

CRS Issue Brief for Congress

Received through the CRS Web

China's Economic Conditions

Updated April 25, 2005

Wayne M. Morrison
Foreign Affairs, Defense, and Trade Division

CONTENTS

SUMMARY

MOST RECENT DEVELOPMENTS

BACKGROUND AND ANALYSIS

An Overview of China's Economic Development

- China's Economy Prior to Reforms

- The Introduction of Economic Reforms

- China's Economic Growth Since Reforms: 1979-2004

- Causes of China's Economic Growth

Measuring the Size of China's Economy

Foreign Direct Investment in China

China's Trade Patterns

- China's Major Trading Partners

- Major Chinese Trade Commodities

Major Long-Term Challenges Facing the Chinese Economy

Outlook for China's Economy and Implications for the United States

China's Economic Conditions

SUMMARY

Since the initiation of economic reforms in 1979, China has become one of the world's fastest-growing economies. From 1979 to 2003, China's real GDP grew at an average rate of 9.3%; it is estimated to have risen by 9.1% in 2004. Many economists speculate that China could become the world's largest economy at some point in the near future, provided that the government is able to continue and deepen economic reforms, particularly in regard to its inefficient state-owned enterprises (SOEs) and the state banking system. Progress in reforming these sectors in recent years has been somewhat mixed.

Trade continues to play a major role in China's booming economy. In 2004, exports rose by 35% to \$593 billion, while imports grew by 36% to \$561 billion — making China the world's third-largest trading economy (after the United States and Germany). China's trade boom is largely the result of large flows of foreign direct investment (FDI) into China (which hit \$64 billion in 2004). According to Chinese data, over half of its trade is accounted for by foreign-invested firms in China.

China experienced some inflationary pressures in 2004, fueled in part by speculation in real estate, over-investment in certain industries, and rising costs for energy and raw materials. The Chinese government responded by raising interest rates and using administrative controls to slow investment in certain sectors.

After many years of difficult negotiations, China became a member of World Trade Organization (WTO) in December 2001. China agreed to significantly reduce a wide variety of tariff and nontariff barriers over the next few years. China's WTO accession is expected to have a significant impact on its economy by greatly diminishing the level of trade protectionism afforded by China to various sectors. Several of China's heavily protected industries (such as automobile manufacturing), various services (such as banking) and certain agricultural sectors (such as corn), could be negatively affected by China's WTO commitments, while many of its labor-intensive industries (especially textiles and apparel) will likely benefit significantly. A major challenge facing the Chinese government is to develop an adequate social safety net to assist workers that are displaced by economic reforms.

China's economy continues to be a concern to U.S. policymakers. On the one hand, China's economic growth presents huge opportunities for U.S. exporters. On the other hand, the surge in Chinese exports to the United States has put competitive pressures on many U.S. industries. Many U.S. policymakers have argued that greater efforts should be made to pressure China to fully implement its WTO commitments and to change various economic policies deemed harmful to U.S. economic interests, such as its pegging of its currency (the *yuan*) to the U.S. dollar and its use of subsidies to support SOEs.

MOST RECENT DEVELOPMENTS

On April 20, 2005, the Chinese government announced that first quarter real GDP grew by 9.5% in 2005.

On April 14, 2005, the House Ways and Means Committee held a hearing on U.S.-China economic relations and China's role in the world economy. Administration officials were urged by several Members to take a tougher stand on China's currency peg.

BACKGROUND AND ANALYSIS

An Overview of China's Economic Development

China's Economy Prior to Reforms

Prior to 1979, China maintained a centrally planned, or command, economy. A large share of the country's economic output was directed and controlled by the state, which set production goals, controlled prices, and allocated resources throughout most of the economy. During the 1950s, all of China's individual household farms were collectivized into large communes. To support rapid industrialization, the central government undertook large-scale investments in physical and human capital during the 1960s and 1970s. As a result, by 1978 nearly three-fourths of industrial production was produced by centrally controlled state-owned enterprises (SOEs) according to centrally planned output targets. Private enterprises and foreign-invested firms were nearly nonexistent. A central goal of the Chinese government was to make China's economy relatively self-sufficient. Foreign trade was generally limited to obtaining only those goods that could not be made or obtained in China.

Government policies kept the Chinese economy relatively stagnant and inefficient, mainly because there were few profit incentives for firms and farmers; competition was virtually nonexistent, and price and production controls caused widespread distortions in the economy. Chinese living standards were substantially lower than those of many other developing countries. The Chinese government hoped that gradual reform would significantly increase economic growth and raise living standards.

The Introduction of Economic Reforms

Beginning in 1979, China launched several economic reforms. The central government initiated price and ownership incentives for farmers, which enabled them to sell a portion of their crops on the free market. In addition, the government established four special economic zones for the purpose of attracting foreign investment, boosting exports, and importing high technology products into China. Additional reforms, which followed in stages, sought to decentralize economic policymaking in several economic sectors, especially trade. Economic control of various enterprises was given to provincial and local governments, which were generally allowed to operate and compete on free market principles, rather than under the direction and guidance of state planning. Additional coastal regions and cities

were designated as open cities and development zones, which allowed them to experiment with free market reforms and to offer tax and trade incentives to attract foreign investment. In addition, state price controls on a wide range of products were gradually eliminated.

China's Economic Growth Since Reforms: 1979-2004

Since the introduction of economic reforms, China's economy has grown substantially faster than during the pre-reform period (see **Table 1**). Chinese statistics show real GDP from 1979 to 2004 growing at an average annual rate of 9.3%, making China one of the world's fastest-growing economies.¹ Real GDP grew by 9.5% in the first quarter of 2005.

Table 1. China's Average Annual Real GDP Growth Rates, 1960-2005*

Time Period	Average Annual % Growth
1960-1978 (pre-reform)	5.3
1979-2004 (post-reform)	9.3
1990	3.8
1991	9.3
1992	14.2
1993	13.5
1994	12.7
1995	10.5
1996	9.7
1997	8.8
1998	7.8
1999	7.1
2000	8.0
2001	7.3
2002	8.0
2003	9.1
2004	9.1
2005 (first quarter)	9.5

Sources: Official Chinese government data and estimates by Global Insight.

Causes of China's Economic Growth

Economists generally attribute much of China's rapid economic growth to two main factors: large-scale capital investment (financed by large domestic savings and foreign

¹ China's statistical methods and standards have come under criticism by various international agencies, especially regarding how China measures its GDP growth, which, many analysts contend, is often overstated.

investment) and rapid productivity growth. These two factors appear to have gone together hand in hand. Economic reforms led to higher efficiency in the economy, which boosted output and increased resources for additional investment in the economy.

China has historically maintained a high rate of savings. When reforms were begun in 1979, domestic savings as a percentage of GDP stood at 32%. However, most Chinese savings during this period were generated by the profits of SOEs, which were used by the central government for domestic investment. Economic reforms, which included the decentralization of economic production, led to substantial growth in Chinese household savings (these now account for half of Chinese domestic savings). As a result, savings as a percentage of GDP has steadily risen; it was 42% in 2002, among the highest savings rates in the world.

Several economists have concluded that productivity gains (i.e., increases in efficiency in which inputs are used) were another major factor in China's rapid economic growth. The improvements to productivity were caused largely by a reallocation of resources to more productive uses, especially in sectors that were formerly heavily controlled by the central government, such as agriculture, trade, and services. For example, agricultural reforms boosted production, freeing workers to pursue employment in more productive activities in the manufacturing sector. China's decentralization of the economy led to the rise of nonstate enterprises, which tended to pursue more productive activities than the centrally controlled SOEs. Additionally, a greater share of the economy (mainly the export sector) was exposed to competitive forces. Local and provincial governments were allowed to establish and operate various enterprises on market principles, without interference from the central government. In addition, foreign direct investment (FDI) in China brought with it new technology and processes that boosted efficiency.

Measuring the Size of China's Economy

The actual size of the China's economy has been a subject of extensive debate among economists. Measured in U.S. dollars using nominal exchange rates, China's GDP in 2004 was about \$1.6 trillion; its per capita GDP (a commonly used living-standards measurement) was \$1,230. Such data would indicate that China's economy and living standards are significantly lower than those of the United States and Japan, respectively considered to be the number-one and number-two largest economies (see **Table 2**).

Many economists, however, contend that using nominal exchange rates to convert Chinese data into U.S. dollars substantially underestimates the size of China's economy. This is because prices in China for many goods and services are significantly lower than those in the United States and other developed countries. Economists have attempted to factor in these price differentials by using a purchasing power parity (PPP) measurement, which attempts to convert foreign currencies into U.S. dollars on the basis of the actual purchasing power of such currency (based on surveys of the prices of various goods and services) in each respective country. This PPP exchange rate is then used to convert foreign economic data in national currencies into U.S. dollars.

Because prices for many goods and services are significantly lower in China than in the United States and other developed countries (while prices in Japan are higher), the PPP

exchange rate raises the estimated size of Chinese economy to about \$7.5 trillion, significantly higher than Japan's GDP in PPPs (\$3.7 trillion), and about 64% the size of the U.S. economy. PPP data also raise China's per capita GDP to \$5,780. The PPP figures indicate that while the size of China's economy is substantial, its living standards fall far below those of the U.S. and Japan. China's per capita GDP on a PPP basis is only 14.4% of U.S. levels. Thus, even if China's GDP were to overtake that of the United States in the next decade or two, its living standards would remain substantially below those of the United States for many years to come.

Table 2. Comparisons of U.S., Japanese, and Chinese GDP and Per Capita GDP in Nominal U.S. Dollars and PPP, 2004

Country	Nominal GDP (\$ billions)	GDP in PPP (\$ billions)	Nominal Per Capita GDP	Per Capita GDP in PPP
United States	11,728	11,728	40,020	40,020
Japan	4,672	3,719	36,690	29,200
China	1,601	7,512	1,230	5,780

Sources: Economist Intelligence Unit Data Services.

Note: PPP data for China should be interpreted with caution. China is not a fully developed market economy; the prices of many goods and services are distorted due to price controls and government subsidies.

Foreign Direct Investment in China

China's trade and investment reforms and incentives led to a surge in foreign direct investment (FDI), which has been a major source of China's capital growth. Annual utilized FDI in China grew from \$636 million in 1983 to an estimated \$64.0 billion in 2004. The cumulative level of FDI in China stood at \$563 billion at the end of 2004. Analysts predict that FDI will continue to pour into China as investment barriers are reduced under China's WTO commitments and Chinese demand for imports continue to increase. The Economist Intelligence Unit projects that FDI in China will hit \$80 billion by 2009.

Based on cumulative FDI (1979-2004), about 43% of FDI in China has come from Hong Kong. The United States is the second-largest investor in China, accounting for 8.5% (\$48.0 billion) of total FDI, followed by Japan (\$46.8 billion), Taiwan (\$39.6 billion), and the Virgin Islands (\$36.9 billion) and South Korea (\$25.9 billion) (see **Table 3**). U.S. FDI in China for 2004 was \$3.9 billion, accounting for 6.1% of FDI for that year, and ranked 5th after Hong Kong, the Virgin Islands, South Korea, and Japan.² Major U.S. investors in China (based on 2003 sales volumes), include Motorola (\$5,763 million in sales volume), General Motors (\$2,242 million), Dell Computer (\$2,123 million), Hewlett Packard (\$1,341 million), Kodak (\$606 million).³

² The Virgin Islands is a large source of FDI because of its status as a tax haven. Much of the FDI originating from Hong Kong comes from non-Hong Kong investors, such as Taiwanese.

³ Source: Chinese Ministry of Commerce.

Table 3. Major Foreign Investors in China: 1979-2004
(\$ billions and % of total)

Country	Cumulative Utilized FDI: 1979-2004		Utilized FDI in 2004	
	Amount (\$ billions)	% of Total	Amount (\$ billions)	% of Total
Total	563.8	100.0	64.0	100.0
Hong Kong	241.6	42.9	19.0	29.7
United States	48.0	8.5	3.9	6.1
Japan	46.8	8.3	5.5	8.6
Taiwan	39.6	7.0	3.1	4.8
Virgin Islands	36.9	6.5	6.7	10.5
South Korea	25.9	4.6	6.2	9.7

Source: Chinese government statistics. Top six investors according to cumulative FDI from 1979 to 2004.

China's Trade Patterns

Economic reforms have transferred China into a major trading power. Chinese exports rose from \$14 billion in 1979 to \$593 billion in 2004, while imports over this period grew from \$16 billion to \$561 billion (see **Table 4**). In 2004, China surpassed Japan as the world's third-largest trading economy (after the United States and Germany). China's trade continues to grow dramatically: In 2003, Chinese exports and imports rose by 35% and 40%, respectively, over 2002 levels. In 2004, exports and imports rose by 35% and 36%, respectively. Chinese exports and imports in 2004 were both more than twice as large as those in 2001.

Table 4. China's Merchandise World Trade, 1979-2004
(\$ billions)

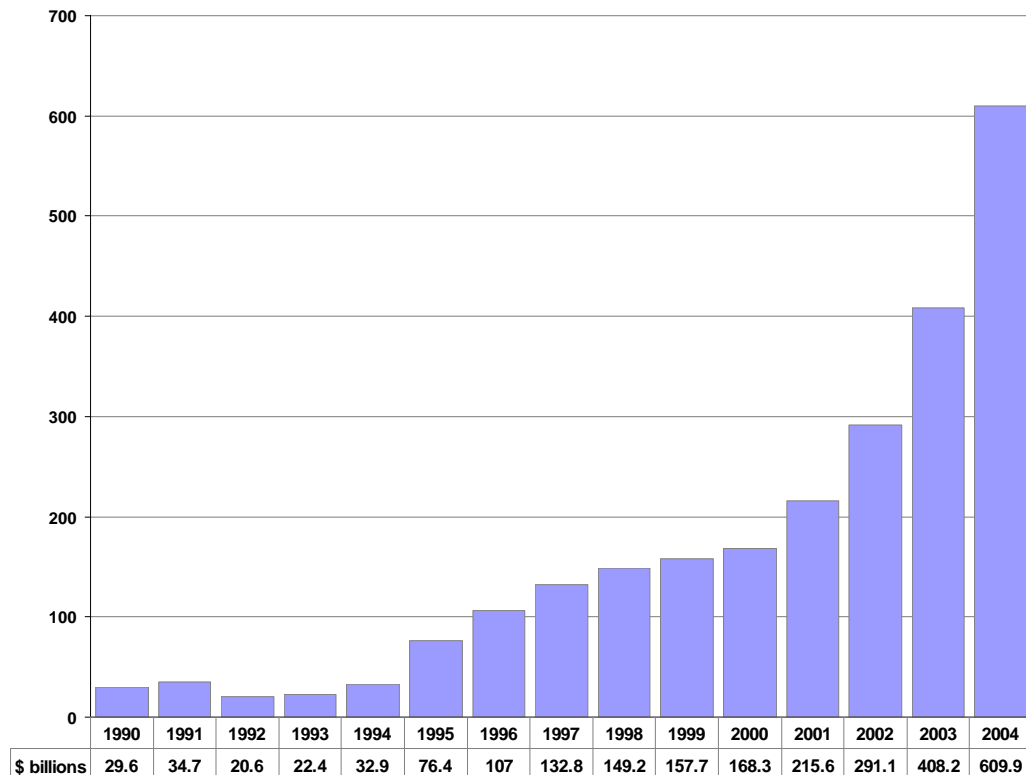
Year	Exports	Imports	Trade Balance
1979	13.7	15.7	-2.0
1980	18.1	19.5	-1.4
1981	21.5	21.6	-0.1
1982	21.9	18.9	2.9
1983	22.1	21.3	0.8
1984	24.8	26.0	-1.1
1985	27.3	42.5	-15.3
1986	31.4	43.2	-11.9
1987	39.4	43.2	-3.8
1988	47.6	55.3	-7.7

Year	Exports	Imports	Trade Balance
1989	52.9	59.1	-6.2
1990	62.9	53.9	9.0
1991	71.9	63.9	8.1
1992	85.5	81.8	3.6
1993	91.6	103.6	-11.9
1994	120.8	115.6	5.2
1995	148.8	132.1	16.7
1996	151.1	138.8	12.3
1997	182.7	142.2	40.5
1998	183.8	140.2	43.6
1999	194.9	165.8	29.1
2000	249.2	225.1	24.1
2001	266.2	243.6	22.6
2002	325.6	295.2	30.4
2003	438.4	412.8	25.6
2004	593.4	561.4	32.0

Source: International Monetary Fund, *Direction of Trade Statistics*, and official Chinese statistics.

Historically, China has run trade deficits in some years and surpluses in others. However, over the past 11 years, China has run trade surpluses; in 2004 that surplus was \$32 billion. Merchandise trade surpluses and large-scale foreign investment have enabled China to accumulate the world's second-largest foreign exchange reserves (after Japan), estimated to have reached nearly \$610 billion at the end of 2004. As seen in **Figure 1**, China's accumulation of foreign exchange reserves has been particularly acute over the past few years; they grew by \$117 billion in 2003 and by \$201 billion in 2004.

**Figure 1. China's Foreign Exchange Reserves, 1990-2004
(\$ billions)**



Source: Official Chinese government data.

China's Major Trading Partners

China's trade data often differ significantly from those of its major trading partners. This is due to the fact that a large share of China's trade (both exports and imports) passes through Hong Kong (which reverted back to Chinese rule in July 1997 but is treated as a separate customs area by most countries, including China and the United States). China treats a large share of its exports through Hong Kong as Chinese exports to Hong Kong for statistical purposes, while many countries that import Chinese products through Hong Kong generally attribute their origin to China for statistical purposes. According to Chinese trade data, its top five trading partners in 2004 were the European Union (EU), the United States, Japan, Hong Kong, and the 10 nations that constitute the Association of Southeast Asian Nations (ASEAN) (see **Table 5**). China's largest export markets were the United States, Hong Kong, and the EU, while its top sources for imports were Japan, the EU, and Taiwan (the United States ranked sixth).

U.S. trade data indicate that the importance of the U.S. market to China's export sector is likely much higher than is reflected in Chinese trade data. Based on U.S. data on Chinese exports to the United States (which, as noted, do not agree with Chinese data), and Chinese data on total Chinese exports, it is estimated that Chinese exports to the United States as a share of total Chinese exports grew from 15.3% in 1986 to 33.1% in 2004.

A growing level of Chinese exports is from foreign-funded enterprises (FFE) in China. According to Chinese data, about half of its trade in 2002 was conducted by FFEs. A large share of these FFEs are owned by Hong Kong and Taiwan investors, many of whom have shifted their labor-intensive, export-oriented, firms to China to take advantage of low-cost labor. A significant share of the products made by such firms is exported to the United States. Chinese data indicate that the share of China's exports produced by foreign-invested enterprises in China rose from 2% in 1986, to 41% in 1996, to 57% in 2004.

Table 5. China's Top Five Trading Partners: 2004
(\$ billions)

Country	Total Trade	Chinese Exports	Chinese Imports	China's Trade Balance
European Union	177.3	95.9	63.4	32.5
United States	169.7	125.0	44.7	80.3
Japan	167.9	73.5	94.4	-20.9
Hong Kong	112.7	100.9	11.8	89.1
ASEAN*	105.9	42.9	63.0	-20.1

*Association of Southeast Asian Nations (ASEAN) member countries are Indonesia, Malaysia, the Philippines, Singapore, Thailand, Brunei, Cambodia, Laos, Myanmar, and Vietnam.

Source: Official Chinese trade data.

Note: Chinese data on its bilateral trade often differ substantially from the official trade data of other countries on their trade with China.

Major Chinese Trade Commodities

China's abundance of cheap labor has made it internationally competitive in many low-cost, labor-intensive manufactures. As a result, manufactured products constitute an increasingly larger share of China's trade. A large share of China's imports, such as raw materials, components and parts, and production machinery is used to manufacture products for export. For example, China imports cotton and textile-production machinery to produce textile and apparel items. A substantial amount of China's imports comprises parts and components that are assembled in Chinese factories (major products include consumer electronic products and computers), then exported.

China's top five imports in 2004 were electrical machinery and parts; boilers, machinery, mechanical appliances, and parts; crude oil; plastics; and organic chemicals (see **Table 6**). China's top five exports in 2004 were boilers, machinery, mechanical appliances and parts; electrical machinery and parts; apparel; furniture, bedding, and lamps, and optical, photo, and medical equipment and parts (see **Table 7**).

Table 6. Major Chinese Imports, 2002-2004

(\$ billions)

Commodity	2002	2003	2004	2004/2003 % change
Electrical machinery and equipment and parts; sound recorders and reproducers, television recorders and reproducers, parts and accessories. ^a	26.4	41.9	61.4	46.8
Boilers, machinery, mechanical appliances, and parts. ^b	21.2	29.8	38.6	29.5
Crude oil	12.8	19.8	33.9	71.1
Plastics	17.4	21.0	28.1	33.4
Organic chemicals	11.2	16.0	23.8	48.8

Source: Global Trade Atlas

a. Electronic integrated circuits and micro-assemblies and parts constitute a large share of these imports.

b. Office machines and automatic data-processing machines (such as computers) and parts constitute a large share of these imports.

Table 7. Major Chinese Exports, 2002-2004

(\$billions)

Commodity	2002	2003	2004	2004/2003 % change
Boilers, machinery, mechanical appliances, and parts	50.9	83.4	118.3	41.8
Electrical machinery and equipment and parts; sound recorders and reproducers, television recorders and reproducers, parts and accessories	65.2	89.0	129.7	45.7
Apparel	36.6	45.8	54.8	19.7
Furniture, bedding, and lamps	9.9	12.9	17.3	34.3
Optical, photo, and medical equipment and parts	7.4	10.6	16.3	53.9

Source: Global Trade Atlas.

Major Long-Term Challenges Facing the Chinese Economy

China's economy has shown remarkable economic growth over the past several years, and many economists project that it will enjoy fairly healthy growth in the near future. However, economists caution that these projections are likely to occur only if China continues to make major reforms to its economy. Failure to implement such reforms could endanger future growth.

- **State-owned enterprises (SOEs)**, which account for about one-third of Chinese industrial production and employ nearly two-thirds of urban workers, put an increasingly heavy strain on China's economy. Over half are believed to lose money and must be supported by subsidies, mainly through state banks. Government support of unprofitable SOEs diverts resources away from potentially more efficient and profitable enterprises. In addition, the poor financial condition of many SOEs makes it difficult for the government to reduce trade barriers out of fear that doing so would lead to widespread bankruptcies among many SOEs.
- **The banking system** faces several major difficulties due to its financial support of SOEs and its failure to operate solely on market-based principles. China's banking system is regulated and controlled by the central government, which sets interest rates and attempts to allocate credit to certain Chinese firms. The central government has used the banking system to keep afloat money-losing SOEs by pressuring state banks to provide low-interest loans, without which a large number of the SOEs would likely go bankrupt. Currently, over 50% of state-owned bank loans now go to the SOEs, even though a large share of loans are not likely to be repaid. Ernst & Young estimates that the level of nonperforming loans by Chinese banks in 2002 was \$480 billion (equal to about 43% of China's GDP).⁴ The high volume of bad loans now held by Chinese banks poses a serious threat to China's banking system. Three out of the four state commercial banks are believed to be insolvent. The precarious financial state of the Chinese banking system has made Chinese reformers reluctant to open the banking sector to foreign competition. Corruption poses another problem for China's banking system because loans are often made on the basis of political connections. This system promotes widespread inefficiency in the economy because savings are generally not allocated on the basis of obtaining the highest possible returns.
- **China's agricultural system** is highly inefficient due to government policies that seek to maintain a 95% self-sufficiency rate in grains, mainly through the extensive use of subsidies and restrictive trade barrier. These policies divert resources from more productive economic sectors and keep domestic prices for many agricultural products above world prices.
- **Infrastructure bottlenecks**, such as inadequate transportation and energy systems, pose serious challenges to China's ability to maintain rapid economic growth. China's investment in infrastructure development has failed to keep pace with its economic growth. The World Bank estimates that transportation bottlenecks reduce China's GDP growth by 1% annually. Chronic power shortages are blamed for holding China's industrial growth to 80% of its potential. Transportation bottlenecks and energy shortages also add inflationary strains to the economy because supply cannot keep up with demand.

⁴ Ernst & Young Asia Pacific Financial Solutions, *Nonperforming Loan Report, Asia, 2002*.

- **The lack of the rule of law** in China has led to widespread government corruption, financial speculation, and misallocation of investment funds. In many cases, government “connections,” not market forces, are the main determinant of successful firms in China. Many U.S. firms find it difficult to do business in China because rules and regulations are generally not consistent or transparent, contracts are not easily enforced, and intellectual property rights are not protected (due to the lack of an independent judicial system). The lack of the rule of law in China limits competition and undermines the efficient allocation of goods and services in the economy. In addition, the Chinese government does not accept the concept of private ownership of land and assets in China.
- **A wide variety of social problems** has arisen from China’s rapid economic growth and extensive reforms, including pollution, a widening of income disparities between the coastal and inner regions of China, and a growing number of bankruptcies and worker layoffs. This poses several challenges to the government, such as enacting regulations to control pollution, focusing resources on economic development in the hinterland, and developing modern fiscal and tax systems to address various social concerns (such as poverty alleviation, education, worker retraining, and pensions). In addition, China faces a serious HIV/AIDS crisis. A 2002 report by the United Nations stated that China was on the verge of “catastrophe that could result in unimaginable suffering, economic loss and social devastation,” due to the rapid rise of HIV/AIDS in China.

Outlook for China’s Economy and Implications for the United States

The short-term outlook for the Chinese economy appears to be positive, but it will likely be strongly influenced by the government’s ability to reform the SOEs and banking system to make them more responsive to market forces, to fully implement its WTO commitments, and to assist workers who lose their jobs due to economic reforms (in order to maintain social stability). Global Insight, an economic forecasting firm, projects that China’s real GDP will grow by 9.5% in 2005 and at an average annual rate of 7.0% from 2006 to 2010.⁵ A 7% GDP growth rate would enable China to double its GDP in 10 years.

China’s rise as an economic superpower is likely to pose both opportunities and challenges for the United States and the world trading system. China’s rapid economic growth has boosted incomes and is making China a huge market for a variety of goods and services. In addition, China’s abundant low-cost labor has led multinational corporations to shift their export-oriented, labor-intensive manufacturing facilities to China. This process has lowered prices for consumers, boosting their purchasing power. It has also lowered costs for firms that import and use Chinese-made components and parts to produce manufactured goods, boosting their competitiveness. Conversely, China’s role as a major international

⁵ Global Insight, *China: Interim Forecast Analysis: Economic Growth*, Feb. 11, 2005.

manufacturer has raised a number of concerns. Many developing countries worry that growing FDI in China is coming at the expense of FDI in their country. Policymakers in both developing and developed countries have expressed concern over the loss of domestic manufacturing jobs that have shifted to China (as well as the downward pressures on domestic wages and prices that may occur from competing against low-cost Chinese-made goods). Japan has complained that China's currency peg and low-cost manufacturing have contributed to deflationary pressures on the Japanese economy, which, they claim, has forced Japan to intervene in currency markets to keep the yen weak against the dollar in order to stay competitive with Chinese goods in U.S. markets.

China is attempting to establish and promote companies that can compete globally, especially in advanced technologies. For example, on December 7, 2004, Lenovo Group Limited, a computer company primarily owned by the Chinese government, purchased IBM's personal computer division. U.S. firms are likely to face increasing competitive pressures from China in a variety of goods and services industries — and not just those that are labor-intensive.

China's rapid economic growth and continued expansion of its manufacturing base are fueling a sharp demand for energy and raw materials, which is becoming an increasingly important factor in determining world prices for such commodities. According to the International Energy Agency, China accounted for one-third of the rise in daily global oil consumption in 2003 and is projected to account for one-third of the rise in consumption in 2004. China has become the world's second-largest oil importer, and it is reportedly the largest consumer of steel, cement, and copper.