	7.55	6.43	10.62	2.92	8.31	1.76	2.53	2.79
2013Q4	7.78	6.55	11.02	4.00	10.21	2.06	2.55	2.91
2012	**7.71**	**8.26**	**9.10**	**6.42**	**3.94**	**2.69**	**1.76**	**1.72**
Gap with the baseline projections	−0.31	−0.01	0.13	−4.39	−1.82	−0.21	−0.22	−0.13
2013	**7.50**	**7.17**	**10.24**	**1.43**	**5.81**	**1.84**	**2.86**	**3.17**
Gap with the basis prediction	−0.79	−0.01	1.19	−14.50	−5.07	−1.43	−1.57	−1.14

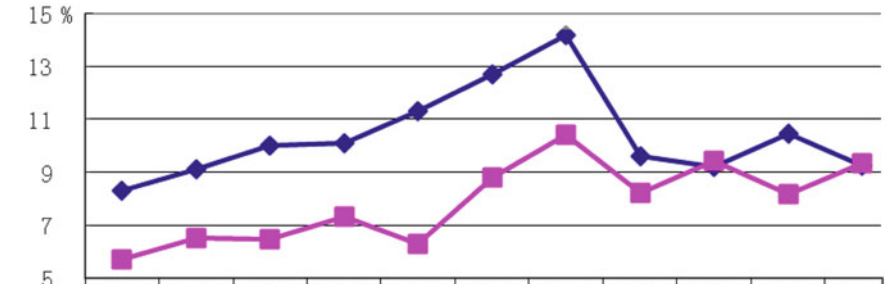
Sources: By the authors

expected to drop sharply, lowering the investment cost. As a result, the investment demand is forecast to climb up to. It is expected that gross fixed capital formation could grow at rates of 9.1 % and 10.24 % in 2012 and 2013, respectively; the former is an upward revision of 0.13 %, while the latter is 1.19 %, compared with the baseline model. This could help to offset the negative influence from the sluggish global market, and consequently, to stabilize the GDP growth.

In conclusion, the simulation in the first scenario indicate that impact of a sluggish global markets on China's economic growth rate is limited. The main reasons for this conclusion are as follows:

(a) Residential consumption expenditure has been growing at a relatively stable rate, which is expected to play an important role in domestic demand, and gradually to function as an economic stabilizer (see Fig. 3.1).

Meantime, as a result of constant increase of residential income, residential consumption began to play an important role in economic growth. The marginal growth rate of residential final consumption expenditure to GDP, in the recent 5 year, showed a notably upward trend (see Fig. 3.1, Table 3.2), which was on



	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
gdp_c	8.3	9.1	10.0	10.1	11.3	12.7	14.2	9.6	9.2	10.4	9.2
con d c	5.7	6.5	6.5	7.3	6.3	8.8	10.4	8.2	9.4	8.2	9.3

Fig. 3.1 Growth rates of GDP and residential final consumption expenditure (Sources: By the authors)

average 71.81 % during the period from 2001 to 2006; and 88.15 % during the period from 2007 to 2011. Though the growth rate of residential final consumption expenditure has been lower than the growth rate of GDP, resulting in a declining trend of residential consumption as a share in GDP, it is definitely a noteworthy and encouraging change that the marginal growth rate of residential final consumption expenditure to GDP is rising. Of course, economic stabilization and further development must depend on a further policy adjustments, institutional reform, and transition of development pattern as well.

(b) Price indices of investment are expected to decline, due to the weakened external demand, hence expanding the investment demand to some degree.

(c) Moderately expansionary fiscal and monetary policies would ease the downside pressure on investment, employment, as well as residential income, stabilizing the growth rate of residential real income, and eventually leading to a steady growth of residential consumption and domestic investment.

Consequently, negative impacts from sluggish external markets are expected to be offset, to some extent, by robust growth of domestic demand, which enables the economic growth to stay at the level of 7.5 %.

3.2 Scenario 2: Effects of the "2-trillion-Yuan stimulus Package" on Growth

With the growth rate on a downward trend, especially at a level of below 8 % in the second quarter of 2012, the call for a new massive investment stimulus policy is escalated. Since May, 2012, the National Development and Reform Commission (NDRC) has approved some magnificent investment projects. The need for "4 trillion Yuan stimulus package" seems quite reasonable again owing to the shrinking external demand and investment contraction in the China's economy.

Table 3.2 Change of the marginal growth rate of residential final consumption expenditure to GDP (2001–2011) (percent)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
The ratio of growth rate of residential final consumption expenditure to growth rate of GDP	68.67	71.14	65.00	72.28	55.75	69.29	73.24	85.42	102.17	78.85	101.09

Sources: Calculated from the data in Fig. 3.1

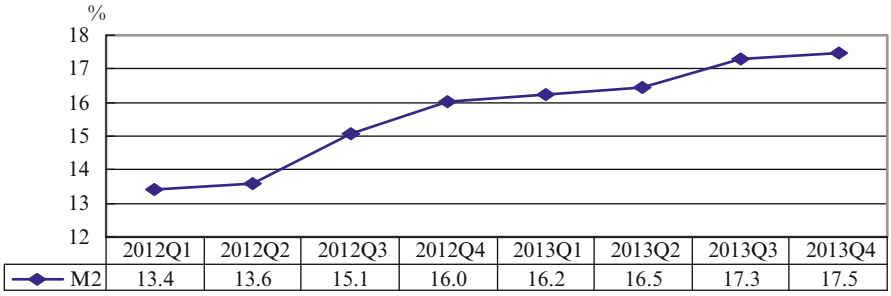


Fig. 3.2 Assumptions of increases in the growth rate of M2 (Sources: By the authors)

Assuming that it is necessary to launch a new massive investment stimulus package, how much in terms of scale should it be? And, how much would that lift China's growth rate? Here, we simulate the effects of launching a new massive investment stimulus policy, a equivalence of "two trillion Yuan stimulus package" using CQMM.

Under the same assumption on the EU and the U.S. economic outlook as in the baseline model, this scenario assumes that money and credit are expected to expand as a result of the launching of the "two trillion Yuan stimulus package", and the growth rates of M2 for 2012 and 2013 are expected to rise by some 3 or 4 percentage points, compared with the baseline model (see Fig. 3.2).

Table 3.3 reports the simulation results based on CQMM with the following suggestions:

1. The launching of the "two trillion Yuan stimulus package" is expected to boost the growth rate of GDP to 8.25 % in 2012, an upward revision of 0.24 percentage points compared with the baseline model. For 2013, the growth rate is forecast to rise further to 8.86 %, an upward revision of 0.55 percentage point, compared with the baseline model. It implies that, the proactive fiscal policy, mainly used for expansion of infrastructure investment, has limited effects on growth.
2. The launching of the "two trillion Yuan stimulus package" is expected to boost investment demand. Gross fixed capital formation is forecast to grow at a rate of 9.58 % in 2012, and 10.67 % in 2013, an upward revision of 0.61 and 1.62 percentage points, respectively, compared with the baseline model.
3. The launching of the "two trillion Yuan stimulus package" is expected to expand, to a certain degree, demand for imports. Import (calculated in U.S. dollar at current price) is forecast to grow at 5.86 % and 11.03 % in 2012 and 2013, respectively, an upward revision of 0.1 and 0.16 percentage point, compared with the baseline model. On the other hand, the growth rate of export is forecast to be 10.69 % and 14.98 %, respectively, as influenced by the weakened external market, which are a slight downward revision, relatively to the baseline model.
4. The launching of the "two trillion Yuan stimulus package" is expected to raise the inflation rate substantially. It is forecast that, CPI in 2012 would climb up to 3.05 %.and then goes up to 4.29 % in 2013, an upward revision of 0.15 and 1.02 percentage points, respectively, compared to the results in the baseline model. In addition, the price index of investment in fixed assets (P_I) and the GDP deflator are expected to rise.

Table 3.3 Influence on China's macro economy in 2012–2013, of "two trillion Yuan stimulus package" (seasonally adjusted) (percent)

	GDP	Domestic consumption	Gross fixed capital formation	Export	Import	CPI	Price index of investment in fixed assets	GDP deflator
	(GDP)	At constant prices	At constants prices	In U.S. dollars at current price	In U.S. dollars at current price	(CPI)	(P_I)	(P_GDP)
2012Q1	8.08	10.82	8.69	7.50	6.66	3.77	2.31	2.95
2012Q2	7.66	10.82	6.95	10.10	6.85	2.88	1.62	1.84
2012Q3	8.50	9.27	10.72	11.40	6.83	2.42	1.76	1.17
2012Q4	8.74	2.90	11.87	13.58	3.28	3.15	2.85	1.83
2013Q1	8.47	9.04	8.09	15.04	5.90	3.44	5.03	4.96
2013Q2	9.18	6.88	12.49	13.37	11.23	3.95	5.58	4.97
2013Q3	8.73	6.44	10.85	14.41	12.10	4.47	5.53	5.03
2013Q4	9.03	6.50	11.24	17.03	14.72	5.27	6.05	5.53
2012	**8.25**	**8.28**	**9.58**	**10.69**	**5.86**	**3.05**	**2.14**	**1.94**
Gap with the baseline projects	0.24	0.01	0.61	–0.13	0.10	0.15	0.16	0.09
2013	**8.86**	**7.19**	**10.67**	**14.98**	**11.03**	**4.29**	**5.55**	**5.13**
Gap with the baseline prediction	0.56	0.01	1.62	–0.95	0.16	1.02	1.13	0.82

Sources: By the authors

5. The launching of the "two trillion Yuan stimulus package" is expected to enhance the imbalance of economic structure. Compared with the baseline model, the share of gross fixed capital formation in GDP is forecast to rise by 0.1 percentage point in 2012 and 0.6 percentage point in 2013, while the share of residential final consumption expenditure in GDP is forecast to decrease by 0.1 percentage point in 2012 and 0.2 percentage point in 2013 (see Table 3.4).[1] It indicates that, although the influence on economic structure is insignificant, compared with the simulation results in the baseline model, it would worsen the imbalance of the economic structure in trend.

The simulation results reveal that, in the context of the current external economic environment (assumed as in the baseline model), launching the "two trillion Yuan stimulus package" could, in a manner, raise the growth rate of GDP. However, the effect is limited. What's more, the corresponding expansion of credit and money would raise the inflation rate considerably, and there exists risks of worsening the existent imbalance in the economic structure.

[1]The proportion of the residential final consumption expenditure in GDP is only 36.9 %, which is already quite low, so there is little room for it to drop any further.

Table 3.4 Influence on the economic structure after launching the "two trillion Yuan stimulus package" (calculated by constant prices) (percent)

	Simulation results			The baseline model		
	The share of residential final consumption expenditure in GDP	The proportion of gross fixed capital formation in GDP	The proportion of net exports in GDP	The proportion of residential final consumption expenditure in GDP	The proportion of gross fixed capital formation in GDP	The proportion of net exports in GDP
2010	37.0	43.9	3.8	37.0	43.9	3.8
2011	36.9	44.5	3.2	36.9	44.5	3.2
2012	36.9	45.0	3.4	37.0	44.9	3.4
2013	36.4	45.8	3.1	36.6	45.2	3.3

Sources: By the authors

Note: Inventories is not included in gross fixed capital formation, and services are not included in net exports

Chapter 4
Policy Implication and Recommendations

How to carry out macroeconomic policies in the next 2 years has attracted a lot of attention because the uncertain external economic outlook: to maintain a high growth rate, by continuing the traditional development pattern and go all out or to achieving steady growth by implementing a mild strength expansionary control policy, gradually shifting policy and then focusing on deepening reform and structural adjustments?

The simulated results of the three different scenarios with different policies are reported in Table 4.1:

Table 4.1 indicates that:

First, the lowest growth rate of GDP would be 7.5 %, in the worst case that the euro area's economic turmoil turns into a recession in 2013. It means that the trend of "stability in slowing down" has being established in China's economic growth. Although the impact of recession in the euro area will put downside pressure on China's economic growth in the short term, a modest macro-control expansionary policy could prevent China's economy from further declining. Otherwise, even carrying out the "2 trillion Yuan" massive investment stimulus policy to improve growth, the economic growth could only be moved up to the level of 8.25 % and 8.86 % 2012 and 2013 respectively, Therefore the stimulus package has neglectable positive impact.

Secondly, on the other way, the cost of such a stimulus policy is very expensive. It includes: newly increased 2 trillion Yuan investment, and thus increasing burden of local governments' debt in the next 2 years; 3.05 %–4.29 % of inflation rate (CPI); a further rise in the share of fixed asset investment in GDP, a further decline in the share of residential consumption in GDP, and in addition to further distortion in the national economy structure; further rise in the proportion of resources that controlled by local governments and central government, and then the more governmental interference to the market economy; the delay of the process of transforming economic development mode once again, and so on.

Thirdly, China has maintained a high growth rate of over 10 % since 2001. The cost to achieve this high growth is also high. At least in its later period, the negative

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Table 4.1 Prediction and simulation of different trends of China's economic growth in 2012–2013

Scenario assumption	Year	Gross domestic product (GDP)	Total domestic consumption Comparable price	Gross fixed capital formation Comparable price	Export US dollar (current price)	Import US dollar (current price)	Consumer price index (CPI)	Fixed assets investment price index (P_I)	GDP deflator index (P_GDP)
Base prediction	2012	8.01	8.27	8.97	10.82	5.76	2.9	1.98	1.85
	2013	8.3	7.18	9.05	15.93	10.87	3.27	4.42	4.31
Euro area economy further deteriorated	2012	7.71	8.26	9.1	6.42	3.94	2.69	1.76	1.72
	Gap with the basis prediction	**−0.31**	**−0.01**	**0.13**	**−4.39**	**−1.82**	**−0.21**	**−0.22**	**−0.13**
	2013	7.5	7.17	10.24	1.43	5.81	1.84	2.86	3.17
	Gap with the basis prediction	**−0.79**	**−0.01**	**1.19**	**−14.5**	**−5.07**	**−1.43**	**−1.57**	**−1.14**
"2 trillion yuan" massive fiscal spending plan	2012	8.25	8.28	9.58	10.69	5.86	3.05	2.14	1.94
	Gap with the basis prediction	**0.24**	**0.01**	**0.61**	**−0.13**	**0.1**	**0.15**	**0.16**	**0.09**
	2013	8.86	7.19	10.67	14.98	11.03	4.29	5.55	5.13
	Gap with the basis prediction	**0.56**	**0.01**	**1.62**	**−0.95**	**0.16**	**1.02**	**1.13**	**0.82**

Sources: Calculation of the Center for Macroeconomic Research (CMR-XMU)

respects include: resource preserving, environment protecting and income share of working class. And the cumulative of these negative effects leaded to the urgency of transforming economic development mode. Transforming development pattern means the requirement of reducing the high economic growth rate appropriately to exchange for effective, resource, environmental protection, for technical progress, industrial restructuring, and for the adjustment of national income and residential income distribution structure, to achieve inclusive growth.

Fourth, the economic growth rate about 8 % should be considered as a normal or potential growth rate after China entered a new development stage with second highest growth rate. In general, when an economy entered into a new development stage that it's economic growth mainly depend on domestic demand, it was very difficult to maintain a growth rate over 10 % for a long period. However, under the current circumstance that external economy continues to deteriorate, China economy is able to hold the economic growth rate of about 7.5 % or above. This indicates that even in so bad external surroundings, China also can generally maintain an economic growth rate of about 8 % primarily relying on domestic consumption and investment demand

By assuming that 8 % is the normal or potential growth rate after China entered a new development stage with the second highest growth rate, we conclude:

In current macroeconomic situation, China should not launch a new massive fiscal spending stimulus plan. Because the previous stimulus plan, launched in 2009, had raised series of issues to be solved, though it supported the economic growth. These issues are: further strengthening the capacity of the government controlling resources and crowding out the share of resources controlled by market economy, exacerbating the imbalance of national economic structure, improving governmental debt burden, boosting inflation, and so on. Among these problems, what we must pay special attention is the soaring debt of local governments.

Up to the end of 2010, governmental debt balance was approximately 17.47 trillion Yuan, among which central government debt balance was 6.75 trillion Yuan, an increase of 1.43 trillion Yuan, 26.88 % compared to the end of 2008; and local government debt balance even reached to 10.72 trillion Yuan, which was 5.15 trillion Yuan higher than the end of 2008.[1] Affected by this, the debt balance ratio of local governments to central government had jumped from 1.04 in 2008 to 1.59 in 2010.

The rapid increase of governmental debt will lead to many adverse effects.

First, large scale debt will offset the effect of macroeconomic policies. In 2010, the proportion of governmental debt to GDP is about 43.5 %, which was low compared with developed economies such as Euro area, the United States and Japan.[2] Comparison 34.7 % in 2 years ago, the proportion had rapidly increased 8.8 percentage points. Meanwhile, from debt-service payment perspective, central government should pay about 1.35 trillion Yuan in 2011, which accounted for more

[1] Quote from No. 35 announcement that published by the National Audit Office of P.R.C in 2011 and CEIC database.

[2] The proportion of public debt to GDP is about 62.2 % in U.S. in 2010; Euro area is nearly 85 % averagely, in which Greece, Italy and Belgium are more than 100 %; Japan is more than 200 %.

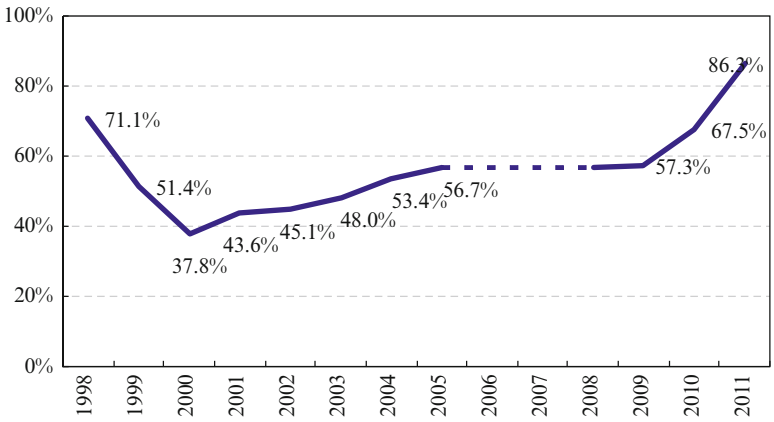

Fig. 4.1 Trend change of the ratio of debt-service payment to the income from issuing bonds (The data of 2006–2008 is missing. We show them with *dotted line*. Sources: CEIC)

than 10 % of total fiscal expenditure, only next to the expenditure scale of education, agriculture, forestry and water conservancy as well as social security; and the ratio of debt-service payment to the income from issuing bonds was up to a new high record of 86.3 % (Fig. 4.1). This means only 13.7 % of the income could be spent on other expenditures. Therefore, the increase of debt-service payment will partially offset funds obtained through debt financing, which will greatly compress the operating space of future macroeconomic policies.

Secondly, the rapid rise of debt will significantly increase fiscal burden of local government, and increase short-term debt payment risk. In 2011, the debt at maturity of local government is up to 2.62 trillion Yuan, which comprises about half of local fiscal income. The scale of maturity debt will be slightly less in 2012 and 2013, but still more than one trillion Yuan, which are 1.84 and 1.22 trillion Yuan respectively. In the context of a significant slowdown in fiscal revenue growth in the next 2 years, it will bring great financial pressures to local government. According to No. 35 announcement that published by the National Audit Office of P.R.C in 2011, by the end of 2010, a total of 78 municipal and 99 county governments bear a high repayment obligation debt ratio over 100 %, which accounted for 19.9 and 3.56 % of the total numbers of the two level governments. Due to insolvency, some local governments had to borrow new debts to roll over old debts, or even had overdue payment.

Thirdly, in addition to micro risks of short-term debt payment pressure, the rapid increase of government debt will also cause macro risks. First of all, residents are the ultimate bearer of government debt. Therefore, the augment of the size of the debt will promote future tax level, reduce the actual income of residents, decrease the willing of consumption, and then further distort the aggregate demand structure, which will neutralize the effect of the expansionary policies in turn; Second, when the normal tax growth cannot afford the scheduled debt service payment, land finance has become the most important and dependable source of revenue to local

governments. Therefore, the high scale of the debt will not be conducive to the adjustment of fiscal system, and it also can be difficult to curb the inner impulse of local government to relax house purchase quota policies.

In the context of large size of government debt, shrinking space to issue more bonds, high overdue risks of debt service payment, and related macro risks, the re-start of massive fiscal spending stimulus plan will undoubtedly increase government debt burden, and will not be conducive to the structural adjustment of aggregate demand, the reform of fiscal system and the implementation of real estate market regulation and control policies. Especially, when external economic environment have no significant change, the pull effect to marginal economic growth of such a high policy cost of re-start massive fiscal spending stimulus plan is very limited. It is unprofitable and harmful, either from policy possibility, or from necessity.

Therefore, the current macroeconomic policies should be located at: a fine-tuning of moderately expansionary policy, which aims to stabilize the growth rate around 8 %, and at the same time, gradually veering the policy priorities to deepen institutional reform and structural adjustment. While maintaining a appropriate growth rate around 8 %, China has to gradually remove the significant structural imbalance and institutional barriers, which hinder and constraint the development of our long-term potential growth, and accelerate the transformation of economic development mode during the "Twelfth Five-Year Plan" by further reform and structural adjustment.

China must focus on improving the efficiency of resource use and economic growth; on changing the structure of income distribution; on restricting governments' power; on reducing tax burden and regulating the proportion of governmental revenue in GDP; on the better using of fiscal revenue to social welfare spending; on eliminating monopoly and narrowing residential income gap, to create the conditions for entering to a new development stage that mainly depend on domestic demand. The research team believes that an healthy economy, should improve social and economic structure, should be efficient and inclusive. In one word, China should pay more efforts on improvement of wellbeing of people with social progress, even growth rate is slightly lower than previous years.

Chapter 5
Comments and Discussions

5.1 Professor Shucheng Liu, Academician with Chinese Academy of Social Sciences

It is an outstanding report on macroeconomic forecasting and analysis that has been done very meticulously and seriously, and its policy suggestion is also feasible. I basically agree with the basic conclusions of the report and analysis.

The issues what I want to discuss are:

1. Whether the current economic growth rate is below the potential growth rate? I think the potential economic growth rate still remains in 8 %–9 %. Therefore, the growth rate in the first half of the year is still below the potential growth rate, which caused the difficulties of the enterprises, the decline in the growth rate of fiscal revenue and the problems of employment.
2. Is the decline of potential growth rate a mutational process or a sequential process? I think it will be a sequential process dropped from 10 %. It will maintain in 8 %–9 % from 2013 to 2017, and then down. The role of consumption is on the increase, but whether it is a trend or cyclical growth? I think it is still a cyclical increase.
3. when the potential economic growth rate moves down, the economic growth rate will be high sometimes and low sometimes. I agree with the forecast of the report, the economic growth rate in 2013 may be slightly higher than 2012. This shows that the economic growth of China will present as the shape of zigzag, which may be high 1 or 2 years and low 1 or 2 years.
4. the problem of the demand structure. We should rely on consumption in long run. Urbanization will become the breakthrough of economic growth in future, and it is also a key factor to maintain growth. In the process of urbanization, both investment and consumption will grow, but we merely improve the investment rate at present. Therefore, in the next period, we still need to rely on the investment, but what to be invested, by who, how to improve the efficiency of investment etc., these issues need to be further discussed.

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5.2 Professor Yansheng Zhang, Secretary-General of the Academic Committee of the National Development and Reform Commission

The main views of the report are quite distinctive. The report is very well, so I have no different opinions. Today what I want to talk about is the significance of the GDP growth rate below 8 % in the second quarter of this year.

As the growth rate goes below 8 %, there are two choices provided to China now. One is to stimulate economic growth and continue to chase high growth rate. But whether it will lead us to reach the upper bound of growth in next 5 years, and then the potential economic growth rate make a steep drop while the economy of the United States, Japan and Europe may significantly rise and quickly pull a larger gap with China? The other is to promote the structural adjustment and institutional transformation which is shackling the China's long-term growth potential capacity. In my opinion, the latter will make the economic growth rate remain around 8 % in 5 years, but the growth potential of China economy can continue to sparkle.

This year, the total number of China's enterprises in the world's Fortune 500 companies exceeds Japan. But almost all of them are traditional industries, which are large but not strong enough. And now, the enterprises are facing with the lack of orders, workers and technologies. In this context, it's useless to these problems if we continue raising the export tax rebate rate and speeding up the process of tax rebate rate. It's not a gross problem. It's a structural and institutional problem to a large extent.

Is the growth rate below 8 % a short-term or long-term phenomenon? If we believe that it's a short-term case, the response strategy of enterprises should be short-term. Then it may ignore the urgency of long-term transformation, which will gradually and finally lead to serious bad results. Conversely, if we think what China need now is a transformation revolution, called creative destruction, then to strengthen the adjustment will win a long-term growth potential.

Now, it's the crucial stage to the transformation of real economy. Government should timely push-off the supply management policies. In order to maintain a long-term growth rate of 7 %, we need a large adjustment in supply side, including large-scale tax cuts that make enterprises adjust easily, significantly reduce of government intervention in the economy, and the need of joint R&D among enterprises, universities and research institutes; among large, medium and small enterprises; among domestic and foreign; among military and civilian, to overcome the plight of technological transformation. These are very urgent.

5.3 Professor Liqun Zhang, Development Research Center of the State Council Researcher

The report provides some important conclusions and judgments. It is very helpful for us to understand the current situation. My basic opinion is that China's economy is at an important transition period now, and it may result in the decline of potential

economic growth rate of China temporarily. Macroeconomic policies should strive to prevent the economic growth decline sharply. The aim of steady growth, which is the most important task, should be maintained for a long time, so as to create the necessary environment and produce the reverse pressure for economic transformation.

The importance for economic transformation of China mainly lie in following: First, the need of market demand change. The high economic growth rate of China since 2002, completely depend on the vigorous domestic and foreign demand. But from the year of 2008 to 2011, the annual growth rate of China's exports had dropped to 9.9 %. The external market environment that the labor-intensive products from China has occurred a profound change. Second, the sustained and rapid growth of automotive and housing market due to the structure upgrade of domestic consumption. With rapid growth of civilian vehicles in the past years, and the improvement of traffic, the demand growth will be turned from quickly to steadily; the speculative and investment demand of housing in the real estate market, are very harmful to the development of real estate industry and the coordination to the income distribution. Since the system construction has speed up and been adopted, the investment role of housing will disappear basically. In addition, with the excess capacity of production, the high growth rate of investment based on capacity expansion is beginning to slowdown. The change of growth rate of "troika", due to the temporary major factor, may significantly affect the potential growth rate of China.

In addition, the change of factor cost. The rapid expansionary speed of enterprises depended on high input, high consumption, high pollution, and low efficiency, which is low factor cost in the past. In recent years, the factor cost had being change. Because of rise of cost, the enterprises must improve technological competitiveness, and make an effort to improve the capacity of R&D and brand competitiveness. The change of factor cost also made the expansion capacity of enterprises decline. So changes in market supply and demand and factor cost, decide the change of economic development mode, and the transformation and upgrade of enterprises also cannot be prevented. Therefore, the temporary decline of potential growth rate is inevitable.

5.4 Professor Ruilong Yang, President of School of Economic Renmin University of China

Since 2011, China's economic growth rate has been declining, and surprisingly fallen to below 8 % in the second quarter of 2012, the situation is no better than that in 2008. Several characteristics in this economic downturn are as below: (1) external factors have played an important role in the economic slump, especially the sovereign debt crisis in the euro area, leading the growth rate of China's import and export to go down. (2) Previous stimulus plan has caused a decrease in the government investment. On the other side, bubbles of asset prices have started to shrink, resulting from the "new regulations in the real estate purchase and loans policy".

What's more, by de-leverage and de-stocking, factors bringing down the economy have turned from exogenous to endogenous. (3) China's potential growth rate has taken on a stepped falling, and started to enter a new period of second-high economic growth rate due to decays of traditional advantages, such as marketing bonus, globalized bonus, traditional industrialization, as well as the high saving rate, and the new growth advantages are yet to develop. (4) Declining in the confidence of investment and consumption is triggered by pessimism.

I have to admit that, the high economic growth rate has brought lots of benefits to China. However, in the established development mode and economic mechanism, China is over-dependent of high economic growth, which I may call "dependency on high economic growth". In this circumstance, however, once the economic growth rate goes down, the unemployment rate would raise, hence a plunge in the local finance revenue, and eventually cause many social issues.

It is usually not a problem that, China's economy is expected to rebound in a short term, as the economic policy is improving. But you should not place too much hope on the revival, since the measures for boosting the economic are still severely limited. At the same time, the external demand is weak, and the consumption is hardly to grow significantly in a short run without an increase of income, therefore the only effective measure may be the investment. Moreover, at present, there is a banking credit crunch towards private enterprises and although, investment in the real estate would be spurred through loosening up the relevant policies, it would trigger retaliatory price rise. Hence, the optimal measure would be the government investment. And so long as the fixed capital investment gain increases, the economic growth rate would bottom out.

Stabilizing the investment is still the core in stabilizing China's economic growth, which is mainly investment of government, including local governments. However, government investment would bring about a series of issues, provided there exists no corresponding structural adjustment and system reform. The fundamental way out for preventing another economic slip remains further deepening reform. For example, when talking about stabilizing investment, we mean, why not open up some relevant fields in the monopoly industries and transit benefits to residential enterprises? On the other hand, transformation of development mode, together with reforming the income distribution system, would allow a raise in the labor income share. Meantime, it is vital to reform the financial system, and improve the price system through further opening up factor markets as well.

5.5 Professor Yunzhong Liu, Researcher of Development Research Center of the State Council

The report from Xiamen University and the speeches the previous experts made indicates that, we almost agree on the current economic situation as well as the medium-and-long-term growth trend. I agree the conclusions resulting from the policy simulation in the report, including some policy proposals.

First of all, I would like to talk about my understanding towards the theme. As a matter of fact, I believe, the theme of this conference not only fits in with the key issues China's economic development faces, but also goes to the core of macro economy. Instead of splitting the short term economic fluctuation from the long term economic growth, it integrates the two in the research. In policy, by doing this, it could prevent a contradiction between short-term policy effects and long-term growth. In doctrine, it is part of Schumpeter's theory framework, making it possible to analyze the influence of short-term monetary policy on innovation investment, and furnishes a better explanation of economic growth and fluctuation.

It's really a great pleasure to be here, to recommend three recent relevant researches from our center. The first one is named "China's economy in 2030", done by Professor Shantong Li in 2009, and its outcome has been published by Economic Science Press in 2010. The second one is concerned with "middle-income trap", done by the vice director of the center, Shijin Liu, and the finding has come off the press in 2011. The third one is in regard to "China 2030", a cooperative research by the Development Center and the World Bank. Actually, if we have a careful look at the conclusions in the three researches, we will find that, for many opinions, the economists have almost reached an agreement.

Back to the conference agenda, I believe it would be no problems for China to meet its economic growth target in the short term. However, for structural reform, there are several aspects needed to be considered: (1) Urbanization. The period, with the rapidest growth in China's urbanization, has already passed. So, it is necessary for us to think about the policies and measures to further support urbanization. (2) The relevant land system reform, including the reforms of land requisition mode and scope. (3) Local government. How to check on the debt capacity of local governments? How to restrain the behaviors of local governments to make investment and financing be more transparent? (4) The reform of capital market. More and more investment and financing activities will be run via capital market; therefore, more drastic supervision is needed, especially the behaviors of the financing body. And many reforms concerning this aspect should be accelerated.

I hope issues as below would be considered in the modification of the report: (1) Predictive data, especially consistency of the internal logic in the predictive data. (2) Change of the proportions of short-term loans and long-term loans. Which one is the normality? (3) Whether we can use the model to simulate the difference between cutting interest rate and lowering the deposit reserve ratio? (4) Whether we can simulate the policy implication of structural tax reduction?

5.6 Professor Luolin Wang, Ad Hoc Consultant of Chinese Academy of Social Sciences

The report is concise, and its prominent merit is fully considering both the subjective and objective factors of the economic development trend. From the aspect of subjective factor, it has taken the fact that China's economy is dominated by the

government into consideration, as well as simulated the policy implications of the "two trillion Yuan stimulus package", which is a feature of this report, and so on. However, since the conference aims at offering comments, I would like to put forward a piece of advice on the report.

My advice contains the followings: First of all, what on earth cause the economic downturn in the first half of the year? There are two factors included in the report, one is external demand, and the other one is the real estate market. Nevertheless, is it possible that, there are others more fundamental or deep-seated factor? And as to external and domestic demand, which one is principal? It seems that, the key factor is the influences of the global economic situation, however, when you have an in-depth look, it is our real economy, especially an explosion of the issue, for several years, of the excess capacity in the manufacturing industry, that cumbers our economy. Secondly, I want to talk about the growth trend of the second half of 2012 and the next year. I assent to the forecast that, it would be no problem for China's economy to grow at a rate of 8 % in this year, and at a higher rate in the next, since there are a number of subjective factors sustaining the economy, such as the government who is not willing to see a continuously declining growth rate. However, the report is too optimistic about it, and I'm afraid the prospect is not as bright as the report points out. The main reason is that the slump in export is not a short-term trend. Thirdly, it is about the stimulus policy. It is true that, in this year, our government has adopted measures to stimulus the economy, and is expected to take more drastically. Therefore, an overall analysis is needed that, how large are the positive and negative effects on the economy when the stimulus is continuously strengthened? Fourthly, it is concerned with the economic growth in the next year. Except from some favorable factors mentioned in the report, is it likely to predict some negative factors that are just temporarily not so apparent, such as employment? Maybe, it does not seem to be that bad in the employment market at present; however, from the aspect of the development trend, it would be a problem in the second half of 2012 and the first half of 2013. Another adverse factor may be the price, I maintain that, the risk of inflation should be taken into a fully consideration. Lastly, it is about the situation of the global economic in this year and the next. I'm afraid we have to consider the drop in demographic dividend. Some experts think the effects of the drop in demographic dividend and aging would be bigger and faster than what we estimate.

I believe that, through effort, the economic growth rate at around 8 % can be achieved. However, is it a potential growth rate? On the other hand, I think the biggest problem in China's economy is the medium term instead of short term. The negative effects appear to be more and more apparent, as the aging is deteriorating, the demographic dividend is declining, and there exist little progress in the structural adjustment. Hence, I am not quite optimistic about the economic growth rate in the medium term. As to the long term, provided that we make obvious achievement in the structural adjustment and the transformation of the mode of economic development, the prospect in the long term would be quite optimistic.