

Part 2 : Chapter 6 - People ' s Republic of China

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Chapter 6

PEOPLE'S REPUBLIC OF CHINA

People's Republic of China

Area:	9.6 million km ²
Population:	1,299.88 million (as of end of 2005)
Capital:	Beijing
Language:	Chinese, Tibetan, Mongolian, Uighur
Religion:	Taoism, Buddhism, Islam, Christianity
Government type:	Socialist republic
Chief of state:	President Hu Jintao
Currency:	yuan (US\$1 = 8.0702 yuan; as of end of 2005, based on median rate of the People's Bank of China)
Fiscal year:	Calendar year

China's Dilemma of High Economic Growth

KENICHI IMAI, HARUKA MATSUMOTO, and MAMI YAMAGUCHI

The successful launch of Shenzhou-6, China's second manned spacecraft, in the autumn of 2005 created a strong impression both at home and abroad that China has been developing very successfully. Following Jiang Zemin's complete resignation from key posts, the administration of President Hu Jintao launched a full-fledged effort to strengthen and expand the political foundation of his government. As part of this effort, Hu adopted a series of slogans, to focus on the promotion of a "scientific concept of development" and the building of "a harmonious society." His administration also pushed an "education campaign to preserve the advanced nature of party members," in a bid to enhance the policy-execution capability of Chinese Communist Party (CCP) senior officials, and to impose tougher discipline on them. But there a large number of deep-rooted contradictions remain in Chinese society, leaving the Hu administration with a pile of problems to tackle.

In the area of bilateral relations, China's ties with Japan have worsened notably, and it seems unlikely that the two countries will soon reach any breakthrough to improve the situation. China has tried to strengthen its diplomatic ties with the United States, through a series of summit talks with the US leader and a strategic dialogue, but relations between the two countries could go either way—towards greater confrontation or greater cooperation. While trying to reinforce its ties with the United States, Beijing has also stepped up its approaches to Russia and European countries. On the multilateral front, China has been pushing for multilateral diplomacy, by actively participating in regional international frameworks such as the Shanghai Cooperation Organization (SCO) and East Asia

Summit, as well as the six-party talks on North Korea's nuclear program, although the major powers that take part in such regional frameworks each try to assert their leadership.

China's economy has maintained a high growth rate of 9.9 percent. But fixed capital investment, a prime mover of China's economic expansion in recent years, is beginning to generate a huge supply capacity that exceeds demand expansion. Despite the fact that the monetary authority has let the renminbi appreciate slightly against the US dollar, as import growth has slackened due to credit tightening, the country's trade surplus swelled to record-breaking levels, surpassing that of Japan and intensifying trade frictions with the United States and Europe. In its economic management policy, China has been facing the difficult task of simultaneously sustaining stable growth and reducing external imbalances.

DOMESTIC POLITICS

In an attempt to strengthen and expand his political power base after taking control of the party (general secretary), the state (president), and the military (chairman of the Communist Party of China Central Military Commission), Hu Jintao has begun to impose himself more in policy making. Hu has put particular emphasis on improving the policy-execution capability of senior party officials, by promoting education tailored to each rank of party members, and implementing an "education campaign to preserve their advanced nature" as part of efforts toward greater centralization of power within the party. But many problems inherent to the Chinese society remain, including corruption and bribery of senior party members, and a wide disparity between rich and poor. The frequency of riots initiated by citizens in recent years is symbolic of the seriousness of these problems.

National People's Congress and Government Policy in 2005

The third conference of the 10th National People's Congress was held from March 5 to March 14, 2005. In reporting on government activities to the conference, Premier Wen Jiabao said that, with reference to the Deng Xiaoping Theory and the important idea of the "Three Represents" as a guide to action, the Chinese government would respect the spirit of the 16 National Congress of the Communist Party of China (CPC), the Third Plenary Session of the 16th Central Committee of the CPC, and the

Fourth Plenary Session of the 16th Central Committee of the CPC. Wen also said China would seriously address all issues related to economic and social development in line with the “scientific concept of development,” strengthen and improve macroeconomic control, promote various activities based on the reform and opening up policy, build a socialist-led “harmonious society,” and push for socialism that can simultaneously advance material civilization, political civilization, and spiritual civilization. The premier also emphasized the following policies in connection with activities being promoted for 2005: (1) setting a GDP growth rate target of about 8 percent, balancing international balance of payments, cutting the issuance of long-term construction bonds by 30 billion yuan from the preceding year, to 80 billion yuan, creating 9 million new jobs in urban areas, and keeping the unemployment rate below 4.6 percent; (2) maintaining the renminbi’s exchange rates at stable levels; (3) giving highest priority to the so-called “three agricultural factors” (agriculture, farm villages, and farmers), and totally repealing agricultural taxes within 2006; (4) promoting major development projects in western China, and promoting development of central China and former industrial areas such as northeastern China; (5) stepping up reforms of state-owned companies and encouraging nonpublic economic development; (6) trying to build a “harmonious society” in order to realize the “scientific concept of development”; and (7) endeavoring to establish a democratic legal system.

China’s defense budget in 2005 surged 15.6 percent from the initial budget for 2004, making 17 years straight of double-digit growth. Commenting on this budget, the Chinese government emphasized that the nation’s defense spending has continued to account for a very small portion of overall fiscal expenditures and gross domestic product (GDP). The government also stressed that part of the increase in defense spending for 2005 was to finance a moderate improvement in the treatment of military personnel, social security for soldiers, and the formation of troop units, and adjustment and revision of their mechanisms.

On March 14, mainland China formally adopted the Anti-Secession Law. The law states its aim to be stopping the Taiwanese independence movement from splitting the country. The law sets three conditions for resorting to non-peaceful action, or the use of force. The three conditions are: (1) if “Taiwan independence” forces, under whatever name and method, accomplish the fact of Taiwan’s separation from the Mainland; or (2) if a major event occurs that could lead to Taiwan’s separation from the mainland; or (3) if all possibility of peaceful unification is lost. The law

empowered the State Council and the CPC Central Military Commission to decide whether to use force against Taiwan (refer to Foreign Relations).

Major Personnel Reshuffle in 2005

Hu Jintao controlled all of the party, the state, and the military, both in name and reality, when he was elected the chairman of the People's Republic of China (PRC) Central Military Commission at the National People's Congress in March 2005. In 2005, the administration led by Hu carried out a major personnel reshuffle, indicating he was gradually building up his power base. In the reshuffle of the State Council, four new ministers were appointed—Gao Qiang as minister of health, Wu Aiying as minister of justice, Tian Chengping as minister of labor and social security, and Li Shenglin as minister of communications. At the provincial level, six new appointments for secretaries of provincial committees were made—Zhang Baoshun as secretary of the Shanxi Provincial Committee, Zhang Qingli as acting secretary of the Tibet Autonomous Regional Committee, Qian Yunlu as secretary of the Heilongjiang Provincial Committee, Shi Zongyuan as secretary of the Guizhou Provincial Committee, Zhang Chunxian as secretary of the Hunan Provincial Committee, and Wang Yang as secretary of the Chongqing Municipal Committee. In addition, three persons were appointed provincial governors—Huang Xiaojing as governor of Fujian Province, Wang Min as governor of Jilin Province, and Yu Youjun as acting governor of Shanxi Province. Minister of Justice Wu Aiying and Zhang Baoshun, secretary of the Shanxi Provincial Committee, are among figures who rose up from the Chinese Communist Youth Corps, from which President Hu Jintao also hails. As of the end of 2005, a total of eight ministers in the State Council were from the Communist Youth League of China. Whether Hu can send his close aides hailing from the youth league and officials with whom he worked when he was secretary of the Guizhou Provincial Committee or secretary of the Tibet Autonomous Regional Committee to key posts can serve as a barometer to measure the extent of his control of China in the future.

In December, a sweeping reshuffle of the Chinese military was conducted, including a change of high-ranking officers at the People's Liberation Army. Xiong Guangkai, deputy chief of General Staff, the No. 3 man at General Staff Headquarters, retired that month. Xiong was moved to the Standing Committee of the National People's Congress after his retirement. Zhang Qinsheng, assistant chief of General Staff, is expected to be promoted to the post previously assumed by Xiong. It was decided

that four Central Committee members would retire—Gen. Tang Tianbiao, deputy director of the General Political Department of the PLA, Gen. Wen Zongren, political commissar of the Academy of Military Sciences, Gen. Jiang Futang, political commissar of the Shenyang Military Region, and Gen. Liu Shutian, political commissar of the Chengdu Military Region. The administration of President Hu conducted the latest personnel reshuffle of the Chinese military on the pretext of implementing retirement rules and rules that set tenures for posts. But the fact is that Hu has launched a full-fledged campaign to control the military in an attempt to reduce the influence of former president Jiang Zemin. Further reshuffling of military personnel is expected to take place in the lead-up to the meeting of the 17th National Congress of the CPC.

The Hu Jintao Administration's Domestic Politics

The administration led by President Hu Jintao has begun to show its colors in the way it is steering domestic politics. Here, we will focus on three unique points of his administration. The first is the “scientific concept of development,” which was upheld as a slogan for 2005 activities. Since becoming general secretary of the Communist Party of China (CPC), Hu has pushed for the promotion of a “scientific concept of development.” This concept does not mean pursuing only speedier development or higher growth rates. But it is a slogan aimed at achieving sustainable growth by emphasizing a balance between development of urban and rural areas, and giving priority to promoting environmental protection and improving social security and other safety nets (*People's Daily*, November 25, 2005). At its Fifth Plenary Session from October 8 to October 11, the 16th Central Committee of the CPC adopted a CPC proposal on the formulation of the 11th Five-Year Long-Term Plan (2006–11) for the national economy and social development (refer to Economy). The adopted proposal included a statement that the “scientific concept of development” should be fully pursued and implemented in the execution of the 11th Five-Year Long-Term Plan. It also stated that by promoting the “scientific concept of development,” economic and social development should be controlled in a solid and unshakable manner. The proposal argued that it is necessary for China to hold firm to the ideas of making humans the basis of society, changing the concept of development, innovating development models, improving the quality of development, and placing economic and social development on a comprehensive, harmonious, and sustainable development path. Summed up, the “scien-

tific concept of development” was regarded as a prime mover for the implementation of the 11th Five-Year Long-Term Plan.

Secondly, President Hu has proposed the building of “a harmonious society.” This idea has often been floated along with the “scientific concept of development” slogan. The government of President Hu has maintained that building “a harmonious society” is indispensable if China is to promote the “scientific concept of development.” “A harmonious society” is a slogan explicitly proposed at the Fourth Plenary Session of the 16th Central Committee of the CPC in October 2004. The slogan has not been adopted just to achieve economic development in China. It is also aimed at realizing the creation of a society in which, (1) both urban and rural areas can develop, (2) provincial areas will prosper, (3) economic development and social development can go hand in hand, (4) humans and nature can coexist harmoniously, and (5) domestic development is well balanced with China’s opening to outside world. The government of President Hu has launched a campaign to correct the growing social contradictions gripping his country, such as the disparities between rich and poor, which is a dark side of the nation’s rapid economic development, problems of rural areas, and corruption of senior party officials. The CPC Central Party School sponsored a seminar on February 19 to discuss how to improve capabilities for the building of “a harmonious socialist society.” At the seminar, President Hu appealed for the nation to move forward toward steadily building “a harmonious socialist society,” under the historical process of promoting the development of “socialist material civilization, political civilization, and spiritual civilization.”

The third idea being pushed forward by President Hu is an “education campaign to preserve the advanced nature of party members.” The campaign is meant to enhance senior CPC members’ policy-execution capabilities, and eradicate official corruption involving them, by reeducating them so that they can maintain the ideology and behavior expected of a CCP member. The education campaign, launched in January 2005 and set to run until June 2006, covers all of the approximately 68 million CPC members. The campaign is roughly divided into three periods. Education in the first period, from January to June 2005, was directed at CPC members belonging to party organizations at prefectural or higher levels across the nation, government institutions, companies, and business organizations. The second period, from June to December 2005, was for educating party members belonging to *jiceng zuzhi*, basic community organizations based in urban areas, such as residents committees, and organizations in

townships. The third period, to run from January to June 2006, targets party members in *jiceng zuzhi*, basic community organizations based in rural areas.

Behind the Hu administration's policy of pushing for an "education campaign to preserve the advanced nature of party members," is its willingness to take new approaches in political management. The policy also reflects the administration's determination to deal with rampant corruption by CPC members, which has reached intolerable levels. Jia Chunwang, procurator-general of the Supreme People's Procuratorate, reported to the National People's Congress that in 2004 a total of 43,757 public servants were criminally charged over corruption. Receiving bribes was the most common form of corruption, with a total of 35,031 government officials indicted on this charge. The number of public servants arrested by investigative agencies for corruption amounted to 120 per day. In 2004, 198 officials in bureau chief-level positions and 11 in section chief-level were arrested over corruption. The trend, if left unattended, could prompt the general public to question the Hu administration's political-management competence, eventually shaking the foundations of its power base. Responding to this situation, Hu launched his "education campaign to preserve the advanced nature of party members." The campaign, intended to significantly toughen discipline against party members, is part of Hu's efforts to solidify his political base.

The education campaign was first proposed at the Fourth Plenary Session of the 15th Central Committee of the CPC in 2004, which adopted a decision on strengthening the CPC's policy-execution capability. The decision stated that it is urgent for the CPC to improve the policy-execution capability of party leaders, ranking party members and core members, and eradicate corruption involving these officials. The CPC then appealed for all party members to get united in starting the education campaign to "preserve the advanced nature" of members, mainly by implementing the so-called "Three Represents," based on the idea that imposing tougher discipline on members belonging to the smallest units of the party and rank-and-file party members can help in building a party with strong policy-execution capability. In November 2004, the CPC announced its No. 20 Central Committee policy, in which the party formally decided to implement the education campaign. On January 5, 2005, the CPC convened a working conference on the education campaign to "preserve the advanced nature" of Central Committee party members, at which the party instructed members across China to start the campaign.

Zeng Qinghong, member of the Standing Committee of the Political Bureau of the CPC Central Committee, told the working conference that all-level provincial party committees and all divisions of Central Committee and State Council agencies should set up expert organizations to concretize the education campaign. On January 14, CPC General Secretary Hu Jintao attended a meeting of an expert panel on the campaign and emphasized that “advanced nature” is a fundamental feature of a Marxist political party. He said the Political Bureau of the CPC Central Committee would do its utmost to promote the “education campaign to preserve the advanced nature of party members.”

Policy-execution Capability of Local Governments

While efforts to build “a harmonious society” based on the “scientific concept of development,” and the “education campaign to preserve the advanced nature of party members” proceeds smoothly, the policy-execution capability of local government officials is being increasingly questioned in recent years. The closed nature of local governments was revealed when an explosion leading to the contamination of the Songhua River occurred in November 2005. On November 13 of that year, a petrochemical plant run by Jilin Petrochemical Company under China National Petroleum Corp. exploded, causing harmful chemicals to pour into the Songhua River, at levels far in excess of the maximum set under environmental standards. On November 21, the government of Harbin City in Heilongjiang Province announced suspension of the water supply, citing the need to inspect and repair water-supply facilities in the city. However, on November 22, the city government revised the previous day's announcement, saying that the Songhua River may have been contaminated due to the explosion of a petrochemical plant in Jilin Province. The contamination of the river was not revealed to the general public until more than 10 days after the explosion occurred. On November 26, Premier Wen made an unscheduled visit to Harbin City to inspect the contamination of the river. On December 2, Xie Zhenhua, director of the State Administration of Environmental Protection, was dismissed from his post, to take blame for the accident. Zhou Shengxian was appointed to replace him. Xinhua News Agency quoted the governor of the Heilongjiang Provincial People's Government as saying that Harbin City lied about the incident as part of information control, terming the action “a well-intentioned lie” meant to prevent confusion (November 27, 2005). But in view of the seriousness of the accident, which resulted in a

number of fatalities, the handling of the matter by Chinese authorities served to promote distrust toward them, both at home and abroad.

In 2005, major accidents continued to occur at coal mines in China. According to statistics compiled by the State Administration of Work Safety Supervision, a total of 5,986 people were killed in coal mine accidents. The number of coal mine accidents amounted to 3,341 for the year, down 8.2 percent from the preceding year. However, the number of coal mine accidents resulting in the deaths of 30 or more people totaled 11, up 3 from the previous year. Ensuring a stable supply of coal is important to China, because it is directly related to state energy policy. The Chinese government has stepped up efforts to strengthen its ability to control work safety, aiming to achieve the dual objectives of ensuring a stable coal supply and establishing a safety systems at coal mines. According to the *People's Daily*, in 2005 Li Yi, director of the State Administration of Work Safety Supervision, ordered the closure of more than four thousand coal mines that were deemed to be significantly lacking in safety measures, and punished 222 officials for major accidents, including two vice governors of provinces (December 24, 2005). Of these 222, 96 officials were criminally charged.

As social contradictions such as corruption and bribery involving senior party members, and widening disparity between the rich and poor, have spread across China in recent years, “incidents caused by collective people,” particularly riots by poor farmers, migrant workers, and jobless people, have occurred frequently. According to the Ministry of Public Security, the number of “collective incidents” jumped from 10,000 in 1994 to 74,000 in 2004, and the number of people participating in them soared fivefold in the 10-year period—from 730,000 to 3.76 million. Most of the incidents are believed to have been triggered by compulsory land expropriation in farm areas by local governments. Riots were often provoked by the land expropriation methods used by local governments, which were often in violation of spirit of the central government. An analysis published in Issue 29 (July 18, 2005) of *Liaowang* [Outlook] concluded that, (1) some local governments are undemocratic in their land expropriation policy, earning profits through resale of the expropriated land to third parties, (2) standard levels of compensation are unfairly low, and (3) bureaucrats and real estate companies have colluded in profiteering. In June for example, an armed group comprising an estimated 200 to 300 people, apparently hired by the local government, attacked farmers who were staging a sit-in in Dingzhou City, Hebei Province, protesting

the lack of adequate compensation for the land taken from them, leaving at least six protesters dead. In the village of Donghua in Shanwei City, Guangdong Province, local people opposing the construction of a wind power plant clashed with armed police in December, leaving many of them dead and injured. The shooting by the armed police, the biggest crackdown by authorities on ordinary citizens since the Tiananmen Square Incident, left 20 people dead and 50 missing, according to the *New York Times* (December 10, 2005).

The Impact of the Death of Zhao Ziyang

Former CPC general secretary Zhao Ziyang died on January 17, aged 85. Yet, oddly, no official memorial service was conducted for him. When Zhao was cremated at the Babaoshan Revolutionary Cemetery in the suburbs of Beijing, some government officials, including Jia Qinglin, chairman of the Chinese People's Political Consultative Conference, attended the cremation. In an obituary, Xinhua News Agency said that comrade Zhao Ziyang had assumed a succession of key posts in the central Chinese government and the state and made a meaningful contribution to the CPC and the Chinese people. But the news agency, referring to his role in the Tiananmen Square incident, added that comrade Zhao had made a serious mistake during the politically turbulent period of the spring and summer of 1989 (January 29, 2005). In the 16 years since being dismissed from key posts, following the incident, former president Zhao remained absent from the center stage of politics. Even after death, his honor was not regained. Several newspapers linked to Hong Kong and Taiwan reported that the Chinese government severely restricted moves by people who wanted to express their condolences over Zhao's death or attend a funeral service for him. The restriction is believed to have reflected a sense of crisis by the Chinese government, which apparently tried to minimize the impact of Zhao's death by preventing protests by pro-democracy activists or other activities that might promote anti-establishment feeling. The Chinese government was not taking any chances, even after the death of an old man who had been away from the public stage for many years. This indicates a lack of confidence by the Chinese government, as the country is gripped by fears of rekindled democracy protests.

Even as it was trying to suppress anti-establishment moves by pro-democracy forces, on October 19, 2005, the Chinese government released a white paper called "Building of Political Democracy in China"—the first white paper by the Chinese government addressing such a theme. The

white paper contains a philosophical framework for political-system reforms geared to building a political democracy in China, and outlines what the government has done so far in order to achieve such a democracy. The paper says, “China’s democracy is a people’s democracy under the leadership of the CPC, a democracy of the widest scope practiced among the people, and China’s democracy is a democracy guaranteed by the people’s democratic dictatorship.” It also says, “China’s efforts to build a political democracy have yielded numerous advancements and achievements.” However, the idea of “political democracy,” as stated in the title of the white paper, is far removed from the reality of China’s current political system, in which democratization has made little progress. The term “the people’s democratic dictatorship” used in the white paper aptly reflects the reality of China’s democratic situation. Yet, by releasing the white paper, China seems to be trying to demonstrate to Europe, the United States, and rest of the international community, that it is making every effort to advance democratization. It has been suggested that one of China’s motivations in taking this initiative is to pave the way for the European Union (EU) to lift an embargo on China-bound arms exports. The EU has refused to lift it, citing the perceived slow democratization in China and the country’s human rights abuse (refer to Foreign Relations).

The Problem of Ethnic Minorities in China

The year 2005 marked the 40th anniversary of the establishment of the Tibet Autonomous Region and the 50th anniversary of the establishment of the Xinjiang Uygur Autonomous Region. When a national working conference on ethnic minorities was held on May 27, 2005, Chinese President Hu and Premier Wen called for unity of peoples and economic development in residential areas for ethnic minorities. The Tibet Autonomous Region held a celebration in September to mark the 40th anniversary of its establishment, and the Xinjiang Uygur Autonomous Region did similarly in October to mark its 50th anniversary. Both celebrations were marked by great pomp and splendor. The Standing Committee members of the Political Bureau of the CPC Central Committee visited the Xinjiang Uygur Autonomous Region one after another—Huang Ju in July, Zeng Qinghong in August, and Luo Gan in October. At a meeting of the Standing Committee of the National People’s Congress of the Xinjiang Uygur Autonomous Region at the end of July, the autonomous region’s vice chairman, Zhang Zhou, was dismissed. Under the reshuffle, Hu Wei, secretary of the Secretariat of the Central

Committee of the Communist Youth League of China, was appointed to replace Zhang.

As celebrations were taking place, speculation was rife that protesters had clashed with armed police in the Xinjiang Uygur Autonomous Region. In an apparent attempt to deny the rumors, *PLA Daily* reported that the PLA Xinjiang Military Area Command regards militias and soldiers in the reserves as an important force for maintaining the security and stability of the autonomous region (October 1, 2005). The daily also reported on the same day that of all the senior military officers of the area command, contingency troop soldiers, militias, and officers and soldiers in the reserves, not a single person had joined splintered forces or conducted nonreligious activities. However, it is difficult to feel entirely optimistic about the situation in the Xinjiang Uygur Autonomous Region, given remarks made by Wang Lequan, secretary of the CPC Xinjiang Uygur Autonomous Regional Committee, on August 25, to the effect that the Xinjiang Uygur Autonomous Region is seeing a growing presence of international terrorist organizations and increasingly violent terrorist activities. Wang also said on October 18 that 19 foreign terrorists were arrested during the period to celebrate the 50th anniversary of the establishment of the Xinjiang Uygur Autonomous Region.

Hong Kong

Tung Chee-Hwa, chief executive of the Hong Kong Special Administrative Region, resigned on March 10, despite the fact that his second term had yet to expire, citing the deterioration of his health. On the same day, he became vice chairman of the Chinese People's Political Consultative Conference. Donald Tsang Yam-kuen, administrative secretary, became acting chief executive in place of Tung. The reshuffle reflected the desires of the mainland, which was unhappy with Tung's unpopularity with the people of Hong Kong, and his incompetent policy execution, which had become increasingly clear since protesters staged a large-scale demonstration against the enactment of the state security ordinance in July 2003. On June 21, Donald Tsang Yam-kuen was formally appointed chief executive of the Hong Kong Special Administrative Region, after a unanimous election procedure. Probably because the resignation of Tung served to placate the people of Hong Kong, a street rally staged in July to mark the eighth anniversary of Hong Kong's return to the mainland was limited in scale, with only about twenty thousand people participating. Still, it was true that the Hong Kong government and the democracy camp were

divided over the reform of an electoral system. In October, the Hong Kong government announced a proposed package to reform Hong Kong's electoral system, including doubling the number of members of the Election Committee that indirectly elects Hong Kong's chief executive. Still, the democracy camp demanded complete direct election of the chief executive, putting it into direct confrontation with the Hong Kong government. This demand led to a large-scale rally of about 250,000 people in December. The Hong Kong government-proposed reform was later rejected by Hong Kong's legislature, the Legislative Council. When Chief Executive Donald Tsang Yam-kuen made an official visit to Beijing at the end of December, Chinese President Hu Jintao told him that he was satisfied with the policies of the Hong Kong government, adding that China would provide full support to the government.

Taiwan

In early 2005, Chinese President Hu Jintao, at a New Year tea party sponsored by the Chinese People's Political Consultative Conference, expressed hopes for an early resumption of dialogue with the government across the Taiwan Straits, after an effective deadlock between the two countries. Hu told the tea party that he hoped for the resumption of cross-straits dialogue and negotiations as early as possible, under the basic policy of realizing "peaceful reunification" and preserving "the one country, two systems policy," and upholding the principle of "one China." Later, one after another leaders of Taiwan's opposition parties visited mainland China. Lien Chan, chairman of the Kuomintang (KMT), visited China on April 26, and James Soong, chairman of the People First Party, visited on May 5, both meeting with Chinese President Hu. The KMT chairman's visit to Beijing led to the first KMT-CPC meeting since Taiwan's split from China. On this political development, the *Mirror*, a media organ of mainland China, reported in June 2005 that KMT Chairman Lien Chan and People First Party Chairman James Soong accepted the principle of "one China," and acknowledged the 1992 Consensus, which, according to the interpretation of mainland China, calls for China and Taiwan to maintain the principle of "one China," putting aside differences on political views. The *Mirror* also reported that the two Taiwanese opposition parties shared the idea of opposing Taiwan's independence with mainland China, enabling the KMT and the People First Party to form a strategic partnership to achieve cross-straits peace, and the happiness of people on both sides of the straits.

While the Chinese administration of President Hu Jintao welcomed the visit to Beijing by the leaders of the two Taiwanese opposition parties, this does not necessarily mean that the Hu administration has softened its stance on Taiwan. During their meeting with Hu, both Lien Chan and James Soong refrained from touching on mainland China's adoption of the Anti-Secession Law. This clearly indicates that the contact between the CPC and the Taiwanese opposition parties was made on the initiative of the mainland. The visits to Beijing by the leaders of the two Taiwanese opposition parties were prompted mainly by the intensifying political struggle between ruling and opposition parties in Taiwan, and the state of disarray of Taiwan's policy toward mainland China as the Chen Shui-bian-led administration became a lame duck. China apparently contacted the leaders of the Taiwanese opposition parties in an attempt to isolate the administration of Chen Shui-bian of the Democratic Progressive Party, a pro-independence party that has steadfastly refused dialogue with mainland China. It is difficult to rule out the possibility of Taiwanese President Chen Shui-bian taking "bold" action during the remaining period of his presidency, since he has been cornered both on the domestic and diplomatic fronts.

(by Haruka Matsumoto)

ECONOMY

The National Bureau of Statistics conducted China's first comprehensive economic census from 2004 to 2005, covering business corporations and offices in the secondary and tertiary industries. On December 6, 2005, the bureau released the outline of results of the census, and 2004 GDP figures were revised based on the census results. According to the bureau, China's GDP amounted to 15,987.8 billion yuan in 2004, an upward revision of 16.8 percent from the previously reported figure. A revision of this magnitude was rare even for China, where statistics are frequently revised. The bureau explained that the GDP figures needed to be revised mainly because the conventional method of statistical calculation did not fully reflect the performance of various kinds of service industries—a part of the economy that has advanced rapidly in recent years. In early January of 2006, the bureau released revised figures for GDP and growth rates retrospective to 1993.

Based on the results of the census, GDP for 2005 was estimated at a preliminary 18,232.1 billion yuan, equivalent to US\$2,225.7 billion after

taking account of a 2.1 percent appreciation of the renminbi against the US dollar in July (to be explained later). The figure indicates that the size of China's economy is about half that of Japan in terms of GDP, making it the world's fourth largest economy after Germany. There is still space to question the reliability of the statistics presented by the government, but China is undeniably becoming a major economic power in the world.

China maintained an impressive economic growth rate, equal to an annualized 9.9 percent in 2005, despite continued credit tightening, mainly in the first half of the year. The country's supply capacity expanded sharply due to booming investment in the real estate and material sectors, signs of adjustment loomed increasingly larger in response to the supply glut. Exports scored significant growth but imports tended to slacken. As a result, China's trade surplus in 2005 jumped 319 percent from the previous year, to US\$101.9 billion, surpassing the surplus registered by Japan. Affected by the rapid increase in trade surplus and continued influx of capital, the balance of China's foreign currency reserves amounted to US\$818.9 billion at the end of the year, a figure expected to swell further and exceed Japan's balance some time in 2006.

With China wielding a growing influence on the world economy, as it becomes a major economic power, the country's trade and investment frictions, particularly with developed countries, have intensified. An important task for China in its economic policy management is to explore ways to achieve the country's harmonious integration into the global economy, while dealing with various economic imbalances and contradictions gripping the country domestically.

Signs of Change in Economic Outlook

While the Chinese economy has been growing excessively since 2003, the government has continued to face a delicate phase in its economic management. The economic growth rate of 9.9 percent recorded for 2005 was slightly lower than the 10.1 percent (revised in line with the GDP revision) of 2004. Fixed capital formation, which had led growth on the demand side, grew by 25.7 percent in 2005, almost unchanged from the preceding year. The ratio of fixed capital formation to total GDP stood at 48.6 percent in 2005, and the absolute scale of capital formation exceeded that of Japan. Industrial production for the year showed high growth, roughly comparable to the previous year's level.

While macroeconomic statistics showed that the Chinese economy continued to grow smoothly in 2005, microeconomic indicators showed

signs of change in the year. For example, inventories grew markedly in the materials industries, such as steel, nonferrous metals, cements, and sheet glass, which had been investing heavily in plant and equipment investment since 2003. On the other hand, investment and production continued to grow sharply. In 2005, growth in steel production was similar to the previous year's levels. Output of steel by China amounted to 370 million tons in 2005, accounting for almost one-third of global production. The amount is said to have exceeded market demand by about 100 million tons, resulting in a sharp decline in prices of steel products. In response to falling steel prices, the China Iron & Steel Industry Association called for a 5 percent output cut in October for some steel items, but the appeal had little effect. Reflecting the downswing in steel product prices, profits in the materials industries grew only marginally or declined in 2005—a turnaround from the sizable profit growth of the preceding year. The auto industry continued to expand production with the number of vehicles produced by Chinese makers exceeding that by German carmakers, making China the world's No. 3, after only the United States and Japan. However, profits of Chinese automakers fell, with profit-to-sales ratio declining sharply in 2005, to below the overall average for Chinese manufacturers.

In the real estate sector, concern over excessive investment is growing. According to the February 21, 2005 issue of *Finance (Caijing)*, the Shanghai branch of the People's Bank of China (the central bank) warned in a report to the bank's head office that lending for property-related deals has expanded excessively, posing a risk that China's real estate bubble may burst. The property market in China has apparently become increasingly speculative, in view of the fact that rent increases have been smaller than property price rises. In regions like Shanghai, where speculative moves in real estate markets had started relatively early, soaring real estate prices have become a social issue. Responding to the upswing in real estate prices, the General Office of the State Council issued a notice in late March, in an attempt to gradually arrest the surge in housing prices. At meeting of its standing members in early May, the State Council studied how to restrict real estate transactions. In the first half of 2005, the central government thus furthered measures to try and take some air out of the real-estate bubble. The State Council, for example, endorsed and issued "some opinions concerning the implementation of policies to stabilize housing prices," which were put forward by seven ministries and commissions of the State Council, including the Ministry of Construction and the State Development Planning Commission.

However, in view of its consequences, this policy change in favor of slowing the real estate bubble was adopted too late. A series of tightening measures by the government, targeting the property market, significantly changed the supply-demand balance of the market in Chinese cities, particularly in Shanghai. Real estate prices in the city, which had seen smaller increases in 2004, temporarily swung upward between the fourth quarter of 2004 and the first quarter of 2005. But price growth later fell again. With property prices coming under falling pressure in the city, potential buyers have sat on the sideline, even causing prices to decline in some regions. Responding to the downswing in real estate prices, the property industry started to campaign against the government's restrictive real estate policy, arguing that excessive measures to limit property transactions are detrimental to economy. The Chinese government then softened the tightening policy and started fine-tuning relevant measures in the middle of 2005, apparently reflecting its concerns that violent fluctuations in real estate prices due to tightening would negatively affect the nation's financial sector and the economy as a whole. However, the real estate market had already shown signs that the bubble came close to bursting, such as the non-utilization rate of land plots for commercial development reaching 25 percent. According to the February 10, 2006 issue of *21st Century Business Herald* (*21 Shiji Jingji Baodao*), the effective non-utilization rates of commercial land were said to have risen more sharply than official government statistics showed. The bursting of the real estate bubble is expected to have further impact on China's property market in 2006.

The highest-priority economic management task for 2006, as defined by the Chinese government at a working conference on the economy in December—as too in the previous year—was to achieve high economic growth in a sustainable manner, and continuously curb excessive investment growth. The working conference referred to the need to heed a necessary principle for achieving this economic management policy—“keep what should be kept and curb what should be curbed”—as well as the need to move toward trying to achieve economic growth through consumption. These references indicate that the Chinese monetary authority had softened its restrictive stance on industrial activity. According to the November 7, 2005 issue of *Economic Observer* (*Jingji Guancha Bao*), there is speculation that the authority has been moving to slightly relax measures to curb lending.

Revival of Industrial Policy?

The National Development and Reform Commission was created when the State Development Planning Commission was expanded through the absorption of a part of the State Economic and Trade Commission, as part of administrative reforms in 2003. The new entity has been reinforcing its policy interference in activities for industrial development. The renewed move by the entity has come at a time when excessive corporate investment in certain sectors has been emerging. The Communist Party of China (CPC), at the Fifth Plenary Session of the 16th Central Committee in October, worked out a CPC proposal on the compilation of the 11th Five-Year Plan, as 2005 marked the final year of the 10th Five-Year Plan. The proposal would serve as a basis for a plan to be adopted by the National People's Congress in March 2006. (The word *jihua* [plan] used previously was changed to *guihua*, which means “vision” rather than “plan,” although the official English translation remains unchanged.) Reference to specific industries under the proposed 11th Five-Year Plan was very limited. Specific policies involving individual industrial sectors are to be addressed by administrative laws, rules, and guidelines being formulated mainly by the National Development and Reform Commission.

Industrial policies adopted to cover major industries included a revised auto industry policy, introduced in June 2004. The auto industry policy was followed by a steel industry development policy, which was introduced by the National Development and Reform Commission in July 2005. The steel industry development policy calls for steel manufacturers to curb production, in response to the excessive level of current investment, to promote industrial rationalization, to enhance productivity, to improve the quality of products and process technologies, and to take account of environmental effects in manufacturing activities. As in the case of the auto industry policy, the steel industry policy is restrictive, as measures envisaged under the policy include the requirement of screening and approval for new steel projects by the National Development and Reform Commission, and the effective banning of the full acquisition of Chinese steelmakers by foreign-affiliated companies. In addition, at the end of the year the National Development and Reform Commission issued an administrative notice concerning curbing of steel production, scrapping of outmoded facilities and technologies, and acceleration of structural adjustment in the steel industry. The notice called for steel production in the country to be limited to 400 million tons during the 11th Five-Year Plan period (2006–10).

On December 21, the State Council also approved and issued a tentative rule on the promotion of industry structural adjustment, which was proposed by the National Development and Reform Commission. As a principle of this adjustment, while the rule emphasizes the need to smooth basic functioning through the market mechanism of allocating business resources, it calls for “the state to optimize resource allocation further by means of rational guidance of industrial policy (Article 3).” More specifically, the National Development and Reform Commission is to take the initiative of compiling a set of guidelines on industry structural adjustment for application to discriminatory policies of taxation and investment licensing, by categorizing products, facilities, and technologies into three categories—those of which production is to be encouraged, those of which production is to be limited, and those of which production is to be terminated (Article 12 to Article 19). At the same time, the commission released specific guidelines to be used for the time being.

Thanks to administrative reforms, the National Development and Reform Commission has been able to regain the control over industrial policy given to it when it was called the State Planning Commission. At a time when the problems of excessive investment and production have become more visible, the National Development and Reform Commission has again shown its willingness to interfere in microeconomic activities. However, in view of China’s past handling of industrial policy, almost all administrative interventions made for the purpose of adjusting supply-demand balances and economies of scale are soon swept away by the dynamism of market forces. In order to remedy the tendency of excessive investment, which is a chronic problem for China, the country has no option but to transform its financial system, which plays the role of resources allocation, into a market-based system, and to introduce a mechanism that can end inefficient resources allocation.

Currency Reform and Revaluation of the Renminbi

On the trade front, China’s import growth slowed significantly in the first quarter of 2005, affected by restrictive policy and changes in the domestic market. On the other hand, exports grew sharply, resulting in the country’s trade surplus surging to US\$16.5 billion as of the end of the first quarter—an amount that represents close to half of its trade surplus for all of 2004. In view of these circumstances, Japan, the United States, and Europe urged China to reform its currency system as soon as possible. In the United States, the political community accelerated moves to link

China's swelling trade surplus with the problem of the renminbi, including congressional moves to push the so-called Schumer Graham bill, which would impose a uniform 27.5 percent punitive tariff on Chinese imports unless Beijing drastically reforms its currency system (refer to the next section).

Meanwhile, when Premier Wen Jiabao unveiled three principles for the reform of the renminbi at an Asia-Europe Meeting (ASEM) of finance ministers in late June, the Chinese government encountered international pressure, from Japan, Europe, and the United States. These principles are: (1) China will decide reforms of the Chinese exchange rate system by itself, (2) reform decisions are to be made in a controlled manner, and (3) time will be taken to implement reforms (*Nihon Keizai Shimbun*, June 27, 2005). On the evening of July 21, however, the People's Bank of China announced a set of measures to reform its currency rate regime—a move that surprised global financial markets. In a public notice, the Chinese central bank said it would revalue the exchange rate of the renminbi to 8.11 to the US dollar, amounting to a 2.1 percent appreciation of the Chinese currency. The central bank also announced it would adopt a managed floating rate system that uses a basket of currencies as a reference for the renminbi exchange rate (Table 6.1). The margin of revaluation was very small, but Chinese monetary authorities effectively ended the pegging of the renminbi to the US dollar. The possibility of the renminbi fluctuating more against the US dollar increased, in view of the declaration by the central bank that “the renminbi exchange rate regime will be improved with greater flexibility,” with consideration to the renminbi's value relative to other key currencies. In August, People's Bank of China Governor Zhou Xiaochuan said currencies making up the “basket” in the new exchange rate regime are the US dollar, euro, yen, and won. However, the governor also pointed out that using a basket of currencies as a reference does not amount to tying the renminbi to a basket of currencies, suggesting that the basket is only a reference for deciding the yuan's exchange rate.

Since the reform of the foreign exchange rate system, the yuan has been gradually appreciating against the US dollar in inter-banking trading (Figure 6.1). The margin of revaluation between July 22, a day after the public notice was announced, and December 31 was only 0.5 percent, but the yuan's appreciation against the US currency apparently showed some upward momentum during November and December. During this period, Chinese monetary authorities took a series of additional measures to

Table 6.1. Public Announcements of the People's Bank of China on Reforming the Renminbi Exchange Rate Regime

(preamble omitted)

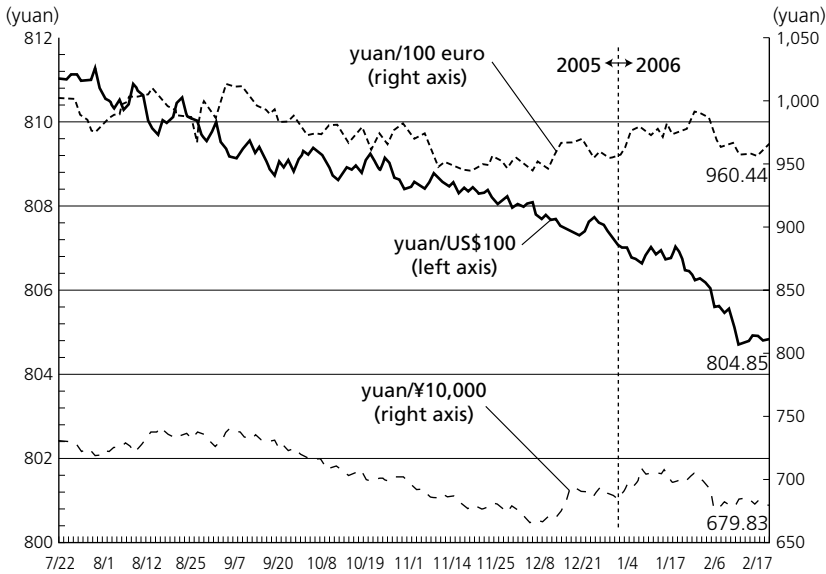
1. Starting in July 21, 2005, China will reform its exchange rate regime, by moving to a managed floating exchange rate regime based on market supply and demand, with reference to a basket of currencies. The renminbi will no longer be pegged to the US dollar and the renminbi exchange rate regime will be improved with greater flexibility.
2. After the closing of the market on each working day, the People's Bank of China will announce the closing price of the US dollar and other foreign currencies traded against the renminbi in the inter-bank foreign exchange market, and will make this the central parity for trading against the renminbi on the following working day.
3. The US\$-renminbi exchange rate will be adjusted to 8.11 yuan per US dollar at 19:00 hours on July 21, 2005. The adjusted quote will be used as the central parity for the US dollar's trading against the renminbi between foreign exchange—designated banks in the inter-banking currency market on the following working day. (remainder omitted)
4. The daily trading price of the US dollar against the renminbi in the inter-bank foreign exchange market will be allowed to continue floating within a band of ± 0.3 percent around the central parity published by the People's Bank of China. (remainder omitted)

The People's Bank of China will adjust the renminbi exchange rate band when necessary, according to market development, and the economic and financial situation. The renminbi exchange rate will be more flexible, since it will be based on market conditions, with reference to a basket of currencies. The People's Bank of China is responsible for maintaining the stability of the renminbi exchange rate at an adaptive and balanced level, so as to promote a basic equilibrium of the balance of payments, and to safeguard macroeconomic and financial stability.

Source: Website of the People's Bank of China (<http://www.pbc.gov.cn/>).

reform the exchange rate system. Among them were the introduction of a market-maker system for inter-banking trading, the creation of a currency futures market, the expansion of a maximum allowable fluctuation range for exchange rates offered by banks to general customers, and the scrapping of a maximum allowable currency fluctuation range in trading of

Figure 6.1. Movement of the Renminbi (after July 22/median rates released by the People's Bank of China)



Source: Website of the State Administration of Foreign Exchange. <http://www.safe.gov.cn>.

currencies other than the US dollar. In the future, the authorities are likely to expand the permissible fluctuation range for the yuan on currency markets, and tolerate a gradual acceleration in the yuan's appreciation against the US dollar, while keeping a close tab on domestic economic developments and external relations.

Intensification of Trade Friction

Trade friction between China and developed countries over textile products intensified in 2005. Export quotas for US- and European-bound Chinese textile products were scrapped at the end of 2004 in line with World Trade Organization (WTO) agreements. But by the time the quotas were removed, textile trade friction had already intensified between China, and the United States and Europe. Following the scrapping of the export quotas, China imposed a unit tax on shipment of 31 major textile products on January 1, in an attempt to block moves by the United States and Europe to introduce measures to restrict trade. Despite the tax, growth in textile exports from China to the United States and Europe was far higher than projected at the beginning of 2005. The surge occurred

mainly because the United States and Europe postponed the scrapping of the export quotas for most product items until the end of 2004, although WTO agreements say that a quota system must be abolished in phases. US-bound exports of major textile items rose sharply, with shipments of cotton shirts and jackets jumping 1,250 percent from the year before, shipments of cotton pants 1,500 percent, and shipments of cotton and synthetic fiber underwear 300 percent (based on Chinese customs-clearance statistics. *Economic Observer* [Jingji Guancha Bao], April 11, 2005).

In response to a sharp increase in textile imports from China, the United States and the European Union (EU) further stepped up protectionist moves. Acting on a request filed by textile producers within the common market, in April the EU released a set of guidelines on the use of a safeguard aimed at targeting EU-bound Chinese textile products. The guidelines called for the EU to begin investigation on whether to invoke safeguard measures when the increase in Chinese textile imports into Europe reaches a specified level. The moment the guidelines were announced, the EU launched safeguard investigation into nine items imported from China, including sweaters, pants, and white shirts. Meanwhile, the United States decided to invoke safeguard measures against seven textile items from China, including sweaters, pants, and white shirts, to limit growth in imports of such items to 7.5 percent.

China expressed opposition to these trade restrictions by the United States and Europe. At the same time, however, in an apparent bid to ease trade frictions, on May 20 Beijing voluntarily announced a substantial increase in the tax on 74 textile items shipped from China, effective June 1. Despite these self-restraint efforts by the Chinese, the United States did not remove the safeguard measures against the seven items, while the EU continued its safeguard investigations into textile imports from China. Reacting strongly against the tough stance of the United States and the EU, China reversed the self-imposed export-tax hike just 10 days after it was implemented. Reflecting uncertainty over the outcome of trade disputes involving the three parties, moves to refrain from buying Chinese textile products spread throughout the United States and Europe, dealing a severe blow to Chinese textile makers, particularly small- and medium-sized companies.

In an attempt to break the deadlock, China began separate textile-trade negotiations with the United States and the EU in pursuit of compromise deals. Negotiations with the EU progressed relatively quickly, resulting in an agreement on June 10, calling for China to set a provi-

sional export limit for 10 major textile items, effective until the end of 2007. At the same time, the EU was to end safeguard investigation into these items. According to a memorandum exchanged between China and the EU as part of the compromise agreement, growth of EU-bound shipments of the 10 specified textile products would be limited to 8 percent to 12.5 percent per year in the prescribed period. The memorandum also called for the EU to refrain from taking safeguard measures against other Chinese textile products under its safeguard clause on Chinese textile imports. The EU side was believed to have taken a cautious stance in its negotiations with China, in view of a divergence in textile-trade policies amongst EU member countries. Southern European countries like France and Italy gave priority to protecting domestic textile industries, while Scandinavian countries were more willing to buy cheaper Chinese products (*Finance [Caijing]*, June 13, 2005). Soon after the memorandum was exchanged, the volume of textile imports for several items from China had already reached limits set for 2005 by August. As a result, a large volume of Chinese products were rejected by customs-clearance offices, and left to pile up at European ports. Meanwhile, distribution businesses in Scandinavian countries demanded the removal of the EU-imposed import restrictions step for Chinese textile products, highlighting a deepening confrontation between EU member countries due to conflicts of interest (*21st Century Business Herald [21 Shiji Jingji Baodao]*, August 29, 2005).

China also held textile trade negotiations with the United States, seeking to strike a compromise deal similar to that it concluded with the EU. However, talks did not proceed smoothly, due to a wide gulf between the two countries. In early November, the two parties finally struck a deal and exchanged a memorandum under which maximum import growth rates for 21 mainstay textile products from China were set at 10 percent to 17 percent per year, for the period from January 2006 to the end of 2008. As in the case of the EU, the memorandum also called for the United States to refrain from applying safeguard clause measures to other textile imports from China.

How textile trade friction with the United States and the EU unfolds is very important to the Chinese textile industry, since the US and European markets account for about 30 percent of all textile products shipped from China. China managed to avoid an immediate crisis due to the compromise deals with the United States and the EU, but many uncertainties will reemerge when the deal with the United States expires at the end of 2008. US and European textile distributors have been moving to diversify their

product sourcing in light of the business risks associated with importing only from China (*Asian Wall Street Journal*, July 28, 2005).

Bargaining over Investment for Natural Resources Development

China also encountered some trade friction with the United States in relation to investment for natural resources development. In view of its increasing reliance on imports of mineral resources such as oil, China's major state-run natural resources and materials enterprises have stepped up efforts to secure supplies of natural resources through mergers and acquisitions, and capital investment, with the support of the Chinese government.

The case attracting the greatest media attention was an offer made by China's CNOOC in June to buy out US oil company Unocal. CNOOC offered a staggering bid price of US\$18.5 billion for Unocal, exceeding a price offered by Chevron, which was also seeking to purchase the US company. The Chinese move became a political issue in the United States, however, because some critics considered it a threat to the United States' security in natural resources supply. Finally, CNOOC was forced to end their buyout negotiations with Unocal, resulting in the company being bought by Chevron for US\$17.7 billion. CNOOC later stated that it had to give up the proposed deal due to political pressure from Washington (*The Nikkei*, August 3, 2005). In light of the fact that Unocal produces only 1 percent of all crude oil and petroleum gas produced in the United States, some observers suggested that blocking a purchase of the company by Chinese interests on the grounds of the possible effects to resources security was irrational (Johan Norberg, "China Paranoia Derails Free Trade," *Far Eastern Economic Review*, January-February 2006).

Meanwhile, China National Petroleum Corp. (CNPC), the largest oil company in China, succeeded in buying PetroKazakhstan of Canada for US\$4.18 billion at the end of October. Behind the deal was the mediation of the Chinese government between CNPC and China Petrochemical and Chemical Corp. (CINOPEC), another Chinese petroleum giant that had also been eager to purchase PetroKazakhstan. It was believed that the Chinese government persuaded CINOPEC to refrain from participating in the tender to buy PetroKazakhstan (*Finance [Caijing]*, February 6, 2006).

The Chinese government, in partnership with state-owned companies, has accelerated efforts to acquire oil concessions overseas and deepen relations with oil-producing countries, in a bid to expand the

potential sources from which it can directly buy oil resources. China's moves to approach Syria, Sudan, and Iran, countries hostile to the United States, are believed to be part of this strategy, making Americans wary of such developments.

Advancement of China's Financial Reform

A major factor behind the surge of investment in China in recent years has been the delayed efforts by the Chinese banking sector—the Big Four state-owned banks—to shift to a market-based economy. In view of the planned abolition of rules limiting foreign capital investment at the end of 2006, China needs to urgently reform its domestic banking sector, so that banks can operate in a more efficient manner. Apparently mindful of the need for such reform, the Chinese government has been transforming state-owned banks into listed stockholding companies, and pushing for capital investment by foreign entities, particularly major financial institutions.

China Construction Bank and the Bank of China, both of which became stockholding companies in 2004, have promoted organizational reforms with an eye to getting their stocks listed on overseas stock markets. China Construction Bank faced a serious scandal in March, when its president Zhang Xizhao was dismissed due to allegations of taking bribes. Yet the bank was able to receive an additional 65.5 billion yuan in capital injection thanks to reinvestment by Central Huijin Investment Co., an entity charged with managing state assets in the financial sector, and income tax returns. In addition, China Construction Bank succeeded in getting the Bank of America and Temasek Holdings, an investment company affiliated with the government of Singapore, to acquire 8.379 percent and 6.125 percent equity stakes in the bank, respectively. The capital injection helped put the state-owned bank on a sound financial footing, enabling it to get listed on the Hong Kong stock market at the end of October. This stock offering raised a remarkable HK\$62.2 billion, making it the most lucrative public offering of shares since 2002. Meanwhile, the Bank of China, another state-owned bank, reached a broad agreement on capital investment with the Royal Bank of Scotland (RBS) and Temasek Holdings. However, the bank was not able to complete its restructuring, and it failed to go public within the year. This was because it took longer than expected for Central Huijin Investment to coordinate the investment deal, which required agreements on capital investment ratios by each party, and per-share purchase prices.

The Industrial and Commercial Bank of China, the largest bank in China, restructured its assets by separating or disposing of nearly 800 billion yuan in nonperforming loans and quasi-nonperforming loans, after receiving a US\$15 billion capital injection from Central Huijin Investment in April. As a result, the bank successfully transformed itself into a stockholding company. In a bid to catch up with the Bank of China, the Industrial and Commercial Bank of China has been in negotiations with several foreign-affiliated companies, seeking capital investment from institutional investors, mainly major foreign-affiliated financial institutions. It aims to go public in 2006.

Shares of China Construction Bank rose after they were listed on the Hong Kong stock market, earning the foreign companies that invested in the bank substantial capital gains, as the market price of shares topped their purchasing price. If listed on a stock market, shares in the Bank of China are likely to rise just as those of China Construction Bank did, triggering criticism by some media that the move is tantamount to selling shares of domestic Chinese banks to foreign-affiliated companies at bargain prices. But the China Banking Regulatory Commission dismissed such criticism and emphasized its policy of continuing to promote capital investment in Chinese banks by foreign-affiliated institutional investors. The commission argued that the policy would not lead to bargain selling of Chinese banks to foreign interests, due to a set of safeguard measures, including the minimum level of foreign ownership at 5 percent and an obligation for investors to keep shareholdings for at least three years.

The realignment of state-owned Chinese banks has progressed thanks to the huge financial backing of the central Chinese government, although the problem of how to restructure the Agricultural Bank of China, which has been saddled with a remarkably high level of nonperforming loans, remains. Medium-sized banks and regional banks have also stepped up efforts to absorb foreign capital investment. However, the motives of the foreign investors and the Chinese government and banks are slightly different. The former are seeking to reap the fruits that should come with growth in the Chinese financial services market, while the latter are looking to acquire the advanced technology, financial expertise, and experience of the investing companies, while retaining control of the banks' management.

The Chinese Stock Market at a Crossroads

Stock markets in China have remained in a slump since its tumble in June

2001, which was triggered by the government's policy of unloading its holdings in state-owned entities. On the evening of April 29, the China Securities Regulatory Commission released a public notice regarding issues related to the pilot split share structure reform of listed companies. Based on the notice, the commission began to implement the split share structure reform, involving the conversion of non-tradable shares, such as state-owned stocks and corporate stocks, into tradable shares.

The Chinese government learned its lesson from the unsuccessful release of shareholdings in 2001, and so the public notice included a set of conditions that must be met before approving a proposal to convert non-tradable shares into tradable shares. Under one condition, major shareholders of a listed company (entities owning non-tradable shares such as the government and state-owned companies) are to convene an extraordinary general shareholders meeting to propose a motion for converting non-tradable shares into tradable shares. The motion will be adopted if it receives support from at least two-thirds of shareholders participating in the meeting, and support from at least two-thirds of holders of non-tradable shares participating in the meeting. Another condition is that originally non-tradable shares shall not be traded on the stock market within 12 months of the date of implementation of the plan to convert them into tradable shares. Under this public notice, tough measures were imposed to restrict the sale of shares by major shareholders after the reform plan is completed, in order to address concerns by general investors over possible drastic changes in supply-demand relationships in stock markets. Among these measures is a rule stating that a former non-tradable shareholder who holds more than 5 percent of the total shares of a listed company may sell their shares, up to a maximum of 5 percent of the total shares of the listed company within 12 months after the expiry of the one-year lock-up period, and not more than 10 percent of total shares within 24 months. In line with the conversion of non-tradable shares into tradable shares, former tradable shareholders are subject to preferential treatment, including free allocation of a specified proportion of shares.

The China Securities Regulatory Commission designated four companies for the first-phase pilot reform project and 46 companies for the second-phase pilot reform project. Based on the results of implementation of these reform projects, the commission issued rules and regulations in September to govern the split share structure reform of listed companies. According to a policy unveiled under these rules, the commission's reforms will start being applied to companies that promptly meet certain

conditions. Moves to reform the split share structure of listed companies picked up momentum following the introduction of these rules and regulations. By early 2006, 434 companies embarked on the reform, accounting for almost 40 percent of combined market capitalization of all companies traded in Shanghai and Shenzhen markets. If reform is to continue at the current pace, all listed companies will have completed the reform by the end of 2006.

Securities markets initially reacted coolly to moves to reform the split share structure for listed companies. Share prices in China continued to fall, leaving the Shanghai Stock Exchange (SSE) in a crisis situation after the benchmark SSE Composite Index fell below 1,000 for the first time in eight years in early June. In response to this situation, Chinese securities authorities declared that they would suspend the issuing of new shares for new public offerings and capital increases for the time being. The authorities also worked out a barrage of other measures, including granting companies full or partial exemption from revenue-stamp duty and income tax, and allowing companies to purchase their own shares. Following the implementation of these measures, stock prices oscillated up and down sharply between July and November, but after December they tended to rise. It was said that behind the recovery were moves by qualified foreign institutional investors (QFII) or overseas investors qualified to trade in Chinese markets (32 foreign firms were designated as QFII as of the end of 2005) to build up investments in renminbi-quoted “A stocks,” centering on stocks of companies that completed the split share structure reform. Yet the total investment quota allotted to QFII was worth just a little over US\$5.6 billion as of the end of the year, accounting for a marginal 4.3 percent of total market capitalization of all tradable shares. Thus, the major players responsible for the recovery of Chinese stocks must have been domestic Chinese capitals, which followed the lead of QFII companies in returning to stock markets. How overall stock prices in China will be affected when the conversion of state-owned and corporate shares from non-tradable issues to tradable issues is completed, as expected, is a question worthy of attention.

Moves to Reform Corporate Systems

At the 18th meeting of the Standing Committee on October 27, the National People’s Congress passed and promulgated an amendment to the corporate law, effective on January 1, 2006, marking the first sweeping overhaul of the law since it was established in 1993. The revised law pro-

vides for a substantial reduction in the minimum capital required for setting up a business corporation, allows the establishment of single-person companies, adopts the principle of general incorporation, adopts the doctrine of piercing the corporate veil, and introduces rules on lawsuits by shareholders. The new corporate law is aimed at providing greater flexibility in establishing a company, while improving corporate governance systems. Along with the revision to the corporate law, the securities law was also comprehensively revised.

On corporate reform, the Communist Party of China (CPC) and the Chinese government have adopted a two-pronged policy—promoting the development of the private sector, and reorganizing major state-owned enterprises. On January 12, the Standing Committee of the State Council adopted in principle “some opinions on encouraging, supporting and guiding the development of non-public economic activities such as those by individuals and private companies,” and on February 24 it promulgated and released the full text of the opinions. The “opinions” allow private-sector companies to invest in all industrial sectors, excluding areas where business activities by private companies are banned or limited by law. As a result, private companies are now able to invest in the public-sector services, infrastructure-related business, financial operations, military business, and other areas that had been previously reserved for state-owned enterprises. The “opinions” also encouraged the use of private-sector capital in the realignment of state-owned companies and collectively owned companies.

The State-owned Assets Supervision and Administration Commission of the State Council, which is in charge of supervising operations of corporations under the State Council, emphasized the policy of promoting further realignment of state-owned companies. At a meeting in September of leaders of state-owned companies under the jurisdiction of the State Council, Li Rongrong, chairman of the commission, unveiled a plan to trim the number of such state-owned companies from the current 169 to about 80–100 in the immediate future (*21st Century Business Herald* [21 *Shiji Jingji Baodao*], September 29, 2005). The State-owned Assets Supervision and Administration Commission of the State Council viewing Tamasek Holdings, an entity affiliated with the government of Singapore, as an ideal model, envisages eventually streamlining state-owned companies under its control into scores of corporate groups, operating mainly in sectors vital to the national economy and national security.

The scrapping and realignment of major state-owned companies is a reasonable policy choice in terms of increasing the efficiency of invest-

ment of state-owned assets. But it is quite likely that such a policy will help to strengthen market control or monopolization by a small number of companies. Therefore, a major challenge likely to face the Chinese government in steering its corporate policy is how to strike a balance between two major policy objectives—expediting competition by encouraging the entry of private companies into formerly state-run businesses, and streamlining large state-owned enterprises.

Agricultural Issues and the Abolition of Agricultural Tax

In early 2005, the Central Committee of the Communist Party of China (CPC) released a public notice in which it stated that China would maintain its policy of trying to raise the income of agricultural households. However, income growth slowed in 2005 with food supply-demand ties softening due to a good harvest. This was in contrast to the increase in farm household income in the preceding year, attributable to higher food prices. In 2005, the income of urban households grew sharply, causing the income disparity with farmers to increase to 3.22:1, the largest gap since China adopted its reform and opening policy (*21st Century Business Herald* [21 Shiji Jingji Baodao], December 1, 2005). In view of these circumstances, the Fifth Plenary Session of the 16th Central Committee of the CPC put forward a slogan calling for the building of new socialist agricultural society in the proposal on the 11th plan (refer to “Revival of Industrial Policy?”). The proposal focuses on improving farm-related institutional systems, through measures to boost public works projects in agricultural districts, to promote modernization of farm businesses, and to permit the sale of tenancy rights of farmland on secondary markets. At a working conference on agricultural affairs at the end of the year, the Central Committee pushed anew its slogan of promoting the building of a new socialist agricultural society, and emphasized the policy of expanding fiscal money supply for the prosperity of agricultural areas.

China has been abolishing agricultural tax in a phased manner since 2004 in order to alleviate the tax burden on farmers. By the end of 2005, 28 provincial governments had abolished the tax. In the three remaining provinces of Hebei, Shandong, and Yunnan, state-designated poor prefectures repealed the tax. As a result, revenues from the collection of agricultural taxes plunged from 23.2 billion yuan in 2004 to about 1.5 billion yuan in 2005, leading the central government to provide 66.4 billion yuan in subsidies to provincial governments. However, the subsidies fell far short of the 160–180 billion yuan, the minimum amount believed neces-

sary for provincial governments across the nation to maintain public services in farm areas. Therefore, the transfer of fiscal money from the central government to provincial governments in the form of subsidies can make up for only a marginal portion of public services in agricultural areas (*Finance [Caijing]*, March 7, 2005). As a result, village and town governments and village-level committees suffered serious budget shortfalls. Following the abolition of agricultural tax, people in some farm areas have been informally ordered to start paying for public services such as education, health, and medical services. Another problem faced by farm villages after the repeal of the tax is the difficulty of finding people to work as ranking village officials, because the debt-ridden state of villages makes potential officials reluctant to work as public servants. To compensate for loss of agricultural tax, various charges are being imposed on activities in farm areas, such as migration by farmers to other areas for work, marriage registration, and the building of a new house. Furthermore, many villages and town governments have continued to levy agricultural tax even after their provincial governments declared the repeal of such a tax (*Finance [Caijing]*, February 6, 2006). Also attracting media attention is the issue of debts accumulated by town and village governments. The total debts of village and town governments across China is said to be approximately 600 billion yuan at present. Some critics are concerned that if unable to handle such debts appropriately, village and town governments may use grants from the central government to finance debt repayments.

As part of agricultural reform following the scrapping of farm tax, the Chinese government has adopted the policy of using larger state and provincial budgets to finance compulsory-education services in farm areas, previously operated largely by money put up by farm households on their own. According to a working report presented to the government in March 2005, children and students from poor households living in poor districts were to be exempt by the end of the year from paying expenses for textbooks and educational materials, and other miscellaneous expenses, and such households were to receive subsidies for accommodation-related expenses. These measures are to expand within three years to cover all elementary school and junior high school students from poor farm households across the nation (*Nanfang Weekly [Nanfang Zhoumo]*, March 10, 2005). The Ministry of Finance of the State Council has set up a project team to study ways to realize financial reform of compulsory education services in agricultural areas. But in view of the fact

that many municipal governments have been saddled with large debts, there is a fear that proceeds from additional investment by the central government for education-related financial reform may be used for debt repayments. At the 19th meeting of the Standing Committee of the 10th National People's Congress, China formally decided to abolish an ordinance on agricultural tax, effective on January 1, 2006. But whether the abolition, an innovative step for China, will surely improve welfare of agricultural households in the future depends largely on the progress of financial reform and administrative-office reform. The CPC and the Chinese government have been stepping up efforts to solve farm-related issues. But it is clear that what is most important to increasing the income of the agricultural populace is job creation in the urban industrial sector. Pay for migrant workers has been rising since around 2003, when labor supply-demand relations tightened in China, particularly in coastal industrial areas.

Economic Relations between Japan and China

Trade between Japan and China has expanded, reaching US\$189.4 billion in 2005. But trade growth in the year declined from the previous year, both in exports and imports. In particular, Japan-originated import growth slowed substantially, falling 8.9 percent from the preceding year in US dollar terms, due to sluggish shipments of semiconductors, production facilities, and finished automobiles. The decline in trade was attributed to two factors—sluggish demand growth in domestic markets and expanded production by Japanese carmakers in China. In 2005, Japan's trade deficit with China amounted to an all-time high of US\$28.7 billion, according to the website of the Japan External Trade Organization (JETRO). Slowing growth in exports to China and expanding trade deficits were seen not only in Japan but also in the United States and the EU.

Boycotts against Japanese products were called for in anti-Japanese demonstrations staged in April. But the losses sustained by Japanese businesses because of the boycott were limited. Also, enthusiasm by Japanese companies to invest in China has remained strong. However, if the souring in relations between Japan and China on the diplomatic and trade fronts persists, negative economic effects are likely to emerge.

(by Kenichi Imai and Mami Yamaguchi)

FOREIGN RELATIONS

China has pushed for diplomacy aimed at promoting multilateral cooperation, by taking part in international frameworks, including the Shanghai Cooperation Organization (SCO) and the first East Asia Summit (EAS), as well as six-party talks on North Korea's nuclear program. On bilateral relations, ties with Japan have deteriorated markedly, as seen in anti-Japanese demonstrations. On relations with the United States, China tried to build cooperative ties through a summit between the leaders of the two countries, and strategic dialogue, although Beijing has remained critical of the unilateralism of the Bush Administration. In addition, China has been promoting strategic partnerships with Russia and European countries.

Japan-China Relations Cooler than Ever

In 2005, relations between Japan and China deteriorated beyond the so-called “cool politically, hot economically”—an expression often used to describe the relationship between the two countries. On April 2, scores of young Chinese broke into a Japanese-affiliated supermarket outlet in Chengdu to protest against Japan's bid to become a permanent member of the UN Security Council. The assault sparked anti-Japanese demonstrations across China, including an April 9 rally staged in Beijing by about ten thousand people, during which rocks were hurled at the Japanese Embassy. On April 16, tens of thousands of people participated in an anti-Japanese demonstration in Shanghai, during which the Japanese consulate was damaged by rock-throwing, and many Japanese-affiliated retail stores were destroyed.

The Chinese government officially opposed the staging of anti-Japanese demonstrations but continued to assert that such incidents resulted mainly from then Japanese Prime Minister Junichiro Koizumi's visits to Tokyo's war-linked Yasukuni Shrine and the Japanese government's screening of history textbooks. The Ministry of Foreign Affairs of China stated on April 13 that demonstrations were voluntary actions by Chinese citizens who were discontented with the mishandling by the Japanese side of history issues, including the invasion of China. The ministry also said the Chinese government could not support the radical actions of protesters, and it continued calling for restraint. The ministry also said that Japan was responsible for this deterioration of Japan-China relations and that therefore Japan should reflect on its conduct. Referring to Japan's bid to obtain a permanent seat at the UN Security Council,

Chinese Premier Wen Jiabao said on April 12 that only a country that respects history and takes responsibility for it can win the confidence of the people of Asia and the rest of the world, and play a larger role in the international community. The Chinese side was apparently trying to block Japan's bid to become a permanent member of the UN Security Council by making Japan's handling of history an international issue.

During his meeting with Chinese Foreign Minister Li Zhaoxing on April 17, Japanese Foreign Minister Nobutaka Machimura demanded that China apologize to Japan over violence by protesters and that it provide compensation for the damage caused to Japanese property in China. But Chinese Foreign Minister Li did not comply with the demands. On April 23, Japanese Prime Minister Junichiro Koizumi and Chinese President Hu Jintao held a summit in Indonesia on the fringes of a ceremony marking the 50th anniversary of the foundation of the Asian-African Conference. Chinese President Hu made a five-point proposal for the advancement of Japan-China relations. Meanwhile, Japanese Prime Minister Koizumi asked China to show an "appropriate response" to the consequences of anti-Japanese demonstrations, although he refrained from explicitly demanding compensation for the damage caused by the demonstrations. But Chinese President Hu did not offer an apology. Hu's consideration for the general feelings of the Chinese people was apparently behind Beijing's tough stance against Japan, as displayed on a series of occasions, including the summit meeting with Koizumi. Chinese people staged anti-Japanese rallies bearing slogans of patriotism. And education to promote patriotic sentiments in the Chinese people was promoted by none other than the Chinese government. The Chinese government thought that directly criticizing anti-Japanese demonstrations would be seen as contradicting its own policy toward Japan. Thus, the government initially took the position of giving tacit approval to the moves. The government's inaction in opposing the moves resulted in continued demonstrations that showed no signs of abating. On the other hand, moves to stage rallies against Japan spread further via the Internet. In Shanghai, the city government issued a preemptive warning that it would prohibit citizens from participating in protests, but tens of thousands of people staged anti-Japanese rallies, defying the warning.

As soon as the rally in Shanghai was staged, the Chinese government started taking comprehensive measures to prevent the further spread of demonstrations. Chinese authorities finally budged for political reasons—they were concerned that forces organizing rallies might link up with

forces dissatisfied with government policy, in relation to social contradictions such as the growing disparities between rich and poor. The authorities feared that these forces would become organized and initiate riots, possibly shifting their target of criticism to the current Chinese government and leading to calls for democratization. Thus a sense of crisis in fear that this worst-case scenario might eventuate has persisted strongly within the Chinese government. Anti-Japanese demonstrations receded by the end of April due to the Chinese government's efforts to crack down on violent actions. But the Chinese government is believed to have been severely damaged by the fact that demonstrations spread across the nation via the Internet, and in Shanghai, an area of concentrated foreign investment, the local municipality had a hard time coping with demonstrators appropriately.

China's relations with Japan have been further strained due to the issue of Japanese Prime Minister Junichiro Koizumi's visits to the war-linked Yasukuni Shrine—a long-time source of contention between the two countries. On May 16, Prime Minister Koizumi told the Budget Committee of Japan's House of Representatives that he has no reasons to stop visiting the Yasukuni Shrine. The remark prompted Chinese Vice Premier Wu Yi to abruptly cancel her scheduled meeting with Koizumi in Japan, citing urgent public duty in China. She promptly returned home, although she did meet with Japanese business leaders. During the shrine's autumn-festival period on October 17, Koizumi visited the Yasukuni Shrine, marking his fifth visit there since taking office in 2001. Following the visit, the Chinese government notified Japan that Japanese Foreign Minister Nobutaka Machimura's visit to China from October 23, and his scheduled meeting with the Chinese Foreign Affairs Minister would be postponed. In addition, China decided not to hold its leader's meeting with Koizumi on the fringes of the East Asia Summit. The meeting between Koizumi and the South Korea leader on the sidelines of the East Asian Summit was also scrapped due to Koizumi's Yasukuni visit. Chinese Ambassador to Japan Wang Yi said on November 16 that the summit meeting between Japan and China would not be resumed until the dispute over the Yasukuni Shrine is resolved. But the Japanese government's position on the issue has remained unchanged, with each party's argument failing to find compromise.

Japan and China held subcabinet-level talks to solve the dispute over natural gas development in the East China Sea in May 2005 and September 2005, however, the talks made little progress. Defying repeated

requests by the Japanese government for restraint, China began pumping natural gas in the Tianwaitian field in the East China Sea in late September. As a countermeasure, Japan has started procedures to grant private-sector companies rights to exploit gas fields in the East China Sea. However, digging on a trial basis has yet to begin. Meanwhile, China, in a sign of intimidation, deployed a warship in waters near the gas field in question. In October, the Japanese government proposed that the two countries jointly explore natural gas on both sides of what Japan claims to be the median line that separates the two countries' exclusive economic zones in the East China Sea. But China has sounded reluctant toward the Japanese proposal. While Japan-China ties later worsened after Japanese Prime Minister Koizumi visited the Yasukuni Shrine, China completed the construction of a pipeline linking mainland China and natural gas fields.

China's Xinhua News Agency reported on December 20, 2005, that the soured political relations between Japan and China due to Koizumi's Yasukuni visit were also hurting their economic relations. In 2005, relations between the two countries changed from "politically cool and economically hot" to "politically cool and economically cool," according to the news agency. Relations have deteriorated so much that they are now seen as entering their "coldest period" since the two countries normalized diplomatic relations in 1972.

China's Diplomatic Efforts to Arrange Resumption of Six-party Talks

Six-party talks on North Korea's nuclear program have effectively come to a halt since Pyongyang declared on February 10 that it has possessed a nuclear weapon and that it would suspend participation in the six-part talks indefinitely. The declaration came in the wake of ongoing coordination between the United States and China to pave the way for the resumption of the talks. Following the development, China, which has chaired the multilateral conference, began to work aggressively to persuade North Korea to return to the negotiation table. Wang Jiarui, Head of the International Liaison Department of the CPC Central Committee, visited North Korea and met with General Secretary of the Korean Workers' Party Kim Jong Il in Pyongyang on February 21. Wang presented to Kim Jong Il a message from CPC General Secretary Hu Jintao saying that resolving the issue of North Korea's nuclear program through six-party talks would serve the fundamental interests of both China and North Korea. Kim Jong

He told Wang that North Korea would not withdraw from the framework of the multilateral talks and is prepared to return to the talks if conditions are met. During the Kim-Wang meeting, the Chinese side is believed to have expressed its readiness to substantially increase oil supplies to North Korea—after shipments were cut sharply following Pyongyang's nuclear weapon declaration—if the North returned to the six-party negotiations. On March 23, CPC General Secretary Hu Jintao held talks with visiting North Korean Deputy Premier Pak Pong Ju in China, and confirmed the friendly relationship between China and North Korea. Hu then told Pak that Beijing is ready to play a constructive role in making the Korean Peninsula free of nuclear weapons.

The US government has placed high expectations on China, North Korea's closest ally and strongest supporter, to play a role in helping resume six-party nuclear talks. These expectations were highlighted during two of US Secretary of State Condoleezza Rice's visits to China, in talks with Chinese leaders regarding the resumption of the multilateral talks. During the bilateral summit held in September and November, between which six-party talks took place, the US and Chinese leaders agreed that the two countries would strive to make North Korea dismantle nuclear weapons through the framework of six-party talks. The United States asked China to use its influence on North Korea, including the threat of economic sanctions, as much as possible, to realize the resumption of the six-way talks. But China's policy toward the North Korean nuclear issue was believed to be slightly different from the policy by the United States. Christopher Hill, US Assistant Secretary of State for East Asia and Pacific Affairs, for example, who had visited Beijing in late April, proposed that China, which has provided oil to North Korea through a pipeline, impose a total embargo on such supply as a means of making the North return to the talks (*Washington Post*, May 7, 2005). But the Chinese side rejected the proposal, saying a pipeline being used to supply oil to North Korea would be clogged with hardened oil components if the oil supply were stopped. Instead, as a counterproposal, China told the United States that it was considering expanding the scope of food items subject to a trade embargo against North Korea, saying that the suspension of food aid would be more effective in helping the North to return to six-party talks.

Thanks to informal negotiations between the United States and North Korea for the resumption of six-party talks, Pyongyang agreed with the United States in early July to return to the talks. Following the agreement, the fourth round of six-party talks were held from July 26. On September

19, the six countries issued a joint statement, their first such statement. The six-point statement committed North Korea to fully scrapping its nuclear weapons, return promptly to the Non-Proliferation Treaty (NPT), and accept inspections of its nuclear facilities by the International Atomic Energy Agency (IAEA). On November 9, the fifth round of six-party talks started. But the talks went into recess with the six countries agreeing to get together again early next year.

The fourth round of talks was held amid speculation that the United States would refer North Korea's nuclear issue to discussion at the UN Security Council if the framework of the multilateral talks collapsed. But the fourth-round talks produced tangible results, as they ended in the release of the first joint statement. This successful result was mainly attributed to the diplomatic role played by China, which wanted to avoid taking tough measures against North Korea. Before and after the six-party talks were held, the Chinese government sent key officials one after another to North Korea. For example, on July 12, just two weeks before the fourth round of six-party talks started, State Councillor Tang Jiaxuan visited North Korea. On October 8, a month before the start of the five-round talks, a period when the fate of that round was imperiled, Vice Premier Wu Yi visited North Korea. In addition, CPC General Secretary Hu Jintao visited Pyongyang on October 26 and held talks with North Korean leader Kim Jong Il. During the summit, Kim Jong Il told Hu that North Korea would participate in the fifth round of six-party talks as scheduled, in line with his country's earlier pledge. During the summit, the leaders of China and North Korea also signed a bilateral economic and technological cooperation agreement.

US-China Relations in 2005

Relations between the United States and China in 2005 were remembered as a mix of confrontation and cooperation. US government officials, including Deputy Secretary of State Robert Zoellick, recently proposed that China become "a responsible stakeholder" in the international community. The proposal reflected the United States' expectations of China, as a responsible major power, to engage actively in international efforts to maintain global order in view of the country's booming economic growth. As if responding to the US proposal for China to become "a responsible stakeholder," some in China have recently asserted that the country should focus on realizing "peaceful development." As shown in a white paper entitled "China's Peaceful Development Road," released by the State

Council in December 2005, “peaceful development” is a concept floated by the administration of President Hu Jintao to prevent the spread of the idea that China is a threat to the world, by clarifying the country’s role in the international community. The concept intends that China, as a major power, participate actively in global efforts to maintain international order, by pursuing “peaceful development” and promoting stability of China and its surrounds. The multilateral-oriented cooperative diplomacy pursued by China in recent years has been in line with its policy of promoting “peaceful development.”

Although China has adopted a policy of “peaceful development,” it does not mean that a solid consensus on the idea has formed in the country. Some hard-liners in China have branded the “peaceful development” policy as “weak-kneed.” In July 2005, for example, Zhu Chenghu, dean of the Defense Affairs Institute of the PLA National Defense University, stated that, “If the Americans train their missiles and position-guided munitions on to targets in Chinese territory, I think we will have to respond with nuclear weapons.... We will prepare ourselves for the destruction of all of the cities east of Xi’an. Of course the Americans will have to be prepared for the destruction of hundreds of cities by the Chinese” (Financial Times, July 15, 2005). The Chinese government quickly distanced itself from Zhu’s statement, with Foreign Affairs Minister Li Zhaoxing saying Zhu’s remarks are his personal views and do not represent the position of the Chinese government. Li also said China’s “no-first-use” policy regarding nuclear weapons could not be changed. How the Hu Jintao administration would push for the “peaceful development” policy while curbing moves by hard-liners like Zhu deserves careful attention.

China has remained very distrustful over the Japan-US security alliance. On February 19, defense and foreign affairs leaders of Japan and the United States met in Washington for the “2 plus 2” security talks and reaffirmed the importance of the Japan-US alliance, in which the security-alliance system is seen as a core of the bilateral alliance. A joint statement issued after the security talks included an agreement by Japan and the United States to seek peaceful solutions to issues related to the Taiwan Straits, through promotion of dialogue. The agreement was one of common strategic objectives in the region agreed on by the two countries. China severely criticized the agreement between Japan and the United States as “absolutely unacceptable,” terming it as boldly challenging China’s sovereignty, territorial integrity, and national security, and as

encouraging forces in favor of Taiwan's independence to take dangerous chances by sending a wrong signal to these forces (*People's Daily*, February 21, 2005). As seen in agenda items at the "2 plus 2" security talks held in February and October, Japan and the United States have recently stepped up efforts to jointly develop a missile defense (MD) system and to realign US forces stationed in Japan. China is likely to strengthen its vigilance against such moves.

The United States explicitly voiced concerns over China's moves to build its military capability in the *2005 Annual Report on the Military Power of the People's Republic of China*, released by the Defense Department in July. The report stated that China's military spending in 2005 was estimated at a maximum US\$90 billion—two to three times higher than the US\$29.9 billion the Chinese government officially reported. In the report, the Pentagon expressed concerns over the opaque nature of China's military capability and judged China's rapid military modernization could pose a clear threat to US forces stationed in the neighborhood of China. The annual report also stated the Chinese military has deployed 650 to 730 short-range ballistic missiles on the coast facing the Taiwan Straits, increasing the deployment of such missiles at the rate of 100 per year. The Chinese government protested strongly against the US perceptions expressed in the 2005 Pentagon report on China's military power, and embarked on dispelling views that China is a threat. In September, the Chinese government released a white paper entitled, *China's Endeavors for Arms Control, Disarmament and Non-Proliferation*, to elaborate on the Chinese government's policies on arms control and disarmament. In the white paper, China emphasized that its military power is limited to the minimum level required for the protection of the country, and that the People's Liberation Army (PLA) has been sharply reducing the number of its forces. At the end of the year, the PLA announced that it had completed a plan to cut 200,000 forces. In addition, China invited military officers from 24 countries, including the United States, the United Kingdom, France, Germany, and Australia, to China to observe a military exercise called North Sword 2005. The invitation is seen as part of Beijing's efforts to demonstrate to the rest of the world that China's military capability has been transparent.

Behind US concern over China's military buildup has been the Taiwan issue. The United States has expressed concern over the possibility of China using military power against Taiwan. On March 14, the National People's Congress formally adopted the Anti-Secession Law, which stipu-

lates that mainland China oppose and suppress secessionist moves by forces in favor of Taiwan's independence. But the following day, on March 15, the US House of Representatives passed a resolution against the Anti-Secession Law by an overwhelming majority. When US Secretary of State Condoleezza Rice visited China, she expressed a critical view toward the Anti-Secession Law, telling the Chinese leadership on March 21 that the United States does not welcome China's enactment of the Anti-Secession Law because it is likely to intensify tensions between China and Taiwan (refer to "Domestic Politics").

Another reason why Washington is concerned about China's military buildup is related to moves by the EU to lift an embargo on arms exports to China. In recent years, China has launched diplomatic offense against the EU in a bid to make it lift the trade embargo. The United States has been adamantly opposed to the EU removing the embargo, arguing the lifting of the measure would lead to a change in the military balance in the region. In February, the US House of Representatives adopted a resolution calling for the EU to review a plan to lift a China-bound arms embargo. Wariness over China mounted in Europe following the March enactment of the Anti-Secession Law, leading the EU to postpone the lifting of the trade embargo against China to next year or later from the originally planned June 2005 (*New York Times*, March 23, 2005). However, after their summit in September, China and the EU released a joint statement to the effect that they would continue discussions on the arms-trade issue. In addition, Chinese President Hu Jintao visited Europe in October, lobbying for EU leaders to lift the embargo at an early date and deepening trade ties between China and the EU.

As mentioned above, the United States and China, despite several pending issues, tried to strengthen their diplomatic relations via meetings of their leaders. On September 13, Chinese President Hu Jintao visited the United States for the first time since taking office. The trip was returned by US President George W. Bush's visit to Beijing on November 19. In August and December, the United States and China also held regular sub-cabinet-level meetings for comprehensive strategic dialogue covering political, economic, security, and international issues, marking the first such talks between the two countries.

China-Russia Relations through Bilateral and Multilateral Cooperation

During their summit meeting on November 18, the leaders of China and

Russia shared the view that 2005 can be remembered as a year of successful relations between the two countries. Throughout the year, the two countries worked to deepen their diplomatic ties through the promotion of bilateral and multilateral interchanges. On June 30, Chinese President Hu Jintao visited Russia and held a summit with Russian President Vladimir Putin. At the summit, the leaders of the two countries signed an agreement on the eastern border, declaring the longstanding border dispute solved. Following the summit, China and Russia also signed the Joint Declaration on the International Order in the 21st Century. Under the declaration, the two countries agreed that the basic foundation for maintaining international order should be built on multilateralism, equally beneficial relations, and a UN-led initiative, and they pledged to oppose the use of arbitrary unilateralism as a means of dealing with international issues. The declaration thus indirectly criticized the US administration of President George W. Bush for his unilateral approach to international issues.

On July 5, the leaders of the Shanghai Cooperation Organization (SCO) held their fifth summit in Kazakhstan. India, Pakistan, Iran, and Mongolia attended the SCO summit as observers, joining the grouping's six regular members—China, Russia, Kazakhstan, Uzbekistan, Kyrgyzstan, and Tajikistan. The participants discussed measures against international terrorism, expansion of economic cooperation in energy resources development and other areas, and promotion of human interchanges on various fronts. A declaration issued by the leaders after their summit meeting demanded the withdrawal of US forces stationed in Kyrgyzstan and Uzbekistan, although it refrained from specifying the names of the countries, saying that, "Considering the completion of the active military stage of antiterrorist operations in Afghanistan, the member states of the SOC consider it necessary that the respective members of the antiterrorist coalition set a final timeline for their temporary use of objects of infrastructure and the presence of their military contingents on the territories of SCO member states."

In August, China and Russia conducted their first joint military exercise, dubbed "Peace Mission 2005." The exercise was carried out over eight days from August 18, in Vladivostok in far eastern Russia, China's Shandong Peninsula, and nearby offshore seawaters. The exercises involved about ten thousand troops from the armies, navies, and air forces of Chinese and Russian armed forces, with about eight thousand troops from the Chinese side taking part. China and Russia invited senior

defense officials from India and Pakistan, as well as representatives of member countries of the SCO, to observe the joint exercise. The exercises included a training drill apparently based on the assumption of an emergency breaking out in Taiwan. This spawned speculation that China tried to test an agreement between Japan and the United States made in February 2005, in which the Taiwan issue was identified as a common strategic objective. As expected, China and Russia brushed off such speculation, expressing their official position that the joint exercise was meant to enhance the capability of the armed forces of the two countries in striking international terrorism and separatism, and that it was not carried out against any third country or imagined enemy. But the joint military exercise still drew attention as a move to counter the unilateralism by the United States and its new military strategy involving the realignment of forces stationed outside the mainland United States.

Russia is a country that could be beneficial to China because its abundant oil and natural gas resources make it a potential long-term energy supplier to China, and also because it is capable of expanding advanced arms exports to the Asian country at a time when the European Union's plan to lift an arms embargo against China has made little progress. It is true that a honeymoon period was seen in 2005 between China and Russia. But in light of their past historical relations, it is difficult to determine immediately the extent to which they will unite strategically.

First East Asia Summit and Chinese Diplomacy in Southeast Asia

China has continued to focus on reinforcing its relations with the Association of Southeast Asian Nations (ASEAN) through a multilateral cooperative framework in the Asia-Pacific region. On December 14, the first East Asia Summit was held in Malaysia. The summit has been seen as the touchstone of Asia's ability to work out the direction of the proposed East Asian Community. China asserted that members of an East Asia Summit should be selected from the framework of ASEAN Plus Three countries (Japan, China, and South Korea). China also made it clear to other Asian countries that it does not want the United States to participate in the summit (*Newsweek*, September 26, 2005). It has been suggested that, in pushing for the formation of the East Asian Community, China is trying to check the unilateralism of the United States. It was finally decided that the summit would involve 13 countries (ASEAN plus Japan, China, and South Korea), and three others—India, Australia, and New

Zealand. At the first East Asia Summit in Malaysia, the leaders of the member nations released a joint declaration, reaffirming their commitment to promoting regional cooperation in political, economic, security, and other fields. The leaders also agreed in the declaration that an East Asia Summit should play an important role for the promotion of regional integration in Asia, with an eye to the formation of an East Asian Community in the future. In view of the divergent strategies being considered by ASEAN countries to becoming a leading player in regional multi-lateral talks, political bargaining between major powers over the proposed East Asian Community is expected to continue for some time.

(by Haruka Matsumoto)

ISSUES IN 2006

An important political task for the administration of President Hu Jintao is to comprehensively solidify its power base in preparation for the 17th party convention set for the autumn of 2007. In preparing for the launch of such a move, the Hu administration is likely to reshuffle high-level officials of the PLA and regional cadres. The extent to which politicians hailing from the Communist Youth League of China—from which Hu himself rose—are chosen for important posts will serve as a barometer for how strong Hu's power base has become. In 2006, Hu is likely to continue an education campaign to help strengthen discipline within the party. However, such a campaign is expected to draw a strong reaction from regional officials, thereby forcing Hu to busy himself in handling the matter. In a bid to make its power base more solid, the Hu administration is expected to strengthen its control over the media and intellectuals by limiting freedom of speech, making the advancement of political reforms difficult in China.

On bilateral diplomacy, it is imperative for the Hu administration to mend its soured ties with Japan. The election of the next Japanese prime minister in the autumn of 2006 will be a key factor in improving Japan-China relations. China is facing the task of revising its policy toward Japan, with consideration given to who will succeed Junichiro Koizumi as new Japanese prime minister. Relations between China and the United States are likely to continue oscillating between confrontation and cooperation. The question of whether regular subcabinet-level meetings between China and the United States can serve as a stable framework for

constructive discussions is under discussion. On multilateral cooperative diplomacy, China would have to appreciate that the United States cannot devote itself to six-party talks on North Korea's nuclear programs in view of the confusion over the reconstruction of post-war Iraq. Under these circumstances, China's role in the six-party talks is likely to grow further. It is also worth paying attention to moves by the Shanghai Cooperation Organization (SCO), of which China is a member, and the proposed creation of an East Asian Community.

Investment-led growth efforts in China in recent years have produced a huge supply capacity in the country. As already widely perceived, it is indispensable for China to shift its growth policy toward consumption-oriented demand if it wants to stably sustain high growth while avoiding further intensification of trade frictions stemming from its excessive reliance on external demand. The most important factor for achieving such growth is increasing the purchasing power of consumers, by promoting the transfer of labor from farm areas to urban areas.

As its international presence grows, China will continue to face trade frictions with foreign countries, especially industrialized countries. Given these circumstances, China is likely to encounter international pressure to implement a phased expansion of the fluctuation range of the renminbi's exchange rate against the US dollar, which is currently set at a very moderate level.

IMPORTANT DATES IN 2005

January

- 1: Attending a New Year tea party sponsored by the Chinese People's Political Consultative Conference, Hu Jintao, general secretary of the Chinese Communist Party, expressed the hope that mainland China and Taiwan will soon resume interchanges.
 - Premier Wen Jiabao visited the Tongchuan Mining Administration of Shaanxi Province and consoled the bereaved families of miners killed in a mine accident on November 28, 2004.
- 3: Koo Chen-fu, chairman of the Taiwanese Strait Exchange Foundation, died. Wang Daohan, president of the Association for Relations across the Taiwan Straits, sent a telegram of condolences to his family.
- 5: The Chinese Communist Party held a working conference on the education campaign to preserve the advanced nature of party members. Zeng Qinghong, a Standing Committee member of the Political Bureau of the CPC Central Committee, delivered an important speech to the conference.
- 5–6: Premier Wen Jiabao visited Indonesia. The premier attended an emergency meeting of ASEAN leaders to help reconstruct the regions of Indonesia hit by the massive earthquake and subsequent tsunami in late 2004.
- 10–11: The Fifth Plenary Session of the Central Commission for Discipline Inspection opened. General Secretary Hu Jintao delivered an important speech to the session.
- 14: An expert panel met to present a report on “a new-era education campaign to preserve the advanced nature of party members.” CPC General Secretary Hu Jintao presented an important report.
- 17: Former CPC general secretary Zhao Ziyang died aged 85. Jia Qinglin, chairman of the Chinese People's Political Consultative Conference, attended his funeral ceremony, held on the 29th.
- 20: China established diplomatic relations with Grenada.
- 23: The Fujian Provincial People's Congress elected Huang Xiaojing as governor of Fujian Province.
- 29: Jia Qinglin, chairman of the Chinese People's Political Consultative Conference, delivered a speech at a meeting commemorating the 10th anniversary of the speech made by Jiang Zemin on China's unification.
 - The Jilin Provincial People's Congress elected Wang Min as governor of Jilin Province.
 - China's first charter flight of the Lunar New Year arrived in Taipei (through February 20).
- 30: The State Council released Document No. 1 of the Central Committee in 2005, presenting some policy proposals to improve the overall production capacity of the agricultural sector.

February

- 1–2: Sun Yafu, vice president of the Association for Relations across the Taiwan Straits, visited Taipei to express his condolences over the death of Koo Chen-fu, chairman of the Taiwanese Strait Exchange Foundation.
- 14: More than 200 people were killed due to a gas explosion at the Sunjiawan coal mine in Liaoning Province. The colliery is operated by the Fuxin Mining Group.
- 19: CPC General Secretary Hu Jintao delivered an important speech on the building of a harmonious socialist society at a meeting of the CPC Central Party School.
 - Wang Jiarui, head of the International Liaison Department of the CPC Central Committee, visited North Korea (through the 22nd). Wang met with General Secretary Kim Jong Il and conveyed China's hope that North Korea will return to six-party talks as soon as possible.
 - The Ministry of Foreign Affairs expressed its opposition to part of a Japan-US joint security statement covering the Taiwan issue, released following a "2 plus 2" security talks of the defense and foreign affairs heads of Japan and the United States.
- 24: The State Council released the full text of its opinions on encouraging nonpublic economic activities and guidance on such activities.
- 25: Foreign Affairs Minister Li Zhaoxing attended a meeting of SCO foreign ministers in Kazakhstan.

March

- 3–12: The 10th National Committee of the Chinese People's Political Consultative Conference opened its third meeting.
- 4: CPC General Secretary Hu Jintao put forward "four opinions" on relations across the Taiwan Straits.
- 5–14: The 10th National People's Congress opened its third meeting. On the 13th, Hu Jintao was named chairman of the CPC Central Military Commission. Hu delivered an important speech at a meeting of representatives of the People's Liberation Army (PLA). On the 14th, the Anti-Secession Law was enacted.
- 10: Tung Chee Hwa submitted his resignation as chief executive of the Hong Kong Special Administrative Region. The plenary session of the State Council endorsed his resignation and Donald Tsang, administrative secretary, was appointed acting chief executive on the 12nd.
- 17: Japanese Foreign Minister Nobutaka Machimura said Japan would discontinue yen loans to China in 2008.
- 20–21: US Secretary of State Condoleezza Rice visited China.
- 22–27: North Korean Premier Pak Pong Ju visited China.
- 24–27: Japanese Vice Defense Minister Takemasa Moriya visited China. Japan and China held the sixth expert-level talks on security issues.

- 28–April 1: Chiang Pin-kung, vice chairman of Taiwan’s Kuomintang (KMT), visited China. He met with Jia Qinglin, chairman of the Chinese People’s Political Consultative Conference.
- 30: The Standing Committee of the State Council approved the outline of 2005 activities of the State Council and the council’s opinion on deepening China’s economic reforms in 2005.

April

- 2: Anti-Japanese demonstrations were staged in Chengdu City. Japanese-affiliated stores were attacked.
- 5: The Chinese Foreign Affairs Ministry filed a request about Japan’s history textbook screening with the Japanese Embassy in Beijing.
- 5–12: Premier Wen Jiabao visited Pakistan, Bangladesh, Sri Lanka, and India. On the 11th, Wen met with Indian Prime Minister Manmohan Singh and signed a pact on China-India border issues.
- 8: The Shanghai and Shenzhen stock markets released a unified stock index.
- 9: An anti-Japanese rally involving about ten thousand people was staged in Beijing.
- 13: The Japanese government initiated procedures to grant private companies rights to dig natural gas fields on a trial basis in the East China Sea.
- 15: The Political Bureau of the CPC Central Committee received a report from a democratic-life group for advanced education activities, with Standing Committee members attending.
- China released its official 2004 gazette on national land resources.
- 16: An anti-Japanese rally was staged in Shanghai with several tens of thousands of people participating.
- 16–18 Japanese Foreign Minister Nobutaka Machimura visited China. He held talks with Chinese Foreign Affairs Minister Li Zhaoxing and State Councillor Tang Jiaxuan to deal with anti-Japanese demonstrations in China.
- 18–19: Australian Prime Minister John Howard visited China.
- 19: A meeting was held to discuss the situation on Japan-China relations. Foreign Affairs Minister Li Zhaoxing presented a report on such relations to the meeting. China began efforts to prevent the further spread of anti-Japanese demonstrations.
- 20–28: President Hu Jintao visited Brunei, Indonesia, and the Philippines.
- 21: The Information Office of the State Council released a white paper on new developments regarding the protection of intellectual property rights in China.
- The Ministry of Public Security released a statement to restrict anti-Japanese demonstrations.
- 23: President Hu Jintao met with Japanese Prime Minister Junichiro Koizumi. During the meeting, Hu put forward a five-point proposal for the advance-

ment of Japan-China relations.

- 24: President Hu Jintao attended a ceremony marking the 50th anniversary of the foundation of the Bandung Conference in Indonesia.
- 26: The Ministry of Commerce criticized the EU for floating the possibility of invoking safeguards against textile imports from China.
- 26–May 3: Lien Chan, chairman of the Chinese Nationalist Party of Taiwan, commonly known as Kuomintang (KMT), visited Beijing. He held talks with CPC General Secretary Hu Jintao on the 29th.
- 27: The Standing Committee of the National People's Congress dismissed Health Minister Wu Yi. Gao Qiang was appointed to replace Wu.

May

- 5–13: James Soong, chairman of Taiwan's People First Party, visited Beijing. He held talks with CPC General Secretary Hu Jintao on the 12nd.
- 5: President Hu Jintao held phone talks with US President George W. Bush.
- 6–7: Foreign Affairs Minister Li Zhaoxing visited Kyoto, Japan. Li attended a meeting of ASEAN Plus Three (Japan, China, and South Korea) foreign ministers, and a meeting of ASEM foreign ministers. On the 7th, Li met with Japanese Foreign Minister Nobutaka Machimura.
- 8–9: President Hu Jintao visited Russia. Hu attended a ceremony marking the 60th anniversary of Russia's victory in the war of defending the country.
- 16: Japanese Prime Minister Junichiro Koizumi told the Budget Committee of the House of Representatives that he has no reason to stop visiting the Yasukuni Shrine.
 - Premier Wen Jiabao met with members of a delegation sent by the American Chamber of Commerce.
- 17–23: Vice Premier Wu Yi visited Japan. On the 23rd, she abruptly canceled a scheduled meeting with Japanese Prime Minister Junichiro Koizumi and returned to China, citing an emergency public duty in her country.
- 20: The State Council granted a hike in export duties for textile products, effective June 1.
- 21–23: Tsutomu Takebe, secretary general of Japan's Liberal Democratic Party (LDP), and Tetsuzo Fuyushiba, secretary general of New Komeito, visited China. They held talks with President Hu Jintao.
- 27–28: A national working conference on ethnic minorities was held. President Hu Jintao delivered an important speech.
- 30: Japan and China held their second bureau-chief talks in Beijing over issues related to natural gas development in the East China Sea.

June

- 1: The Tariff Regulations Committee withdrew export duties on 81 textile items.
- 1–3: Foreign Affairs Minister Li Zhaoxing visited Russia.

- 1–4: US Commerce Secretary Carlos M. Gutierrez visited Beijing. He held talks with Chinese Commerce Minister Bo Xilai over the textile trade dispute.
- 4: Foreign Affairs Minister Li Zhaoxing attended a meeting of SCO foreign ministers.
- 6: A national working conference on the reform of agricultural tax was held.
- 7: The Chinese government released documents concerning China's views on the reform of the United Nations.
- 11: A riot broke out in Dingzhou City, Hebei Province. An armed group attacked 200 to 300 villagers, leaving six of them dead.
 - A meeting of trade ministers between China and the United States was held in Beijing.
 - A China-EU dispute over textile trade was settled with the EU withdrawing a plan to invoke safeguard measures, following China's decision to limit textile exports on a voluntary basis.
- 16: The election of a new chief executive of the Hong Kong Special Administrative Region was held. Donald Tsang was acclaimed the winner without a vote, as he was the only eligible candidate. The plenary session of the State Council finalized his election as chief executive.
- 17: Bank of America agreed to acquire an equity stake in China Construction Bank.
- 19: The China Securities Regulatory Commission announced that 42 companies would be subject to second-tier reforms on a trial basis, as part of efforts to promote the secondary sale of listed firms.
- 19–23: South Korean Prime Minister Lee Hae Chan visited Beijing.
- 30–July 2: Thai Prime Minister Thaksin Shinawatra visited Beijing.
- 30–July 3: President Hu Jintao visited Russia. He met with Russian President Vladimir Putin and signed a joint declaration.

July

- 1: The Standing Committee of the National People's Congress named Wu Aiying as minister of justice and Tian Chengping as minister of labor and social security.
 - The CPC Central Committee decided to appoint Zhang Baoshun as secretary of the Shanxi Provincial Committee.
- 3: President Hu Jintao visited Kazakhstan (through the 6th). He attended the Fifth SCO summit.
 - The second summit of the Greater Mekong Subregion (GMS) Economic Cooperation Program was held. Premier Wen Jiabao delivered a speech at an opening ceremony for the summit.
- 6–7: President Hu Jintao visited the United Kingdom. He attended the summit of the G-8 powers in Gleneagles.
- 9: The Shanxi Provincial People's Congress named Yu Youjun as acting governor of the Shanxi Provincial People's Government.

- 9–10: US Secretary of State Condoleezza Rice visited Beijing.
- 12–14: State Councillor Tang Jiaxuan visited North Korea. He held talks with General Secretary Kim Jong Il.
- 21: The People's Bank of China announced the adoption of a new currency system for the renminbi that makes use of a basket of currencies as a reference for exchange rate. It also revalued the Chinese currency by 2.1 percent against the US dollar.
- 26: The Fourth six-party talks on North Korea's nuclear programs were held (through August 7: The meeting went into recess).

August

- 1: The Sichuan Provincial Health Bureau released details of the damage caused by a swine virus infection that affected a southwest province.
- 1–2: China and the United States opened their first regular subcabinet-level meetings.
- 15: The State Council released some opinions on the promotion of the distribution industry.
- 18–25: China and Russia conducted a joint military exercise, called "Peace Mission 2005."
- 19–24: Zeng Qinghong, a Standing Committee member of the Political Bureau of CPC Central Committee, visited the Xinjiang Uygur Autonomous Region.

September

- 1: A meeting celebrating the 40th anniversary of the establishment of the Tibet Autonomous Region was held. Jia Qinglin, chairman of the Chinese People's Political Consultative Conference, delivered an important speech at the meeting.
 - The Information Office of the State Council released a white paper entitled "China's Endeavors for Arms Control, Disarmament and Non-Proliferation."
- 3: A meeting commemorating the 60th anniversary of the Chinese people's victory in the Anti-Japanese War was held. CPC General Secretary Hu Jintao delivered an important speech.
- 5: China concluded a new agreement with the EU over its textile exports to the EU.
- 9: President Hu Jintao visited the United States, Canada, and Mexico.
 - Zeng Qinghong, a Standing Committee member of the Political Bureau of CPC Central Committee, visited Hong Kong (through September 12). He attended an opening ceremony for Hong Kong Disneyland.
- 13: President Hu Jintao met with US President George W. Bush. Hu expressed sympathy over the victims of the devastating hurricane that had recently hit the United States.
- 13–19: The fourth six-party talks on North Korea's nuclear program were

- resumed. The talks ended with the six countries releasing a joint statement.
- 14: President Hu Jintao delivered an important speech at a summit meeting held to mark the 60th anniversary of the foundation of the United Nations. He met with Russian President Vladimir Putin and Indian Prime Minister Manmohan Singh.
- 20: The Japanese government filed a protest against China over its start of natural gas pumping in the Tianwaitian field in the East China Sea.
- 27: China conducted a military exercise, called “North Sword 2005.”
- 29: The Political Bureau of the CPC Central Committee convened a meeting and discussed its activities during and after the Fourth Plenary Session of the 16th Central Committee, as well as the 11th Five-Year Long-Term Plan.
- 30: Japan and China held their third subcabinet-level talks in Tokyo, over natural gas development in the East China Sea.

October

- 1: A meeting celebrating the 50th anniversary of the establishment of the Xinjiang Uygur Autonomous Region was held.
- 8–11: The 16th Central Committee of the CPC kicked off its Fifth Plenary Session. The session adopted a CPC Central Committee proposal on the 11th Five-Year Long-Term Plan.
- Deputy Premier Wu Yi visited North Korea. She held talks with General Secretary Kim Jong Il.
- 11–15: US Treasury Secretary John Snow visited Beijing.
- 12: China successfully launched Shenzhou 6, marking the nation’s second manned spacecraft flight.
- 15–16: The seventh meeting of the G-20 finance ministers and central bank governors opened. General Secretary Hu Jintao delivered an important speech at the meeting.
- 17: Japanese Prime Minister Junichiro Koizumi visited Yasukuni Shrine, prompting China to cancel its scheduled foreign ministerial meeting with Japan.
- 18–20: US Defense Secretary Donald Rumsfeld visited Beijing.
- 19: The Information Office of the State Council released a white paper on the construction of a democratic political system in China.
- 25: A ceremony celebrating the 60th anniversary of Taiwan’s retrocession was held in Beijing. Jia Qinglin, chairman of the Chinese People’s Political Consultative Conference, delivered an important speech at the ceremony.
- 26–27: Premier Wen Jiabao visited Russia. He attended the fourth meeting of prime ministers of SCO member countries.
- 26–30: CPC General Secretary Hu Jintao visited North Korea. He held talks with General Secretary Kim Jong Il.

31–November 1: President Hu Jintao visited Vietnam. He signed an agreement between China and Vietnam to develop oil in the Gulf of Tonkin.

November

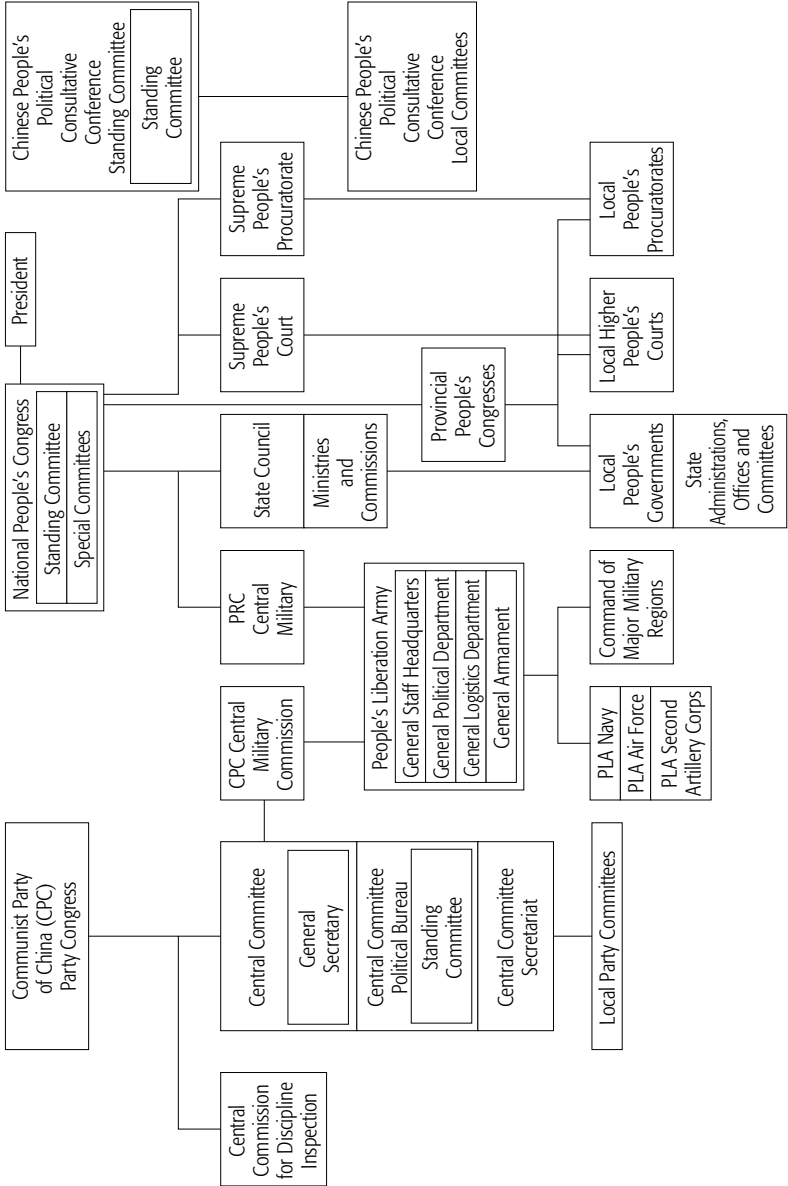
- 1: China and Russia held their ninth regular meeting of prime ministers.
- 3: China and Russia held their 10th regular meeting of prime ministers. Chinese Premier Wen Jiabao and Russian Prime Minister Mikhail Fradkov attended the meeting.
- 8: President Hu Jintao visited the United Kingdom, Germany, and Spain (through the 15th).
 - The governments of the United States and China reached a comprehensive agreement on textile trade.
- 9: The fifth six-party talks on North Korea's nuclear programs were held (The talks went into recess on November 11).
- 18: Round-table talks were held in Beijing to commemorate the 90th anniversary of the birth of comrade Hu Yaobang, with Premier Wen Jiabao attending. Zeng Qinghong, a Standing Committee member of the Political Bureau of CPC Central Committee, delivered an important speech at the talks.
 - The commercial airline industries of mainland China and Taiwan reached an agreement to operate charter flights at Chinese New Year.
- 18–19: President Hu Jintao visited South Korea. Hu attended the 13th APEC informal summit in Pusan. He signed a free trade agreement (FTA) with Chile. He held talks with Russian President Vladimir Putin.
- 19–21: US President George W. Bush visited Beijing. Bush held talks with President Hu Jintao. Meeting with Bush, Hu put forward a five-point proposal to advance relations between China and the United States.
- 21: The government of Harbin City announced the suspension of water supply in the city, following the contamination of the Songhua River by chemicals due to an explosion at a chemical plant in Jilin Province. Premier Wen Jiabao visited Harbin City to inspect the situation relating to the river contamination. On December 2, the State Council dismissed Xie Zhenhua, director of the state administration of environmental protection. Zhou Shengxian was appointed to replace Xie.
- 27: The Central Committee of the CPC appointed Zhang Qingli as acting secretary of the Tibet Autonomous Region Committee.
- 28: President Hu Jintao held talks with Mongolian President Nambaryn Enkhbayar.
- 29–December 1: A central working conference on economic issues opened.

December

- 1: The Chinese and Indian navies conducted their first joint military exercise in the Indian Ocean.

- 4–15: Premier Wen Jiabao visited France, Slovakia, Czech, Portugal, and Malaysia.
- 6: Armed police clashed with protesters opposing the construction of a power plant in Donghua, Shanwei City, Guangdong Province.
- 7–8: China and the United States opened their second regular subcabinet-level meetings.
- 9: Foreign Affairs Minister Li Zhaoxing attended the second meeting of foreign ministers of ASEAN and China.
- 10: Foreign Affairs Minister Li Zhaoxing attended a meeting of foreign ministers being held on the fringes of the first East Asia Summit.
- 12: A summit of ASEAN Plus Three was held.
- 14: Premier Wen Jiabao attended the first East Asia Summit.
- 20: The State Statistics Bureau announced the preliminary results of the first economic census. The bureau revised 2004 GDP upward by 16.8 percent from its initial estimate.
- 22: The Information Office of the State Council released a white paper entitled “China’s Peaceful Development Road.”
- 24: The Central Committee of the CPC appointed Qian Yunlu as secretary of the Heilongjiang Provincial Committee, Shi Zongyuan as secretary of the Guizhou Provincial Committee, Zhang Chunxian as Secretary of the Hunan Provincial Committee, and Wang Yang as Secretary of the Chongqing Municipal Committee.
- Wang Daohan, president of the Association for Relations across the Taiwan Straits, died.
- 28–29: A central working conference on agricultural villages opened.
- 29: The Standing Committee of the National People’s Congress adopted a proposal to repeal an ordinance on agricultural taxes. Li Shenglin was appointed communications minister.
- 31: The People’s Liberation Army (PLA) completed a plan to slash the number of its troops by 200,000.

APPENDIX 6.1. STATE ORGANIZATION CHART



APPENDIX 6.2 LIST OF COMMUNIST PARTY OF CHINA (CPC) LEADERS AND STATE LEADERS

(as of end of 2005)

1. COMMUNIST PARTY OF CHINA (CPC)

(1) Sixteenth Central Committee

General Secretary: Hu Jintao

Standing Committee Members of Central Committee Political Bureau: Hu Jintao, Wu Bangguo, Wen Jiabao, Jia Qinglin, Zeng Qinghong, Huang ju, Wu Guanzheng, Li Changchun, Luo Gan

Members of Central Committee Political Bureau: Wang Lequan, Wang Zhaoguo, Hui Liangyu, Liu Qi, Liu Yunshan, Li Changchun, Wu Yi, Wu Bangguo, Wu Guanzheng, Zhang Lichang, Zhang Dejiang, Chen Liangyu, Luo Gan, Zhou Yongkang, Hu Jintao, Yu Zhengsheng, He Guoqiang, Jia Qinglin, Guo Boxiong, Huang ju, Cao Gangchuan, Zeng Qinghong, Zeng Peiyan, Wen Jiabao

Central Committee Political Bureau Alternate Members: Wang Gang

Members of Secretariat of Central Committee: Zeng Qinghong, Liu Yunshan, Zhou Yongkang, He Guoqiang, Wang Gang, Xu Caihou, He Yong

(2) Central Commission for Discipline Inspection

Secretary: Wu Guanzheng

Deputy Secretaries: He Yong, Xia Zanzhong, Li Zhilun, Zhang Shutian, Liu Xirong, Zhang Huixin, Liu Fengyan

(3) Central Military Commission

Chairman: Hu Jintao

Vice Chairmen: Guo Boxiong, Cao Gangchuan, Xu Caihou

Members: Liang Guanglie, Li Jinai, Liao Xilong, Chen Bingde, Qiao Qingchen, Zhang Dingfa, Jing Zhiyuan

(4) Organs under Central Committee

Director of Central General Office: Wang Gang

Head of Central Organization Department: He Guoqiang

Head of Central Publicity Department: Liu Yunshan

Head of Central United Front Work Department: Liu Yandong

Head of Central International Liaison Department: Wang Jiarui

2. STATE SUPREME ORGANIZATIONS

President: Hu Jintao

Vice President: Zeng Qinghong

Chairman of Standing Committee of National People's Congress: Wu Bangguo

Chairman of Chinese People's Political Consultative Conference: Jia Qinglin

Premier of State Council: Wen Jiabao

Chairman of PRC Central Military Commission: Hu Jintao

President of Supreme People's Committee: Xiao Yang

Procurator General of Supreme People's Procuratorate: Jia Chunwang

3. PEOPLE'S LIBERATION ARMY

Chief of General Staff Headquarters: Liang Guanglie

Director of General Political Department: Li Jinai

Director of General Logistics Department: Liao Xilong

Director of General Armament Department: Chen Bingde

Commander of PLA Navy: Zhang Dingfa

Commander of PLA Air Force: Qiao Qingchen

Commander of Second Artillery Corps: Jing Zhiyuan

4. STATE COUNCIL

Premier: Wen Jiabao

Vice Premiers: Huang Ju, Wu Yi, Zeng Peiyan, Hui Liangyu

State Councillors: Zhou Yongkang, Cao Gangchuan, Tang Jiaxuan, Hua Jianmin,¹ Chen Zhili

Foreign Affairs Minister: Li Zhaoxing

National Defense Minister: Cao Gangchuan

State Development and Reform Commission Minister: Ma Kai

Education Minister: Zhou Ji

Science and Technology Minister: Xu Guanhua

Minister of State Commission of Science, Technology and Industry for National Defense: Zhang Yunchuan

State Ethnic Affairs Commission Minister: Li Dek Su

Public Security Minister: Zhou Yongkang

State Security Minister: Xu Yongyue

Supervision Minister: Li Zhilun

Civil Affairs Minister: Li Xueju

Justice Minister: Wu Aiyang

Finance Minister: Jin Renqing

Personnel Minister: Zhang Bailin

Labor and Social Security Minister: Tian Chengping

Land and Natural Resources Minister: Sun Wensheng

Construction Minister: Wang Guangtao

Railways Minister: Liu Zhijun

Communications Minister: Li Shenglin

Information Industry Minister: Wang Xudong

Water Resources Minister: Wang Shucheng

Agriculture Minister: Du Qinglin

Commerce Minister: Bo Xilai

Culture Minister: Sun Jiazheng

Health Minister: Gao Qiang

State Population and Family Planning Commission Minister: Zhang
Weiqing

Governor of People's Bank of China: Zhou Xiaochuan

Auditor General of Auditing Administration: Li Jinhua

State-owned Assets Supervision and Administration Commission²
Chairman: Li Rongrong

1 Concurrently serves as President of State Administration College.

2 Special Organization under State Council.

APPENDIX 6.3 LIST OF TOP OFFICIALS OF PROVINCES, CITIES, AND AUTONOMOUS REGIONS (as of end of 2005)

<i>Provinces, Cities, Autonomous Regions</i>	<i>Secretaries of Provincial Committees</i>	<i>Governors, Mayors, and Chairman</i>	<i>Chairmen of Standing Committees of Provincial People's Congresses</i>
Beijing	Liu Qi	Wang Qishan	Yu Junbo
Tianjin	Zhang Lichang	Dai Xianglong	Fang Fengyou
Hebei	Bai Keming	Ji Yunshi	Bai Keming
Shanxi	Zhang Baoshun	Yu Youjun (acting)	(vacant)
Inner Mongolia	Chu Bo	Yang Jing	Chu Bo
Liaoning	Li Keqiang	Zhang Wenyue	Li Keqiang
Jilin	Wang Yunkun	Wang Min	Wang Yunkun
Heilongjiang	Qian Yunlu	Zhang Zuoji	Song Fatang
Shanghai	Chen Liangyu	Han Zheng	Gong Xueping
Jiangsu	Li Yuanchao	Liang Baohua	Li Yuanchao
Zhejiang	Xi Jinping	Lu Zushan	Xi Jinping
Anhui	Guo Jinlong	Wang Jinshan	Guo Jinlong
Fujian	Lu Zhangong	Huang Xiaojing	Lu Zhangong
Jiangxi	Meng Jianzhu	Huang Zhiquan	Meng Jianzhu
Shandong	Zhang Gaoli	Han Yuqun	Zhang Gaoli
Henan	Xu Guangchun	Li Chenshu	Xu Guangchun
Hubei	Yu Zhengsheng	Luo Qingquan	Yang Yongliang
Hunan	Zhang Chunxian	Zhou Bohua	Yang Zhengwu
Guangdong	Zhang Dejiang	Huang Huahua	Huang Liman
Guangxi	Gao Bochun	Lu Bing	Cao Bochun
Hainan	Wang Xiaofeng	Wei Liucheng	Wang Xiaofeng
Chongqing	Wang Yang	Wang Hongju	Huang Zhendong
Sichuan	Zhang Xuezhong	Zhang Zhongwei	Zhang Xuezhong
Guizhou	Shi Zongyuan	Shi Xiushi	Qian Yunlu
Yunnan	Bai Enpei	Xu Rongkai	Bai Enpei
Tibet	Zhang Qingli (acting)	Qiangba Puncog	Legqog
Shaanxi	Li Jianguo	Chen Deming	Li Jianguo
Gansu	Su Rong	Lu Hao	Su Rong
Qinghai	Zhao Leji	Song Xiuyan	Zhao Leji
Ningxia	Chen kuiyuan	Ma Qizhi	Chen kuiyuan
Xinjiang	Wang Lequan	Ismail Tiliwaldi	Abudurehim Amet

APPENDIX 6.4: MAJOR STATISTICS

1. General

	1999	2000	2001	2002	2003	2004	2005
Population (10 thousand persons)	125,786	126,743	127,627	128,453	129,227	129,988	130,756
Number of workers (10 thousand persons)	71,394	72,085	73,025	73,740	74,432	75,200	...
Increase in consumer price index (%)	-1.4	0.4	0.7	-0.8	1.2	3.9	1.8
Urban unemployment rates (%)	3.1	3.1	3.6	4	4.3	4.2	4.2
Exchange rates (US\$1=yuan, average)	8.2783	8.2784	8.277	8.277	8.277	8.2768	8.1917

Sources: *China Statistical Yearbook, 2005* and data from the National Bureau of Statistics of China.

2. Gross Domestic Product by Type of Expenditure (at current prices)

	(100 million yuan)					
	2000	2001	2002	2003	2004	2005
Consumption expenditure	54,601	58,927	62,799	67,494	75,438	...
Private	42,896	45,898	48,882	52,679	...	...
Government	11,705	13,029	13,917	14,764	...	...
Gross domestic capital formation	32,500	37,461	42,305	51,383	62,875	...
Exports of goods and services (net)	2,240	2,205	2,794	2,686	4,079	...
Gross domestic expenditure	89,341	98,593	107,898	121,311	142,394	...

Sources: *China Statistical Yearbook, 2005*. However, because this yearbook does not reflect data from the 2004 economic census, major corrections are expected.

3. Gross Domestic Product by Industries (at current prices)

	(100 million yuan)						
	1999	2000	2001	2002	2003	2004	2005
Primary industry	14,548	14,716	15,516	16,239	17,068	20,956	22,718
Secondary industry	41,034	45,556	49,512	53,897	62,436	73,904	86,208
Tertiary industry	34,095	38,942	44,627	50,197	56,318	65,018	73,395
Gross domestic product (GDP)	89,677	99,215	109,655	120,333	135,823	159,878	182,321
Gross national product (GNP)	...	...	...	...	...	...	...
Food* production (10 thousand ton)	50,839	46,218	45,264	45,706	43,070	46,950	48,401
GDP per person (yuan)	7,129	7,828	8,592	9,368	10,510	12,299	13,944

Sources: *China Statistical Yearbook, 2005* and data from the National Bureau of Statistics of China. (The GDP is revised based on the 2004 economic census.)

Note: * Grain, beans, and potatoes.

4. Growth Rates in Gross Domestic Product by Industries

	(%)						
	1999	2000	2001	2002	2003	2004	2005
Primary sector of industry	2.8	2.4	2.8	2.9	2.5	6.3	5.2
Secondary sector of industry	8.1	9.4	8.4	9.8	12.7	11.1	11.4
Tertiary sector of industry	9.3	9.7	10.2	10.4	9.5	10	9.6
Gross domestic product (GDP)	7.6	8.4	8.3	9.1	10	10.1	9.9

Sources: Same as Table 3.

5. Foreign Trade by Country and Area

	(US\$ 100 million)					
	2003		2004		2005	
	Exports	Imports	Exports	Imports	Exports	Imports
EU	721.5	530.6	1,071.6	701.2	1,437.1	740.0
Germany	174.4	242.9	237.6	303.7	325.3	307.2
USA	924.7	338.6	1,249.4	446.6	1,629.0	487.3
Japan	594.1	741.5	735.1	943.3	840.0	1,004.5
Hong Kong	762.7	111.2	1,008.7	118.0	1,244.8	1,222.7
ASEAN	309.3	473.3	429.0	629.8	553.7	750.0
South Korea	201.0	431.3	278.1	622.3	351.1	768.2
Taiwan	90.1	493.6	135.4	647.6	165.5	746.8
Others	778.9	1,007.5	1,025.8	1,503.5	1,073.5	574.5
Total	4,382.3	4,127.6	5,933.3	5,612.3	7,620.0	6,601.2

Sources: Figures up to 2004, *China Statistical Yearbook, 2005*; Figures for 2005 are from China Customs.

6. Budget of the Central Government

	(100 million yuan)						
	1999	2000	2001	2002	2003	2004	2005
Revenue	11,444	13,395	16,386	18,904	21,715	26,356	31,628
Expenditure	13,188	15,887	18,903	22,053	24,650	28,361	33,708
Overall balance	-1,744	-2,491	-2,517	-3,150	-2,935	-2,005	-2,080
Deficit financing	3,715	4,180	4,604	5,679	6,154	6,879	...
Domestic bonds	3,715	4,157	4,484	5,679	6,033	6,726	...
Foreign borrowing	0	23	120	0	121	145	...

Sources: *China Statistical Yearbook, 2005*; Figures for 2005 are from the fiscal report presented at the National People's Congress.

7. Balance of Payments

	(US\$100 million)			
	2002	2003	2004	1H-2005
Trade balance of goods	441.7	446.5	589.8	542.3
Exports, fob	3,256.50	4,382.70	5,933.90	3,424.50
Imports, fob	-2,814.80	-3,936.20	-5,344.10	-2,882.30
Balance of invisible trade	-67.8	-85.7	-97	-39.3
Income balance	-149.5	-78.4	-35.2	48.7
Current transfers	129.8	176.3	229	120.9
Current account	354.2	458.7	686.6	672.6
Capital and financial account	322.9	527.3	1,106.60	383
Capital account	-5	-0.5	-0.7	21.5
Financial account	323.4	527.7	1,107.30	361.4
Direct investment	467.9	472.3	531.3	224.8
Outflow	-25.2	-82.8	-18.1	-39
Inflow	493.1	555.1	549.4	263.7
Portfolio Investment	-103.4	114.3	196.9	-9.7
Asset	-120.9	29.8	64.9	-84.6
Debts	17.5	84.4	132	74.9
Other investment	-41.1	-58.8	379.1	146.3
Asset	-30.8	-179.2	19.8	-180.9
Debts	-10.3	120.4	359.3	327.2
Net errors and omissions	77.9	184.2	270.5	-51.1
Reserve assets	-755.1	-1,170.2	-2,063.6	-1,004.5

Sources: *China Statistical Yearbook*, various editions. Figures for first half of 2005 from China's National Foreign Currency Management Bureau.