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Washington, D. C. 20505

DIRECTORATE OF INTELLIGENCE

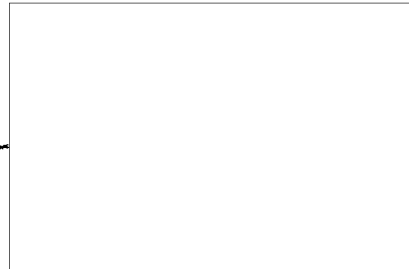
15 September 1983

MEMORANDUM FOR: Recipients of China: Quarterly Economic Report
 FROM : Chief, China Division
 Office of East Asian Analysis
 SUBJECT : China: Quarterly Economic Report

1. The attached memorandum provides a quick fix on current trends and prospects for China's economy. The tables provide data on key economic indicators and are convenient for reference and use in briefings.

2. We welcome suggestions for improvements.

Attachment:
As stated



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CHINA: QUARTERLY ECONOMIC REPORT

Second Quarter: Fiscal, Monetary Problems Emerge Amid
Continued Investment, Heavy Industry Boom

Summary

In the second quarter, Beijing continued to complain that investment spending was out of hand and that local projects still were diverting construction resources from high-priority infrastructure projects. Heavy industry growth once again outstripped light industry, although the latter recovered somewhat from its first quarter doldrums. Budget data, though spotty, confirm that Beijing may be headed for an uncomfortably large budget deficit, and other information indicates excessive money supply growth. Agricultural output is acceptable, even though there was severe flooding this summer. We expect that China will fall far short of its plan to boost imports by 40 percent this year and that it will have another large trade surplus, increasing its already substantial foreign exchange reserves.

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Energy, Transport Projects Delayed

Throughout the second quarter, the government complained that top-priority energy and transportation projects were being held up by shortages of construction materials, siphoned off by large numbers of local projects. As a result of government jawboning and new control measures, investment growth did slow marginally in the second quarter. At mid-year, capital

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_____ the China Division of the Office of East Asian
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are welcome and may be directed to the Chief, Domestic Policy
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construction was running 17 percent above first-half 1982, down from 21 percent in the first quarter. (The 1983 plan calls for an 8 percent drop.) In particular, investment from retained earnings--that pool of funds outside government control--grew by only 5.6 percent in the second quarter, compared with 17 percent in the first. Sectors where spending grew most rapidly in Jan-Jun were energy (up 34 percent) and transportation (up 68 percent). [redacted]

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Budget Deficit Growing

Since the large budget deficits of 1979 and 1980, Beijing has succeeded in keeping them at more manageable levels. Data for first-half 1983, however, signal a rising deficit. In Jan-May, budget revenues rose a scant 0.1 percent compared with the 1982 period, against a planned 9.6 percent increase for the year. At the same time, expenditures seem to have increased at close to the 10 percent called for in the budget. [redacted]

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Industry

Industrial output in the second quarter grew at a 10.4 percent rate over second quarter 1982, a marked increase over the 6.9 percent of the first quarter. Growth for the first six months was 8.8 percent, twice the 4-percent rate specified in the annual plan. [redacted]

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In **heavy industry**, where production grew by 11.7 percent in Jan-Mar, growth accelerated and reached 12.2 percent for the half. The annual plan calls for a 3.9 percent increase. The largest halfyear increases came in investment goods: cement up 14 percent, mining equipment up 49.2 percent, power-generating equipment up 81.2 percent, machine tools up 24.2 percent, hand tractors up 50.8 percent, and motor vehicles up 18.3 percent. Steel production increased at a rate (6 percent) greatly exceeding the plan (zero percent). **Energy** production was up a bit over 5 percent in the second quarter, approximately the rate achieved in the first quarter. [redacted]

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In spite of the unwelcome diversion of resources from light to heavy industry, **light industry** turned in a very respectable 8.1 percent growth rate for second quarter 1983, raising the Jan-Jun increase to 5.4 percent. The plan calls for 4.1 percent growth. Textile output regained momentum after a relatively poor first-quarter. [redacted]

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Through the end of May, **quality** and **cost** indicators showed little, if any, improvement. Of 75 indices of quality, 19 percent declined in the Jan-May period, a slight worsening of the situation in Jan-Feb 1983 when 16 percent showed declining quality. Also, in Jan-May, 70 percent of the 105 indices of energy and raw material usage showed signs of improvement, up

slightly from the 67.5 percent in Jan-Feb. Industrial costs, targeted to drop 2 percent in 1983, actually rose 1 percent in the first six months. [redacted]

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Agriculture

Cool, wet weather reduced the early rice crop in central and southern China. The second quarter also saw serious flooding in central and eastern China, but Beijing announced in July that the flood waters had abated and that damage, while serious, was not as bad as portrayed in Western press reports. [redacted]

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Foreign Trade

Chinese customs data for Jan-Jun show a 1.0 percent decline in imports and a 6.5 percent decrease on the export side. Of greatest interest in the second quarter was China's continuing unwillingness to purchase US grain, an important factor in the 24 percent drop in Sino-US trade in Jan-Jun. China's imports from the US were down 39 percent; exports declined 2 percent. [redacted]

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Elsewhere in the Economy

Retail sales: Spurred by a 2.6 percent increase in nonagricultural employment and a 6.9 percent rise in total wages, sales of consumer goods grew by 10.7 percent in Jan-Jun. [redacted]

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Transport: Performance in the first half was slightly ahead of plan, with rail freight volume up 3.8 percent over 1982. Freight handling at major coastal ports was up an impressive 7.4 percent. [redacted]

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Construction: Total floor space under construction was up by 3.2 percent compared with Jan-Jun 1982. Housing construction, however, which accounts for over half of the space being built, fell by 2.4 percent. And completions ("total floor space completed") fell for both housing (down 4.5 percent) and other buildings (down 3.0 percent)--probably attributable to shortages of building materials. [redacted]

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Inflation: Strong investment and consumer demand, a large increase in currency in circulation, and the government's widely publicized complaints about rising construction costs make it clear that inflationary pressures remain strong and that prices are rising at higher-than-average rates. [redacted]

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*Growth rates are in dollar terms. Chinese customs data are on a FOB-CIF basis, and for other reasons differ from trading-partner data used by CIA. Consequently, these percentage increases should not be applied to statistics in the accompanying table. [redacted]

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Performance Outlook**Domestic Economy**

Midyear through 1983, the economy bears a striking similarity to conditions that led Beijing to retrench drastically in 1981. Particularly nettlesome problems in 1983--only the first of which appeared in 1981 and 1982--are historically high investment rates, a growing budget deficit, and excessive monetary expansion. The Chinese press has noted the resemblance to the earlier period and specifically raised the spectre of the 1981 retrenchment. All public statements suggest that Beijing believes such a strong remedy is undersirable. We believe the corrective measures will fall short of retrenchment, and may ease but will not remedy the problem. []

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Beijing recently has acknowledged that the goal of cutting investment by 8 percent is unattainable, but has asked that this year's level not exceed last year's. We believe this still is too optimistic and project that investment easily will exceed last year's level. This will contribute to a continuation of unbalanced industrial growth. We also believe that the planned budget deficit 3 billion yuan--will be exceeded for the first time in 3 years, probably by a significant amount. If the government is not able effectively to control currency creation by yearend, Beijing may have to resort to measures they used in 1981. []

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Over the next few months, we expect to see:

- Higher-than-planned industrial growth based on both strong investment and consumer demands. Producer goods production may slow if Beijing succeeds in reducing investment spending; the output of consumer goods may hold at the 8 to 9 percent growth displayed in the second quarter, especially if a slowing of producer goods output results in improved supplies of energy, raw materials, and transport for consumer goods industries.
- Shortages of construction materials that will hamper progress on important energy and transport projects, even if investment continues to taper off.
- Rising industrial costs that will make it difficult to increase budget revenue and avoid a larger deficit.
- Strong inflationary pressures, based on investment and wage growth, and on an expanding deficit financed in part by increases in the money supply. []

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Foreign Trade

We see little likelihood of China's imports rising by the planned 40 percent*, even if Beijing honors the US-China grain agreement. Consequently, we believe that China will experience another current account surplus this year: about \$3 billion in trade and another \$500 million in net earnings from invisibles. We expect China's foreign reserve position by yearend to be about \$15 billion, up nearly \$4 billion from yearend 1982.

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*In dollar terms; 25 percent in yuan terms.

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	Quarters					Annual		
	1982			1983		1982	1983	
	II	III	IV	I	II	Chinese Plan	Actual	Chinese Plan
Production (Bil 1980 Yuan, except where noted; numbers in parentheses are percent change from previous year)*								
Total Industry	143.77 (8.9)	136.24 (5.7)	148.71 (4.1)	138.29 (7.1)	158.61 (10.3)	538.9 (4.0)	557.9 (7.7)	580.2 (4.0)
Heavy Industry	72.09 (10.4)	69.51 (10.4)	72.73 (7.9)	69.33 (11.7)	81.27 (12.7)	254.0 (1.0)	276.4 (9.9)	287.2 (3.9)
Light Industry	71.52 (7.3)	66.73 (0.0)	75.98 (1.6)	68.96 (2.5)	77.34 (8.1)	284.9 (7.0)	281.5 (5.7)	293.0 (4.1)
Agricultural Production						240.4 (4.0)	256.6 (11.0)	266.9 (4.0)
Grain Production (Million tons)						333.5 (2.6)	353.4 (8.7)	N.A.
Energy Production								
(Million tons coal equivalent)	168.1 (8.0)	164.6 (5.6)	181.14 (-5.2)	162.19 (5.2)	176.81 (5.2)	625.4 (-0.3)	668.0 (5.7)	N.A.
Oil Production (Million tons)	26.06 (3.5)	25.44 (0.6)	25.28 (-0.9)	25.88 (2.1)	26.33 (1.0)	100.0 (-1.2)	102.1 (0.9)	100.0

*Quarterly growth rates shown in the table may differ from the official growth rates cited in the text. The difference is caused by unannounced revisions of data for earlier quarters by the Chinese State Statistical Bureau. We assume the quarterly industrial output value data are in 1980 prices, but they may in fact be in current prices. Nevertheless, the growth rates represent real growth.

(Percent change from previous year in parentheses)

	Quarters					Annual		
	1982				1983	1980	1981	1982
	I	II	III	IV	I			
<u>International Trade and Finance</u>								
(Mil \$US, f.o.b., not seasonally adjusted, except where noted)								
Total Exports	5547.8 (14.3)	5487.9 (4.6)	5612.3 (2.6)	5571.4 (-7.1)	5204.4 (-6.2)	18893.6 (40.4)	21566.2 (14.2)	22219.6 (3.0)
Total Imports	4076.3 (-25.7)	4135.7 (-3.7)	3884.5 (-0.9)	4043.8 (-5.0)	3998.0 (-1.9)	19179.8 (34.1)	17959.1 (-6.4)	16140.2 (-10.1)
Trade Balance	1471.6	1352.1	1727.8	1527.6	1206.3	-286.2	3607.1	6079.4
Oil and Petroleum Products Exports	1196.9 (14.4)	1047.2 (-4.5)	1303.5 (12.1)	1272.6 (-1.3)	1035.2 (-13.5)	4165.1 (84.5)	4595.4 (10.3)	4820.4 (4.9)
Grain Imports (Million tons)	3.209 (-4.7)	4.165 (30.7)	3.954 (20.2)	3.656 (8.9)	4.643 (44.7)	13.673 (26.0)	13.204 (-3.4)	14.984 (13.5)
Liquid Assets	5460 (129.8)	7287 (90.7)	9444 (139.9)	11339 (124.6)	12609 (130.9)	2545	5048	11339
Liquid Liabilities*	3719 (-41.3)	3697 (-38.3)	3724 (-37.4)	3745 (-21.3)	3991 (7.3)	5667	4759	3745
Exchange Rate (yuan/dollar)	1.8675	1.9310	1.9684	1.9227	1.9941	1.5115	1.7183	1.9224
<u>Japan - China Trade</u>								
Exports to Japan	1299.9 (24.8)	1250.3 (4.0)	1250.6 (-3.5)	1282.6 (-14.0)	1145.0 (-11.9)	4139.5 (48.3)	5031.9 (21.6)	5083.4 (1.0)
Petroleum and Products	716.1 (30.0)	572.0 (-1.9)	704.0 (0.1)	711.8 (-7.6)	601.9 (16.0)	2159.4 (104.6)	2607.7 (20.8)	2703.0 (3.7)
Imports from Japan	848.6 (-40.7)	888.2 (-34.0)	839.6 (-27.1)	923.5 (-19.5)	871.0 (2.6)	5109.6 (38.8)	5076.1 (-0.7)	3500.0 (-31.1)
Trade Balance with Japan	451.3	362.1	410.9	359.1	274.0	-969.9	-44.2	1583.4

*Liquid assets are almost all foreign exchange reserves; liquid liabilities are mainly national bank liabilities. In addition, the Chinese have some SDRs and IMF liabilities and 12.7 million ounces of gold.

(Percent change from previous year in parentheses)

	Quarters				1983 I	Annual		
	1982					1980	1981	1982
	I	II	III	IV				
<u>U.S. - China Trade</u>	(Mil \$US, f.o.b., not seasonally adjusted, except where noted)							
Exports to U.S.	556.6 (47.0)	487.6 (-0.5)	697.0 (29.6)	542.4 (11.7)	534.9 (-3.4)	1053.3 (78.2)	1892.0 (79.6)	2283.6 (20.7)
Textiles and Clothing	200.6 (39.6)	175.4 (44.0)	261.4 (44.8)	188.5 (11.1)	246.5 (22.9)	354.6 (78.5)	615.6 (73.6)	825.9 (34.2)
Petroleum and Products	114.3 (412.6)	95.6 (69.2)	214.7 (77.6)	173.1 (84.7)	90.4 (-20.9)	134.7 (39.6)	293.5 (117.9)	597.7 (103.7)
Imports from U.S.	905.2 (-23.5)	801.9 (18.1)	686.6 (-16.1)	518.6 (-43.8)	668.8 (26.1)	3754.4 (117.8)	3602.8 (-4.0)	2912.3 (-19.2)
Grain (million tons)	1.968 (0.3)	2.564 (90.9)	2.407 (-0.7)	1.527 (-35.2)	2.132 (8.3)	8.037 (101.2)	8.084 (0.6)	8.466 (4.7)
Textile Fibers	237.1 (-46.9)	94.2 (-46.3)	37.6 (-79.0)	26.5 (-89.5)	16.8 (-92.9)	1016.4 (127.0)	1053.5 (3.7)	395.3 (-62.5)
Trade Balance with U.S.	-348.6	-314.3	10.4	23.8	-133.9	-2701.1	-1710.8	-628.7
<u>Aggregate Indicators</u>								
Population (mil on July 1)						981 (1.3)	993 (1.2)	1008 (1.5)
Gross National Product (Bil 1982 \$US)						271.8 (5.2)	280.0 (3.0)	300.7 (7.4)
GNP per capita (1982 \$US)						277.1 (5.5)	282.0 (1.8)	298.3 (5.8)
State Budget (Bill yuan):								
Revenues						108.5 (-1.6)	109.0 (0.5)	110.7 (1.6)
Expenditures						121.3 (-10.6)	111.5 (-8.1)	113.7 (2.0)
Deficit (-) or Surplus (+)						-12.8	-2.5	-3.0

SUBJECT: China: Quarterly Economic Report
[redacted] EA M 83-10180

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