

China's plan to spend and liberate

AT A GLANCE

- China's latest blueprint for managing its economy sets forth an agenda of moderate growth and social reform. In its 12th five-year plan, the government has made concessions on growth ambitions in favour of improving social structures such as housing, health care and income distribution.
- The planning process has been central to China's growth, yet failure to provide adequate social safety nets and evenly distribute the gains from China's economic expansion has highlighted its shortcomings.
- The latest plan seeks to rectify economic inequality while investing in the country's future to make the transition from an export-led to a consumer-driven economy.

The overall objectives of China's 12th five-year economic plan are the promotion of sustainable economic growth while restricting over-investment in certain sectors of the economy. The plan also devotes considerable attention to social reforms. Significant investment in the area of research and development is another key platform, set to make China the centre for technology development in Asia. Will China succeed in meeting such a diverse range of goals?

PLAN FOR BALANCED GROWTH NOW IN PLACE

The policy framework of its latest five-year plan should be considered as a 'guide' rather than a 'plan'. By the time authorities in Beijing were implementing their 11th five-year plan (2006 to 2010), they decided the word "plan" failed to capture the country's shift to a "socialist market economy". So they softened the language to reference the content as "guidelines". The 12th five-year plan, covering goals for 2011 to 2015, is now in place but calling them "guidelines" may in time understate its significance, if the extent of economic transformation prescribed by them is any indication.

EVOLUTION OF THE PLANNING PROCESS

Like other centrally-controlled economies, a considered and comprehensive plan is imperative if the economic model is to remain effective. China first embarked on the five-year planning model not long after the Second World War. Its first five-year plan (1953 to 1957) was adopted from the Soviet model. The inaugural plan introduced initiatives to transform China's agriculture-focused economy to the industrial powerhouse it is today. The concept of privately operated industrials was integrated into the socialist structure, supported by the commencement of 654 large and medium-sized industrial projects. The initial plan was successful in some respects, but managing the rapid transformation to industrial output and away from agricultural production came at a cost. Initiatives such as the 'great sparrow campaign', which sought to improve agricultural efficiency by eradicating the country of notorious pests – rats, flies, mosquitoes and sparrows, led to an ecological imbalance. A locust plague attacked crops and severely reduced food supplies.

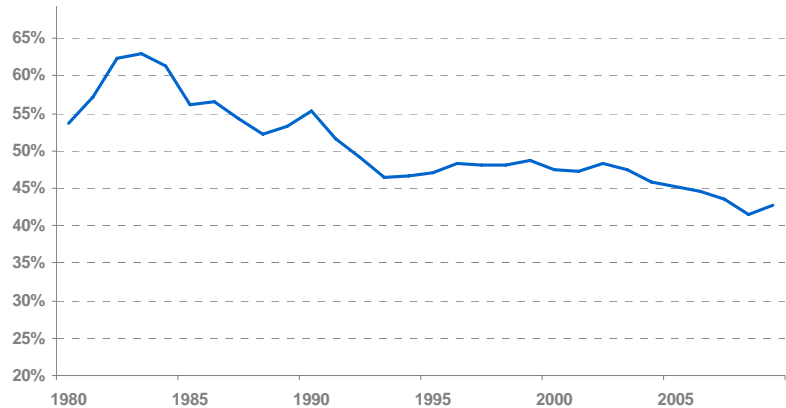
GROWTH BALANCED WITH EQUALITY

Reforming social structures is a key policy platform in the current plan, and for good reasons. Although the average Chinese worker has enjoyed a remarkable rise in living standards in one generation, they have failed to fully benefit from China's modernisation. The ratio of household income to gross domestic product in China declined to only 41% in 2009 from 63% in 1982 because the economic gains have been unevenly distributed.¹ The 12th five-year plan proposes to correct this by making wealth distribution more equitable, expanding domestic consumption, boosting rural and inland development and improving social safety nets.

In the latest five-year plan, China is clearly seeking to balance growth with improving social structures. The plan contains measures to boost social housing, effectively redistributing gains to workers. The government says 36 million public housing units will be built in the coming five years. The government also hopes to reduce the country's savings rate by increasing state pensions and expanding national health care cover. It is hoped that these policies will reduce the need for people to save large proportions of their income for their old age or if they get sick.

1. Source: National Bureau of Statistics, China, Datastream. Based on the ratio of total household income to gross domestic product per capita, in RMB.

RATIO OF HOUSEHOLD INCOME TO GROSS DOMESTIC PRODUCT



Source: National Bureau of Statistics, China

China's 11th Five-year plan: 2006-2010 - Targets and outcomes

	Target	Actual
Economic growth	7.5% p.a	11.2% p.a
Urbanisation rate in 2010	47%	47.5%
Wind energy capacity~	5 gW	40 gW
Average urban disposable income (per capita)	27%	82%
Target for treated urban waste water	70%	75%

Source: People's Republic of China official website, sourced 21 March 2011; China National Bureau of Statistics.

~ gW refers to Gigawatts – a unit of electrical power equal to one billion watts.

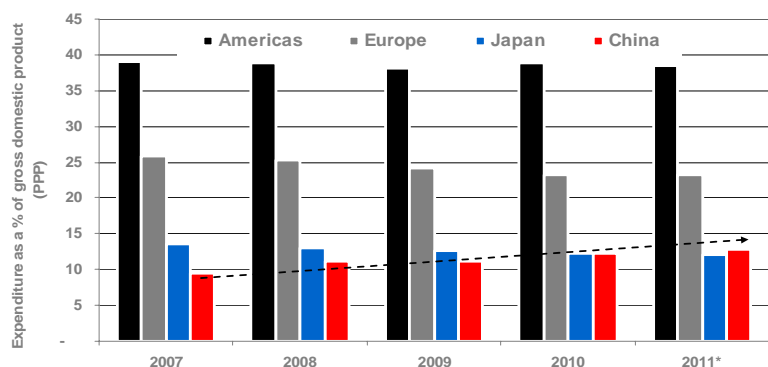
Rapid urbanisation has highlighted the need to narrow the urban-rural gap as it relates to incomes and living standards. Over the five-year period there will be a boost to agricultural investment, aiming to improve productivity and income. Changes to rural property rights will effectively vest farmers with 16 trillion yuan (US\$197 billion) worth of land-leasehold rights, which can be sold or used as collateral for borrowing. It is likely that the Hukou system, which prevents many rural immigrants and their descendants from settling in cities, will be relaxed.

FOCUS ON A NEW ERA IN CHINA'S DEVELOPMENT

Other areas of the plan have received considerably less public attention but over time, may be considered revolutionary. The government has ear-marked seven sectors for focussed investment. These "strategic industries" are: environment/energy-saving technology, alternative energy, bio-technology, new information technology, high-end equipment, new materials and new-energy cars. Policy measures include subsidies for technology acquisition, research allowances and tax incentives. The government views alternative energy as a way to make economic growth more sustainable and create jobs. Comparison with the previous set of strategic industries highlights the significant change in focus. The 11th plan stipulated focus on national defence, telecommunications, electricity, oil, coal, airlines, and marine shipping.

Research and development have been areas of focus in recent years. In 2006, the Chinese government stepped up efforts to develop "indigenous innovation". Since then, expenditure on research and development has continued to rise, despite setbacks from the global financial crisis and sovereign debt dilemmas. China is on its way to replace Japan as Asia's research and development centre, just as it has done so in gross domestic product terms over the past year.

RESEARCH AND DEVELOPMENT EXPENDITURE



Source: Battelle, "2011 Global Research and development funding forecast", December 2010*

FROM “MADE IN CHINA” TO “DESIGNED IN CHINA”

Since launching economic reforms in 1978, China has persisted with an export-led and investment-driven recipe for economic success. The results of these efforts are clearly evident in the China the world sees today. Within 30 years, China has become the world's biggest exporter and the world's second-largest economy.

A clear signal from the government is its intention to shift focus from importing technology to local innovation. The country's advances in defence, satellite and space technologies are examples of emerging capabilities in technological development. Unlike many western countries, China's national accounts show its capacity to grow investment in these areas.

Spending on next-generation information technologies, one of the key development areas, is resulting in a rapid response from companies operating in the sector. China Mobile, a company with the world's biggest wireless subscriber base, has increased its proposed capital expenditure to 132.4 billion yuan (US\$20.1 billion) in 2011, compared with 124.3 billion yuan spent last year to expand the range of data services currently offered.² China Mobile had a total of 584 million mobile phone subscribers at the end of last year, including 20.7 million customers using a high-speed, third-generation mobile service that enables smartphone users to access the internet.² In December the company received approval from the Ministry of Industry and Information Technology to begin a trial of its fourth generation TD-LTE network, a technology standard designed to increase the capacity and speed of mobile telephone networks. The company recently added Beijing to the original six cities in the trial program: Shanghai, Hangzhou, Nanjing, Guangzhou, Shenzhen and Xiamen.

REFORMS AIMED AT LONG TERM ECONOMIC TRANSFORMATION

Details around financial and fiscal reforms highlight the government's intentions to pursue more prudent financial regulation and reform. Relaxing controls on interest rates and the capital account is likely to continue in line with steps to internationalise the yuan and make the exchange rate more flexible. The central government is likely to increase transfer payments to local government, while provincial governments will be granted more discretion over taxes. At the same time, the plan seeks to restructure state monopolies to encourage competition, efficiency and private investment.

The government's moderation of economic growth targets to 7% from the previous plan's target of 7.5% is aimed at promoting economic and social equilibria. It is only with social harmony that China's economic goals can continue to be achieved. The focus on creating the right development foundations are noble, yet evolutionary in setting the scene for future economic expansion.

Sources:

2. Bloomberg, "China Mobile unexpectedly boosts annual spend to \$20 billion", 16 March 2011



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