

MACROECONOMIC PERFORMANCE

In 2008, the Chinese economy realized a relatively rapid economic growth of 9 percent and the price level declined from a high level as well in spite of shocks from the devastating natural disasters and global financial crisis. In terms of the quarterly economic performance, due to remarkable contract of external demand and somewhat shrink of domestic demand, Chinese economy was on the downward trend with industrial production slowing down remarkably, economic profits greatly reducing and employment pressure increasing.

In 2009, global economy including Chinese economy will be in the period of adjustment and recovery in general and Chinese economy will face many uncertainties due to various factors both at home and abroad. However, with the implementation of a series of policy measures aimed at boosting domestic demand to sustain economic growth and adjusting economic structure, domestic economy will gradually stabilize and recover. Firstly, large increases in construction of new projects will promote the acceleration of investment growth; Secondly, policy measures to improve people's well-beings such as tax reduction, income increase, job creation, grain purchasing price hike and etc will positively stabilize consumption; Thirdly, huge internal demand potential and high savings ratio in China will give enough room for macro-adjustment. In general, with proper policy measures and timely and effective implementation, China will realize the around 8 percent of economic growth target in 2009.

Main Features of China's Economic Performance in 2008

In 2008, due to the remarkable shocks from the catastrophic natural disasters and global financial crisis, the economic performance in China reversed from a sustained growth since 2003 to a gradual decline. Especially after September, with deepening of global financial crisis, external demand shrank markedly and dragged domestic output and price level to decline rapidly, and so Chinese economic downside risks increased remarkably. Faced with the complicated and severe economic situation both at home and abroad, in line with the changing situation, the CPC Central Committee and the State Council, giving priority to expand effective domestic demand in particular consumption demand, adjusted macro-policy orientation in a timely manner to implement the proactive fiscal policy and moderately loose monetary

policy and formulated a package of plan aimed at promoting stable and relatively rapid economic development, such as expanding government expenditure in a large scale, carrying out structural tax reduction, launching the 2-year 4 trillion yuan investment plan, increasing interest rate-cut frequencies and injecting liquidity in the banking system, implementing industrial adjustment and revival plan in a large scale to promote industrial structure adjustment and upgrade, promoting technology innovation and technical reform in great efforts and substantially enhancing social safety net. All of the measures played a crucial role in promoting stable economic development and maintaining financial market stability.

Economic Growth Fell down from Its High Level

According to the preliminary calculation of the National Statistic Bureau, the GDP grew 9 percent y-o-y to 30.067 trillion yuan in 2008, representing a

deceleration of 4 percentage points from 2007, but 6.5 percentage points higher than the average 2.5 percent of global economic growth. Broken down by quarters, the quarterly GDP growth registered 10.6 percent, 10.1 percent, 9 percent and 6.8 percent y-o-y respectively (Figure 1). Broken down by industries, the added value of the primary industry grew 5.5 percent to 3.4 trillion yuan, representing an acceleration of 1.8 percentage points from that of 2007; The added value of the secondary industry enjoyed a growth of 9.3 percent y-o-y to 14.6183 trillion yuan, representing a deceleration of 5.4 percentage points from that of 2007; The added value of the tertiary industry increased by 9.5 percent y-o-y to 12.0487 trillion yuan, representing a deceleration of 4.3 percentage points from 2007. In terms of the proportion of GDP, the share of the primary, the secondary and the tertiary industry in GDP was 11.3 percent, 48.6 percent and 40.1 percent respectively, up 0.2 percentage points and 0.1 percentage points and down 0.3 percentage points from 2007 respectively.



Inflation Declined after Rising with Downward Pressure Increasing

The CPI gradually declined and its growth accelerated before decelerated. Due to a variety of factors including relatively rapid price hike in food and

raw materials in the international markets, the domestic inflation speeded up since the fourth quarter of 2007, and the CPI surged to 8.7 percent year-o-year in February 2008, the largest monthly increase since June 1996. Thereafter, with the moderation of economic growth and rapid raw material price decline in the international markets, and in addition, effects of the policy measures to contain excessively rapid price hike, the CPI gradually went down, and registered a growth of 5.9 percent for the whole of 2008.

The prices of industrial products declined sharply from its elevated level. From the second half of 2007 to August 2008, given the soaring raw material prices in the international market, domestic PPI increased gradually, with the purchasing price of raw materials, fuel and power up 15.4 percent year-on-year in July 2008 and the industrial producer price up 10.1 percent in August 2008 year on year. Thereafter, as the markedly deepening of global financial crisis, raw material prices in the international market plunged, and domestic producers began to de-inventory so that the PPI declined substantially and turned into negative growth very rapidly. Till December of 2008, the purchasing price of raw materials, fuel and power and the industrial producer price decelerated by 1.3 percent and 1.1 percent respectively (Figure 2).



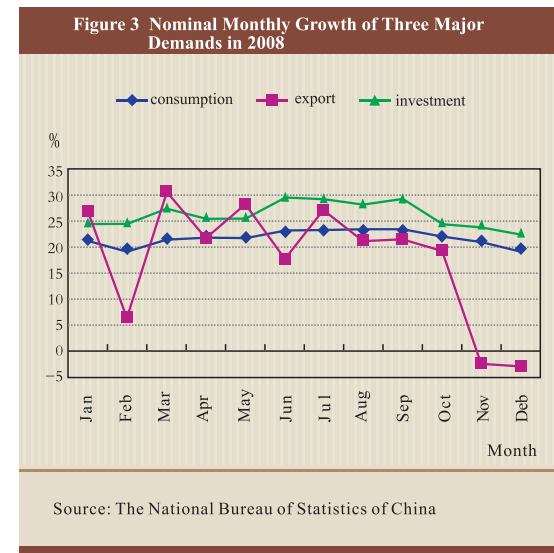
External Demand Contracted Sharply and Domestic Demand Declined Somewhat

Along with depressed global economy and sharply contracted external demand and reduction of payment capacity of importing countries due to the worsening of global financial crisis, the external environment for China deteriorated remarkably. In 2008, the export grew by 17.2 percent y-o-y, down 8.5 percentage points from the previous year; import increased by 18.5 percent y-o-y, down 2.3 percentage points from 2007. The total trade surplus in 2008 realized \$295.46 billion, representing an increase of \$33.26 billion compared with 2007.

Domestic demand declined somewhat. In 2008, the social fixed-asset investments totaled 17.229 trillion yuan, representing a nominal increase of 25.5 percent y-o-y, down 1.5 percentage points from the first three quarters, but up 0.7 percentage points from 2007. The real growth was 18.1 percent y-o-y after deducting price factor. Urban fixed-asset investment grew 26.1 percent y-o-y, down 1.5 percentage points from the first three quarters but up 0.3 percentage points from 2007. In 2008, the total commodity retail sales grew by 21.6 percent in nominal term, down 0.4 percentage points from the first three quarters but up 4.8 percentage points from 2007. In real term, the total commodity retail sales grew by 14.8 percent, up 2.3 percentage points from a year earlier (Figure 3). Broken down by classifications, the decline of demand for real estate and relevant products was one of the important factors for moderation of the domestic demand. The selling squares of commodity housing in the whole year reduced by 19.7 percent y-o-y, substantially down 42 percentage points from 2007.

Industrial Production Slowed Down Remarkably

In 2008, the total industrial added value grew by 9.5 percent y-o-y to 12.91 trillion yuan, down 4 percentage points from 2007. The added value of statistically large enterprises increased by 12.9 percent y-o-y, down 5.6 percentage points from 2007. In terms of quarterly trend, the monthly average growth of the added value of



statistically large enterprises accelerated by 1.5 percentage points from the first quarter of 2007, but decelerated by 2.4 percentage points and 5.2 percentage points from the second quarter and third quarter of 2007 respectively. And in the fourth quarter, the y-o-y monthly growth decelerated (Figure 4).

In the second half of 2008, due to the slowdown of internal and external demand and the inventory adjustment resulted from dramatic price volatility of raw materials in the international market, the industrial production growth decelerated greatly. Because of the continued price hike of raw materials in the

international market in the first half of 2008, enterprises stored excess raw materials and accordingly, while the price of raw materials slumped in the second half of 2008, especially in the fourth quarter, enterprises had to consume the excess inventories and therefore reduced their demands for raw materials, resulting in the dramatic production contraction in upper-stream heavy industry who produce raw materials, thus industrial production sharply shrank, especially heavy industrial production, since the fourth quarter.

Economic Efficiency Declined Markedly and Households' Income Growth Moderated

In terms of companies' profits, the realized profits of the statistically large enterprises grew by 4.9 percent y-o-y in the first 11 months, down 14.5 percentage points from the first 8 months, representing a substantially depreciation of 31.8 percentage points y-o-y. Except for the impacts from economic moderation, demand reduction, the slump of raw material prices from high level since September also stroke enormously enterprises' profits, profits of the statistically large enterprises declined by 26.5 percent y-o-y between September and November, representing a deceleration of 45.9 percentage points from the first 8 months.

In terms of fiscal revenue, the fiscal revenue exceeded 6 trillion yuan in 2008, representing an increase of 19 percent y-o-y, down 13.4 percentage points from the growth of 2007. The growth of fiscal revenue decelerated dramatically, recording two consecutive negative growths in October and November. The main reasons for the negative growth of fiscal revenue were the large increase of export tax refunds and reduction of stamp tax revenues.

In terms of urban and rural households' income, growth of urban and rural per capita income decelerated in real term in 2008. In particular, the urban per capita households' disposable income grew by 8.4 percent in real terms, down 3.8 percentage points from 2007; the rural per capita households' cash income grew by 8.0 percent in real term, down 1.5 percentage points from

2007. The moderation of resident's income was mainly attributed to the declined economic profits and increased employment pressure. Urban registered unemployment ratio edged up for the increase in the number of suspended or bankrupted enterprises and home-returning rural migrant workers. In December, the PMI employment index was 43.3 percent, below 50 percent for 3 months in a row, falling into the economic contraction zone.

Macroeconomic Outlook in 2009

China's Economy Will Gradually Stabilize and Recover

Global and China's economy will broadly stay in the adjustment and recovery stage in general. In terms of global economies, major advanced economies including the US, Europe and Japan will be possibly in recession while developing countries' economic growth will slow down substantially, so that demand for China's exports will be contained further to a large extent. In terms of domestic situation, with the gradual implementation of a package of policy measures to restructure and boost domestic demand to sustain economic growth since the third quarter of 2008, the rapid economic downward momentum has been contained preliminarily in the first quarter of 2009 and the majority of economic indicators presented a positive change, i.e., phased stabilizing. Although 2009 will confront with many uncertainties because of various factors at home and abroad, generally speaking, in a short run, the risk of dramatic economic drop has already diminished remarkably. First, with the gradual conduction of a series of new construction projects, investment growth will speed up further and become an important economic driving force with an anticipation that the social nominal and real yearly investment growth will surpass that of 2008. Second, a series of policy measures aimed at improving people's well-beings including tax reduction, expenditure expansion, job creation and grain purchasing price hike implemented by the Chinese