
Key Targets in the 12th Five-Year Plan and Policies for their Realization —Reasons for the 7% Growth Target—

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Summary

1. The 12th Five-Year Plan identifies the shift to a new development model as China's most important priority. While this goal reflects the existence of favorable factors, including China's latecomer advantage in relation to science and technology, and the existence of massive latent demand in its markets, it is also an indication that China is keenly aware of changes in its domestic and external environment and alarmed that it will not be able to cope adequately with those changes under its existing growth model and living standard improvement measures.
2. Compared with current trends and the growth target in the 11th Five-Year Plan, the yearly average growth rate target adopted for the 12th Five-Year Plan is modest at just 7%. This target can be seen as an expression of the Hu Jintao administration's determination to ensure that local governments, which are still eager to pursue high growth, will instead give first priority to the shift to a economic development model by working to raise the quality of economic growth through the improvement of sustainability and the correction of the imbalance.
3. Under the 12th Five-Year Plan, China aims to reconcile a change in its economic development model with sustainable growth. The key policies listed in the plan for the achievement of these two goals are (1) the expansion of consumption, (2) the improvement of industrial competitiveness, (3) regional development centering on multiple urban areas, and (4) an increased emphasis on two-way external economic relations. Existing initiatives, such as the development of inland regions and the advancement of manufacturing, will be maintained. At the same time, China will adopt new approaches that differ from those of past, including the enhancement of social security systems as part of efforts to boost consumption, as well as the promotion of urbanization and the development of the energy conservation industry.
4. Of the four priority policies, the expansion of consumption is the most crucial from the perspective of creating a new growth engine to replace growth driven primarily by investment and exports.
5. To achieve this transition to a new economic development model, China will need to combine caution with a determination to apply basic principles consistently. For example, hasty moves to raise minimum wages could cause income to decline because of restructuring triggered by the resulting pressure on corporate finances. It will also be necessary to reduce the burden on the wealthy and state-owned enterprises, for which the implementation of the 12th Five-Year Plan will not be entirely beneficial, but excessive compromises could hinder efforts to strengthen the redistribution function of government finances and stimulate industrial activity through competition among companies.
6. Will it be possible to change the commitment to high growth that imbues China's leadership, or the excessive emphasis on investment expansion that is a feature of its economic management? To achieve this, it will be necessary to create personnel evaluation systems that encourage senior executives to give priority to the shift to a new economic development model. Based on an economic cycle in which impulsive investment by local governments causes the growth rate to peak in years when the National Congress of the Communist Party of China are held, growth is likely to surge in late 2011 and during 2012. This could hinder the economic soft landing that China hopes to achieve under the 12th Five-Year Plan.

Introduction

In recent years the Hu Jintao administration has sought to shift from investment-led economic growth to growth driven by consumption. In line with this basic stance, the government introduced policies designed to realize this goal, specifically the improvement of national living standards and an increased commitment to energy conservation, and environmental protection.

This position was promoted within and beyond the government in the 11th Five-Year Plan, which began in 2006, and in the Political Report to the 17th National Congress of the Communist Party of China in 2007. However, the change in the economic growth model was subsequently shelved as the government responded to the global financial crisis triggered by the 2008 Lehman shock by giving priority to economic measures, including monetary easing and stimulatory measures worth 4 trillion yuan. For a time there was also doubt about the achievability of the goal set down in the 11th Five-Year Plan for the reduction of energy consumption.

Under the 12th Five-Year Plan, the Hu Jintao administration is again seeking to transform China's economic growth model. As is usual for a five-year plan, the 12th Five-Year Plan contains numerous goals and priority policies. However, explanations presented by Premier Wen Jiabao and Vice Premier Li Keqiang when the plan was at the drafting stage and comments by Premier Wen at a press conference following the conclusion of the National People's Congress in March 2011 clearly indicate the shift to a new economic development model is the most important goal in the 12th Five-Year Plan.

In this article, we will analyze the composition and characteristics of the 12th Five-Year Plan, including the policies through which China hopes to maintain growth while changing its economic development model, and the challenges that are likely to emerge during this process. In particular, we will examine the reasons why China has set its target for average annual growth at just 7%, the lowest level ever, and the challenges on the path to stable growth.

Since the adoption of the reform and open-door policy, and in particular since the 1990s, the Chinese economy has tended to achieve its highest growth in years in which the National Congress of the Communist Party of China were held. We also investigate whether it is possible to control the economic cycle in this way.

This article consists of three parts. Part 1 begins with a general overview of the content of the 12th Five-Year Plan. This is followed by an analysis of the reasons why the shift in the direction of economic development has been identified as a key objective, and the intentions of the central government in setting the target for the average annual economic growth rate at 7%. Part 2 examines the four policies through which China aims to reconcile the shift in its development model with sustained growth. In Part 3 we will look at the challenges that will need to be overcome as China implements this shift in its development model, and the influence of an economic cycle based on political factors on the 12th Five-Year Plan.

1. Why 7%?

(1) The Overall Composition of the 12th Five-Year Plan

The adoption of a new economic development model is generally seen as the most important priority under the Twelfth Five-Year Plan For National Economic & Social Development Of The People's Republic Of China (the "12th Five-Year Plan"), which will cover the period from 2011 to 2015. Evidence of this thinking can be found in the overall structure of the plan.

As shown in Table 1, the 12th Five-Year Plan consists of a preamble and 16 sections. Each section is further divided into between two and seven chapters. In all there are 16 sections and 62 chapters covering a wide range of fields, including the economy, society, culture, government administration and national defense. In keeping with its role as medium-term state policy, the Five-Year Plan also identifies numerous targets and priority projects in each area, and for this reason it is difficult

Table 1 Structure of the 12th Five-Year Plan

Sections and Chapters	
Preamble (The significance of the plan)	
Section 1: Changing the pattern and opening up a new phase of Scientific Development	
	(1) The development environment
	(2) Guiding philosophy
	(3) Key goals
	(4) Policy direction
Section 2: Strengthening agriculture, enriching farmers and accelerating the development of new socialist farming communities	
	(5) Accelerated development of modern agriculture
	(6) Expansion of income expansion routes for farmers
	(7) Improvement of rural production and living conditions
	(8) Improvement of rural development mechanisms
Section 3: Enhancing core industrial competitiveness through model changes and upgrading	
	(9) Restructuring and improvement of manufacturing industries
	(10) Incubation and development of new strategic industries
	(11) Accelerated innovation of energy production and utilization methods
	(12) Development of comprehensive traffic and transportation systems
	(13) General improvement in information technology level
	(14) Development of marine economy
Section 4: Improving the environment, accelerating the development of service industries	
	(15) Accelerated development of production-related service industries
	(16) Emphasis on development of consumer-related service industries
	(17) Creation of an environment that will contribute to service industry development
Section 5: Optimizing structure and accelerating harmonious regional development and healthy urbanization	
	(18) Implementation of overall regional development strategy
	(19) Implementation of major function zone strategy
	(20) Promotion of dynamic, sustained urbanization
Section 6: Building a resource-conserving and environment-friendly society through green development	
	(21) Active response to global climate change
	(22) Reinforcement of resource conservation and management
	(23) Emphasis on development of recycling-based economy
	(24) Reinforcement of environmental protection
	(25) Protection and accelerated restoration of ecosystems
	(26) Reinforcement of water management and disaster prevention and mitigation systems
Section 7: Driving innovation and implementing strategies to achieve national development through science, technology and education, building national strength based on human resources	
	(27) Improvement of science/technology innovation capacity
	(28) Accelerated reform and development of education
	(29) Development of a wide range of high-quality human resources
Section 8: Improving welfare and establishing and developing basic public service systems	
	(30) Improvement of standard of basic public services
	(31) Implementation of strategies that give priority to employment
	(32) Rationalization of income distribution relationships
	(33) Development of social security systems covering urban and rural residents
	(34) Completion of basic healthcare and public health systems
	(35) Improvement of housing guarantee standards
	(36) Comprehensive initiatives to solve population problems
Section 9: Strengthening and innovating social management through a combination of countermeasures and fundamental measures	
	(37) Innovation of social management systems
	(38) Reinforcement of autonomy and services in urban and rural communities
	(39) Increased emphasis on social organization development
	(40) Improvement of mechanisms to protect the rights and interests of the masses
	(41) Increased emphasis on reinforcement of public safety systems
Section 10: Accelerated achievement of cultural development and prosperity through transmission of knowledge and innovation	
	(42) Improvement of cultural assets of all ethnic groups
	(43) Promotion of cultural innovation
	(44) Achievement of prosperity and development for cultural businesses and industries
Section 11: Perfecting the socialist market economy through reform	
	(45) Maintenance and improvement of the basic economic system
	(46) Reform of administrative systems
	(47) Accelerated reform of fiscal and taxation systems
	(48) Deepening of financial system reform
	(49) Reform of resource product prices, deepening of environmental protection levy reforms
Section 12: Raising the level of opening through mutual benefit/win-win relationships	
	(50) Improvement of regional opening structures
	(51) Optimization of external trade structures
	(52) Formulation of integrated policies based on <i>yin jin lai</i> (introducing foreign investment) and <i>zou chu qu</i> (expanding overseas)
	(53) Active participation in governance of global economy and regional cooperation
Section 13: Advancing democracy and promoting the development of a socialist political civilization	
	(54) Advancement of socialist democratic politics
	(55) Comprehensive reform of legal systems
	(56) Increased efforts to prevent corruption and encourage honesty
Section 14: Deepening of cooperation and development of common homeland for the Chinese people	
	(57) Long-term maintenance of prosperity and stability in Hong Kong and Macao
	(58) Peaceful development of cross-strait relations and promotion of national unification
Section 15: Reinforcing defense and army modernization through civil-military integration	
	(59) Reinforcement of defense and army modernization
	(60) Promotion of development through civil-military integration
Section 16: Strengthening implementation and realizing a macroscopic blueprint	
	(61) Improvement of plan implementation and review mechanisms
	(62) Reinforcement of plan adjustment and management

Notes: The figures in parentheses represent consecutive chapter numbers through all sixteen sections.

Source: The original source for the 12th Five-Year Plan is a government website (http://www.gov.cn/2011lh/content_1825838.htm)

to determine the order of priority. Specific information is provided in the second and subsequent sections, while the first section is devoted to a general and condensed discussion of general issues and key targets during the period covered by the plan.

Chapter 2 of the first section of the plan deals with the guiding philosophy. The Scientific Development Concept is identified as the main theme, and an accelerated shift to a new economic development model as the main direction. The plan also refers to the connection between the Scientific Development Concept and the change in the economic development model, which is defined as “a path that must be followed under the Scientific Development Concept”⁽¹⁾. All of this indicates that the change in the economic development model has been positioned as the most important goal for the period covered by the plan.

Aspects of the plan other than its format point to the same conclusion. For example, Premier Wen Jiabao identified the accelerated shift to a new economic development model as a “key direction” when presenting the draft of 12th Five-Year Plan in October 2010⁽²⁾. In response to a question at a press conference following the conclusion of the National People’s Congress in March 2011, Mr.

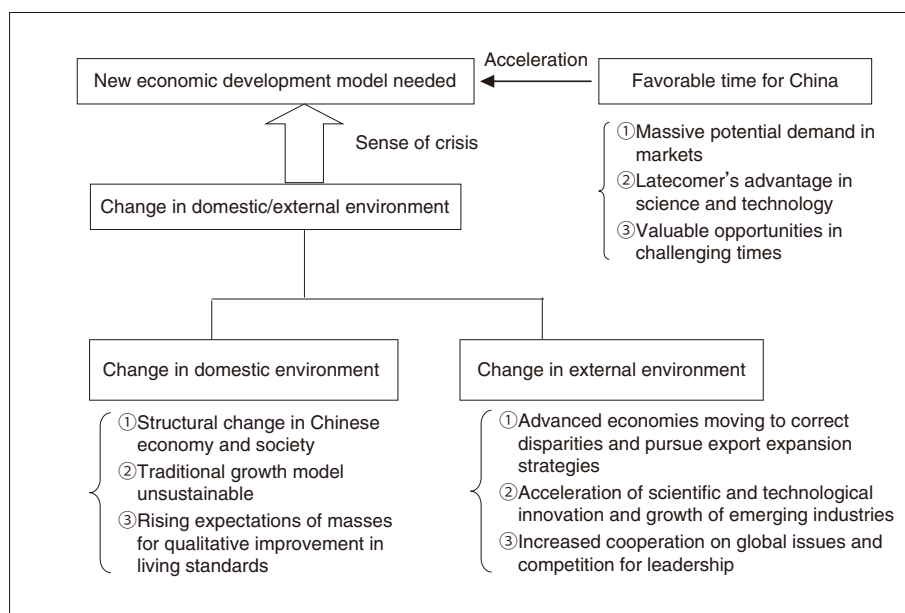
Wen further stated that the change of the economic growth model would remain a key direction not only during the next five years, but also for a considerable period after the completion of the plan⁽³⁾.

(2) Reasons for the Shift to New Economic Development Model

The content of the 12th Five-Year Plan and views expressed by Premier Wen Jiabao both highlight the need to change China’s economic development model. However, little has been said about the reasons for this transition. References to the concept seem to have taken on a rather abstract tone, and explanations are based on vague concepts about changing times. For this reason, the following analysis examines the reasons for change as expressed in Vice Premier Li Keqiang’s explanatory paper⁽⁴⁾.

In gist, Li Keqiang says in his paper that there is an urgent need to change China’s economic growth model during the period of the 12th Five-Year Plan. He cited two reasons for this. First, there have been alarming changes in the domestic and external environment. Second, this is an advantageous time for China to make such a change (Fig. 1).

Fig. 1 Reasons for the Shift to New Economic Development Model



Source: Based on explanatory paper by Vice Premier Li Keqiang, as posted on Xinhua website (http://news.xinhuanet.com/politics/2010-11/14/c_12773751.htm)

The paper divides the reasons for alarm into external and domestic factors and lists three items in each category. On the external side, Mr. Li refers to the growing influence of emerging and developing economies in the world economy and the international financial system because of the international financial crisis and concludes that there has been an upsurge of both cooperation on international problems and also competition for leadership. He also notes that the slow pace of economic recovery and the rise of debt risk since the onset crisis have prompted the advanced economies to change their economic policies, and that this has made export expansion increasingly difficult for China. Mr. Li further comments that the international financial crisis has become a trigger for the acceleration of scientific and technological innovation and the growth of emerging industries on a global scale, and that China is at risk of being left behind in the race to develop new advances in such fields as low-carbon technology and biotechnology.

On the domestic side, Vice Premier Li Keqiang suggests that the Chinese economy has reached a crossroads at which it is in danger of falling into the middle-income trap, although he uses indirect language to make this point. "The transition from a middle-income country to a medium-level developed country is an important phase, but is also a stage at which contradictions expand, as well as the key to climbing over a mountain pass and on toward greater heights"⁽⁵⁾. Mr. Li also recognizes that China is facing limitations in terms of resources and the environment, as well as various types of imbalances, including income disparity and an investment-consumption gap, and that the traditional growth model, which is strongly weighted toward investment and quantitative expansion, is becoming unsustainable as a result. Mr. Li further observes that while China has made some progress in its efforts to achieve qualitative improvement in living standards, there are still considerable gaps between the expectations of the masses and actual conditions in such areas as housing, healthcare, public health, environmental protection and social security. He concludes that existing initiatives are not meeting the aspirations

of the Chinese people in relation to living standards.

The concept of shifting to a new growth model appears to have arisen out of concerns about changes in the domestic and external environment. However, Mr. Li also states that the change should be implemented now because the conditions are favorable for China at this time. He refers specifically to China's latecomer advantage in relation to the development of science and technology, and to the existence of massive potential demand in the Chinese market. Some of his arguments are simply based on the use of logic to argue for change, such as his assertion that challenging times are also times of opportunity. However, it is significant that the decision to make a shift to a new economic development model the most important priority under the 12th Five-Year Plan was based largely on objective arguments pointing to the conclusion that this is a favorable time for such a transition.

(3) Reasoning Behind the 7% Average Growth Target

Section 1/Chapter 3 of the 12th Five-Year Plan lists 24 key numerical targets in four areas (economic development, science/technology/education, resources/environment, living standards) (Table 2). There are two more key numerical targets than in the 11th Five-Year Plan, reflecting the introduction of additional targets in the resource and environment category as a result of changes to the category structure⁽⁶⁾. A detailed analysis shows that the target for the reduction of energy consumption per unit of GDP has been reduced from 20% to 16%. However, the base year for this target is 2010, by which time significant reductions had already been achieved, and in this sense we can conclude that the government has actually set a target that will be more rather than less difficult to achieve. This emphasis on energy conservation and the environment in the targets can be seen as groundwork for a shift in China's approach to economic development, which has tended to accord lower priority to these issues in the past.

The key target that will attract most interest is

Table 2 Key Targets in the 12th Five-Year Plan

Key Targets	Numerical Target
①Average real GDP growth rate during the plan period	7.00%
②GDP contribution from service industries	4-point increase over five years to 47.0%
③Urbanization ratio	4-point increase over five years to 51.5%
④Ratio of R&D expenditure to GDP	0.45-point increase over five years to 2.2%
⑤Patented inventions per 10,000 of population	Increase from 1.7 to 3.3 over five years
⑥Energy consumption per unit of GDP	16% reduction from 2010 level by 2015
⑦CO ₂ emissions per unit of GDP	17% reduction from 2010 level by 2015
⑧Emissions of key pollutants	8% reduction in chemical oxygen demand and SO ₂ emissions and 10% reduction in ammoniac nitrogen and NOx emissions over five years
⑨Per capita real disposable income	Increase in excess of 7% in both urban and rural areas
⑩Construction of urban welfare housing	36 million units during the plan period

Notes: This analysis is based on data extracted from the key targets in Section 1/Chapter 3 of the 12th Five-Year Plan.

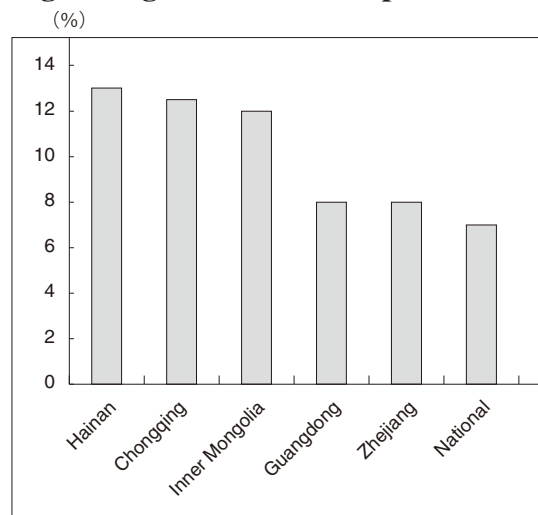
Source: 12th Five-Year Plan

that for the average yearly real GDP growth rate⁽⁷⁾. At 7.0%, the target is significantly lower than the actual average achieved under the 11th Five-Year Plan (11.2% per annum) or recent trends in quarterly data, which put the growth rate for 2010 at around 10%. It is also 0.5 points lower than the growth target adopted for the 11th Five-Year Plan.

Basically there were two reasons for setting the growth rate target at 7.0%. First, the target was intended as a message for local leaders that are focused on high growth to the effect that they should enhance the quality of growth rather than simply increasing the growth rate.

An analysis of the economic growth targets of regional governments during the period covered by the 12th Five-Year Plan range shows that the lowest target is that of Zhejiang Province at around 8%, and that the highest, that of Hainan Province, is around 13% (Fig. 2). While regional five-year plans were formulated before the national plan, regional leaders must have been aware that the Hu Jintao administration had made the transition to a new economic development model its top priority for the 12th Five-Year Plan, since this has been made clear through various channels, including conferences and documents, since the second half of 2010. The fact that local governments have continued to set high growth targets appears to reflect their inability to break away from the behavior pattern of achieving high growth through massive investment because of the implications for

Fig. 2 Regional Growth Aspirations



Notes: The figures for Hainan, Chongqing and Zhejiang are qualified with "about" and those for Guangdong and Inner Mongolia with "at least."

Source: Regional government websites, the 12th Five-Year Plan, etc.

assessments of their own performance. (The link between growth rates and performance assessment will be examined again in Part 3.) We can deduce that this situation led the central government to set a growth target of 7.0%, which is lower than the targets of any province, autonomous region or municipality. The target appears to reflect a strong desire for the regions to give priority to a shift to a new economic development model during the five-year plan period, instead of focusing exclusively on growth rates. Evidence of this can be found in Section 1/Chapters 3 and 4 of the 12th

Five-Year Plan, which contain a clearly stated policy of working toward improvement in the quality of economic growth, and in comments by Premier Wen Jiabao, who said during a press conference following the conclusion of the National People's Congress in March 2011 that China aimed to achieve growth 7% while also focusing on quality and efficiency.

The second reason for setting the growth rate target at 7.0% was to achieve consistency with the target for rate of increase in per capita disposable income. A sustained increase in per capita disposable income will be essential to the achievement of China's goal of moving to an economic development model that takes into account such factors as consumption-led growth and the improvement of living standards. For this reason, it was proposed while the 12th Five-Year Plan was still at the drafting stage that similar growth rates should be targeted for both personal incomes and economic development⁽⁸⁾. Since 2000, China's real GDP growth rate has generally been higher than the rate of increase in per capita real disposable income (Fig. 3). This situation appears to have influenced the central government, when it set these two targets. By setting the target for the average yearly rate of increase in real per capita

disposable income at over 7% and that for the real GDP growth rate at an average of 7% per annum, it seems to have sought to shift to a structure in which the achievable rate of increase in personal incomes would be at least marginally higher than the economic growth rate.

2. Measures to Reconcile the Development Model Shift with Continued Growth

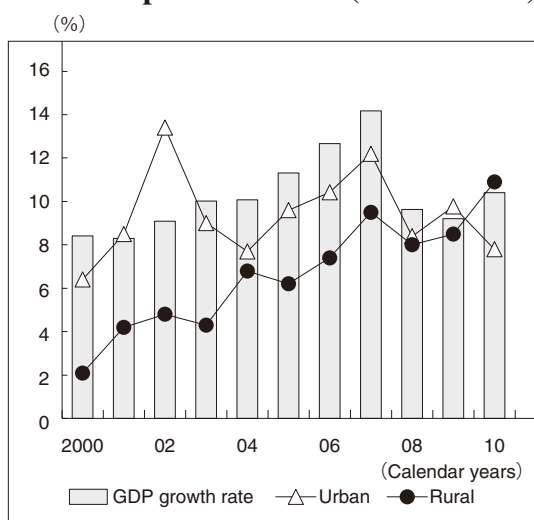
In Part 1 we described how the shift to a new economic development model had been positioned as the number one priority under the 12th Five-Year Plan. We also looked at other aspects, including the overall structure of the Plan, and the reasons why the growth target was set at 7%. However, there is a clear statement in Section 1/Chapter 2 of the 12th Five-Year Plan that the maintenance of development remains a "hard truth" (= supreme proposition)⁽⁹⁾. Will China be able to maintain its growth at the target level of 7% while changing its development model? In Part 2 we will examine the content and characteristics of four key policies—(1) the expansion of consumption, (2) the improvement of industrial competitiveness, (3) regional development centering on multiple urban areas, and (4) the promotion of two-way external economic relations—in relation to China's ability to reconcile the shift to a new development model with continued growth.

(1) Expansion of Consumption

We first need to consider the level of emphasis placed on consumption among other demand items.

In Section 1/Chapter 2 of the 12th Five-Year Plan, economic restructuring is described in relation to an accelerated shift in China's economic development model. Demand items are used as an example of this restructuring process. The plan then advocates economic growth driven by a balanced mixture of consumption, investment and exports. On the surface, all demand items seem to be given equal weight as growth drivers. As we

Fig. 3 Rate of Increase in Real Disposable Income (Year on Year)



Notes: The GDP growth rate for 2010 is based on the adjusted figure released in September 2011.
Source: National Bureau of Statistics, *China Statistical Abstract 2011*

read further into the Plan, however, it becomes clear that consumption is treated differently from the other items.

For example, the description of economic growth drivers is immediately preceded by a reference to the effective, long-term expansion of domestic demand. Yet there is no reference whatsoever to the external demand. When this is seen in conjunction with predictions of slower world economic growth and the emergence of protectionism in the analysis of the current situation and the forecast for the next five years in Section 1/Chapter 1, it suggests that China is aiming for growth led by domestic demand rather than a mixture of

domestic and external demand.

Looking at individual domestic demand items, we find references to investment in Section 1/Chapter 4, which puts forward a policy of maintaining reasonable growth while curbing duplicated construction and the expansion of facilities without adequate planning. In contrast, consumption is identified in the same chapter as the focus of domestic demand expansion, and there is no reference to measures to slow the pace of expansion. Although the language is indirect, this can be interpreted as an indication of the government's intention to move away from growth that relies heavily on investment and exports, and toward

Table 3 Composition and Key Points in Section 8

Areas Referred to in the Seven Chapters	Key References
①Public services	· After clarifying the scope of and standards for public services, the government will improve fiscal support systems and apportion management responsibilities (central-regional).
	· Competitive mechanisms will be introduced to the provision of basic public services, and restrictions on participation in non-basic services will be eased.
②Employment	· Employment for university graduates, transfer workers from the agricultural sector and urban residents with employment difficulties will be facilitated through tax and cost reductions or exemptions, training subsidies and other measures.
	· Other priorities will include the improvement of employment-related information services and statistics and incentives for business creation.
③ Income distribution	· Income distribution systems based on tax and social security will be strengthened.
	· During the plan period, minimum wage levels will be raised by an average of at least 13% per year, and mechanisms will be established to guarantee wage increases and payment (formulation of wage guidelines, encouragement of collective wage negotiation).
④Social security	· Full coverage under the new pension scheme will be provided in rural areas, and the pension portability system for workers who relocate within urban areas will be administered efficiently.
	· Minimum livelihood guarantees will be raised to appropriate levels through increases averaging 10% or more each year during the plan period in both urban and rural areas.
⑤Healthcare/public health systems	· The capacity to prevent serious infectious and endemic diseases and deal with outbreaks will be strengthened.
	· Priority will be given to the improvement of access to medical facilities and physicians and the reform of drug prices.
⑥Housing	· Construction of welfare housing will be accelerated.
	· Regional governments will be responsible for the stability of local housing prices and other factors.
	· Taxation and financial systems will be used to induce reasonable demand.
⑦Population problems	· Family planning (the one-child policy) will remain as a basic national policy.
	· Silver industries (care services) will be developed, and incentives will be provided for participation by private sector capital.

Source: 12th Five-Year Plan

consumption-led growth.

The 12th Five-Year Plan lists two approaches to the expansion of consumption: the accelerated growth of personal incomes, and the improvement of the consumption expectations of residents. The main initiatives to achieve these two goals are listed in Section 8 of the Plan, which deals with measures to raise living standards and improve social security systems (Table 3)⁽¹⁰⁾.

Specific measures to increase personal incomes include (1) the expansion of employment opportunities (including business creation), (2) the reduction of the tax burden for low- and middle-income people through changes to minimum thresholds and tax rates for personal income tax, and (3) increases in minimum wage levels and the creation of mechanisms to raise wages to appropriate levels and ensure payment, such as wage guidelines and the encouragement of collective wage negotiations. In particular, the government has set a numerical target of raising minimum wage levels by an average of at least 13% per year. There is clear evidence of the government's strong determination to use all available methods to raise incomes and increase consumption. The priority targets for measures to expand employment are university graduates, workers transferring from the agricultural sector, and urban workers who have been unable to find jobs. This emphasis appears to reflect the heightened risk of social unrest when people in these groups are forced to endure harsh living conditions in urban areas.

Measures designed to improve the consumption expectations of residents include (1) the provision of full coverage under the new pension scheme in rural areas, (2) the efficient administration of the pension portability system for workers who relocate within urban areas, and (3) appropriate increase in the minimum livelihood guarantee level. The government has set a numerical target calling for average increases of at least 10% per year for the minimum livelihood guarantee levels for urban and rural areas. The measures described in the plan can be seen as a clear reflection of the government determination to eliminate uncertainty about the future and lift consumer confidence through accelerated improvements to social secu-

rity systems.

(2) Strengthening Industrial Competitiveness

Section 2 (agriculture) through Section 4 (service industries) of the 12th Five-Year Plan contain policies and measures designed to strengthen the competitiveness of industries and businesses. To strengthen competitiveness, it is necessary to raise the level of science and technology and recruit quality human resources. Parts of Section 7, which deals with the development of research infrastructure and the training of people with specialized skills, are also relevant to the improvement of industrial competitiveness.

In terms of its contribution to GDP (40.2% in 2010) and growth (49.3% in 2010), manufacturing is obviously a core sector of the Chinese economy at present⁽¹¹⁾. In his aforementioned explanatory paper, Vice Premier Li Keqiang referred to the development of emerging industries as a way to adapt to global-scale competition. There will be keen interest in the choice of industries and the measures used to promote them. For this reason, we need to focus in particular on the content of the chapters dealing with manufacturing and emerging industries in Section 3 of the 12th Five-Year Plan (Table 4)⁽¹²⁾.

Section 3/Chapter 9 of the 12th Five-Year Plan, which summarizes measures to stimulate manufacturing industries, begins with the phrase "from big to strong." These words can be interpreted as a succinct expression of the government's intention to shift away from an industrial policy that was weighted toward quantitative expansion, in favor of a stance that emphasizes further improvements in technology levels and other areas.

This policy explicitly calls for measures to strengthen the product development capabilities of businesses and encourage brand development, and for the elimination of obsolete production capacity (facilities). Eight specific industries, including motor vehicles and iron and steel, have been selected under this policy, which also calls for accelerated corporate mergers and restructuring.

The final paragraph of Chapter 9 calls for the

Table 4 Content of Section 3 and Key References

Areas Referred to in the Six Chapters	Key References
① Manufacturing	<ul style="list-style-type: none"> Industrial restructuring, including the optimization of industry locations and the improvement of technology levels, will be facilitated (from big to strong). Corporate mergers and restructuring will be encouraged, and SME development will be accelerated.
② Strategic emerging industries	<ul style="list-style-type: none"> The seven industries selected as strategic emerging industries are energy conservation/environmental protection, next-generation information technology, biotechnology, high-end equipment manufacturing, new energy, new materials (raw materials) and new energy automobiles. The government will implement support measures to raise the contribution to GDP to around 8%.
③ Energy	<ul style="list-style-type: none"> A wide range of green energy technologies will be developed. Priority will be given to the storage of energy resources, the development of transportation routes for petroleum and natural gas, and the improvement of the power transmission grid.
④ Integrated traffic and transportation systems	<ul style="list-style-type: none"> Inter-regional and inter-city transportation networks will be improved and there will be prioritized development of public transport. The convenience of transportation services will be improved, and safety management will be strengthened.
⑤ Information technology	<ul style="list-style-type: none"> The development of next-generation information infrastructure and the use of information technology for economic and social purposes (including e-commerce and government services) will be accelerated. Network and information security will be strengthened.
⑥ Marine economy	<ul style="list-style-type: none"> The government will promote the rational development and utilization of marine resources and the development of related industries. Steps will be taken to ensure the safety of marine transportation routes and protect marine rights.

Source: 12th Five-Year Plan

accelerated development of small and medium enterprises as a way of strengthening the industrial base and expanding employment opportunities. Specific measures cited include tax incentives and the expansion of financing.

Another feature of Chapter 9 is its inclusion of detailed strategies for the advancement of individual industries, including the development of high-added-value ships, the development of basic materials for information technology by the non-ferrous metals industry, and the development of lightweight automotive materials. This level of detail is indicative of the government's commitment to the reinforcement of China's competitiveness in the manufacturing sector.

Section 3/Chapter 10 deals with the incubation and development of emerging industries. The seven strategic emerging industries selected in this chapter are energy conservation/environmental protection, next-generation information technology, biotechnology, high-end equipment manufacturing, new energy, new materials (raw materials)

and new energy automobiles. In the area of new materials, priority development targets have been set for some industries, such as semiconductors and high-performance rare earths. The government has also set a numerical target calling for a GDP contribution of around 8% from strategic emerging industries during the period covered by the 12th Five-Year Plan⁽¹³⁾. The government has announced various support measures with a view to achieving this target. These include the establishment of funds, increased government investment, and incentives for lending by financial institutions. Throughout this chapter, environmental protection and the conservation of energy and other resources are identified not only as solutions to growth-limiting factors, but also as new growth engines. This can be seen as an indication of the government's determination to link these industries to an accelerated transition to a new economic development model.

(3) Regional Development Centering on Multiple Urban Areas

Section 5 consists of three chapters dealing with such topics as regional development and land utilization categories (Table 5). Chapter 18 covers the implementation of regional development strategies, Chapter 19 the division of land into four major function zones as the basis for appropriate utilization within each category, and Chapter 20 guidelines and policies for the promotion of urbanization⁽¹⁴⁾.

The basic composition of Chapters 18 and 19 is the same as in the 11th Five-Year Plan, and they can be interpreted as meaning that the government has decided to continue the inland development strategy in western, central and northeastern regions, and the optimization of land utilization. In contrast with the previous Five-Year Plan, however, regional development in eastern (coastal regions) will be based on sub-regions rather than specific locations, such as special economic zones or the Pudong New Area in Shanghai. Jing-Jin-Ji (Beijing, Tianjin, Hebei), the Yangtze Delta and the Pearl River Delta have been identified as the three major eastern sub-regions and will play a leading role in various policies, including the shift to a new development model.

Policies concerning the promotion of urbanization are stated more clearly and in greater detail than previously. The aim is to achieve economic growth and market expansion through intensive

development efforts focusing on 21 city groups consisting of major cities and small and medium cities located on two horizontal (east-west) lines and three vertical (north-south) lines drawn across the whole of China⁽¹⁵⁾. During the process of forming these city groups, the cities will be divided into mega-cities, large-medium cities and medium-small cities. The government has adopted a stance of guiding migration from rural areas mainly into medium-small cities, while limiting the size of mega-cities. (Large-medium cities will be encouraged to accept external migration after their population management systems have been strengthened and improved.)

This stance was adopted for the following reasons. According to the official explanatory document for the 12th Five-Year Plan, a 1-point increase in the urban population causes a 1.2-point rise in personal consumption demand⁽¹⁶⁾. Based on this estimate, the government aims to expand consumption by encouraging migration to the cities. However, it also needs to avoid the social disruption and cost increase that would incur if population was allowed to gravitate into mega-cities. Careful weighing of these concerns appears to have led the government to adopt an urbanization promotion policy that combines both aggressive and cautious approaches.

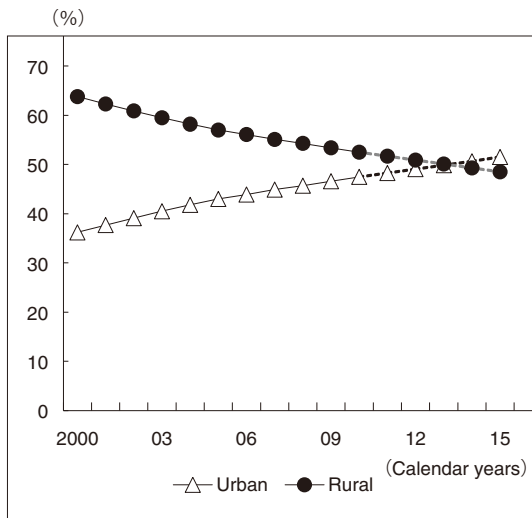
One of the key goals included in the 12th Five-Year Plan is that the “aggressive yet steady” promotion of urbanization should put the urban population on track to exceed the rural population as

Table 5 Content of Section 3 and Key References

Areas Referred to in the Three Chapters	Key References
①Regional development	· Development strategies will be implemented in inland regions (western, central, northeastern).
	· Support will be provided for development in eastern (coastal) regions, which will lead and support national economic development.
②Major function zone strategy	· Land utilization categories (including development restrictions) will be optimized.
	· Results of performance evaluations based on categories
③Urbanization	· Multiple urban centers consisting of major cities and small and medium cities will be formed in each region.
	· Rural residents will be steadily encouraged to relocate into urban areas, and conditions for migrant workers from rural areas will be improved.
	· The size of megacities will be limited, but the development of other cities will be encouraged.

Source: 12th Five-Year Plan

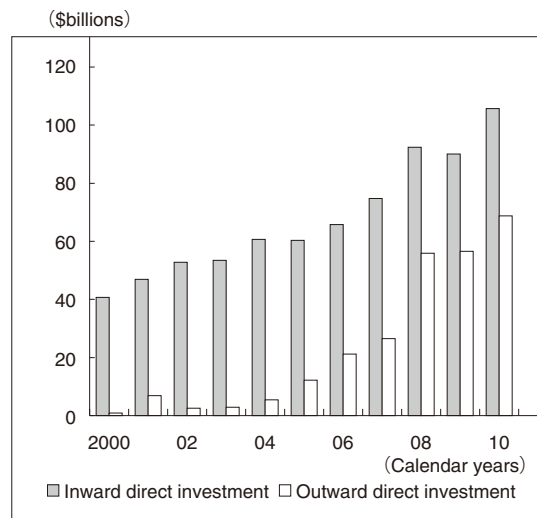
Fig. 4 A Rising Urbanization Ratio



Notes: The figures were calculated on the assumption that the urbanization ratio would rise (or fall) at a uniform pace during 2011-14 toward the target set down in the 12th Five-Year Plan.

Source: National Bureau of Statistics, 12th Five-Year Plan

Fig. 5 China's Inward and Outward Direct Investment



Notes: 1. Outward direct investment in 2000-2002 is based on data published by UNCTAD.

2. There are no published data for outward direct investment by the financial sector in 2003-2005.

Source: Ministry of Commerce et al., *Statistical Bulletin of China's Outward Foreign Direct Investment*, National Bureau of Statistics, *China Statistical Abstract 2011*, UNCTAD, *World Investment Report*

percentages of the total population before the end of the period covered by the plan (Fig. 4).

Overall, we can conclude that the central government regards the development of urban areas as an important element in its efforts to reconcile the shift to a new development model with the maintenance of growth.

(4) Promoting Two-Way External Economic Relations

Section 12 of the 12th Five-Year Plan sets out the government's basic stance on external economic policies. It begins with a statement that China intends to shift from a model based primarily on exports and the attraction of foreign capital to one that places an equal emphasis on exports, imports, the attraction of foreign capital and outward investment. In short, China's first priority in relation to external economic policies will be to adopt a two-way approach to trade and direct investment. This can be seen as a key policy adopted by the government with the aim of reconciling the shift to a new development model with the maintenance of growth⁽¹⁷⁾.

Specific policies relating to trade call for quantitative export growth through market develop-

ment, combined with an emphasis on qualitative improvement based in such areas as technology levels and service. The plan also states that imports are expected to play an important role in relation to the macroeconomic balance, structural adjustment and the optimization of the trade balance. These policies indicate that the government aims to expand imports as a way of stimulating domestic consumption and correcting trade balances or alleviating trade friction.

On the subject of inward direct investment, the plan emphasizes (1) the attraction of investment in such areas as advanced manufacturing, energy conservation and environmental protection, and (2) incentives for the establishment of a R&D centers by foreign companies. Both of these goals are linked to the policy of attracting foreign capital with the aim of strengthening the competitiveness of domestic industries.

The government's policy in relation to outward direct investment is to provide comprehensive support for overseas expansion by businesses, including the supply of information about the investment environment and the improvement of legal systems. Outward direct investment from

China has increased dramatically in recent years, and there is evidence that Chinese investment exceeded that from Japan in 2010 (Fig. 5). However, the 12th Five-Year Plan also states that China is aiming for the gradual development of its own major multinationals and financial institutions, which suggests that the government aims to limit its support to leading local companies with the potential to become multinationals.

3. Anticipated Challenges during the Implementation of the 12th Five-Year Plan

China is likely to be confronted by a number of challenges when it begins to change its economic development model under the policies set forth in the 12th Five-Year Plan. Given the aims of the plan, including a shift to consumption-led growth, the improvement of industrial competitiveness and the qualitative improvement of living standards while maintaining average annual growth of 7%, the following factors are likely to have a particularly decisive influence on the extent to which the targets set down in the plan are achieved.

(1) Challenges Concerning the Shift to New Development Model

First, when raising minimum wages and other items, the government will also need to take into account negative impacts on businesses and household budgets. For example, when subsidies and other mechanisms are used to stimulate consumption, there is a risk of reactionary downturn after the completion of the measures. Also significant is the increased fiscal burden. Sustained growth in consumption should ideally be achieved through income growth driven by wage rises.

Yet if excessive wage increases are forced onto the economy, national living standards could in fact be adversely affected by runaway inflation as the resulting cost increases are passed on through higher prices. If prices are not adjusted, business earnings would come under pressure. This situation would also cause consumption to decline be-

cause of income declines caused by redundancies and other factors.

In view of these possibilities, we need to look at the size of minimum wage level increases in the second half of 2011. In all of the 17 provinces, autonomous regions and municipalities in which adjustments were carried out; the increases were greater than the 13% target defined in the 12th Five-Year Plan (according to an article in the September 1, 2011 edition of JETRO, *Nikkan Tsusho Koho* [Trade Information Daily]). However, in some provinces, wages have been adjusted by around 30% year on year, and there is concern about the impact on businesses and household budgets in the regions concerned. Doubts remain about the sustainability of these increases.

The best way to reconcile the shift to an economic growth model based on the expansion of consumption with sustained growth is by raising wages at a steady pace while remaining properly aware on the negative consequences of wage increases. Policies need to be guided by a shared awareness of this fact by central and regional governments.

Second, it will be necessary to deal with the impact on the wealthy and state-owned enterprises, for which the implementation of this plan will not be entirely beneficial. While one of the goals defined in the 12th Five-Year Plan is to increase personal incomes, it also calls for measures that will be costly for the wealthy (high-income earners), including tighter tax adjustments and the introduction of asset taxes. Additionally, Section 11 of the plan calls for incentives for market entry by private sector businesses and the removal of barriers to their development. In recent years, one of the key arguments put forward in relation to economic restructuring in China is that the existence of state-owned enterprises, which enjoy advantages in terms of market entry and access to finance, is hindering the development of private sector business. This view is expressed in the Chinese phrase *guo jin, min tui* (advance of the state sector, retreat of the private sector)⁽¹⁸⁾. The state-owned enterprises that survived the restructuring that occurred between the second half of 1990s and the first half of the first decade of the 21st century enjoy oligol-

opolistic positions in such areas as energy and finance. Attention is also focusing on the vast sums paid to corporate managers. A number of policies in the plan, including measures to encourage participation by private sector businesses, appears to reflect the view that action is needed to remedy the *guo jin, min tui* phenomenon. The policy concerning remuneration for managers of state-owned enterprises, which calls for tighter controls and the reduction of payments to appropriate levels, can also be seen as part of measures to correct income disparity.

Instead of simply forcing these measures through, the government will need to make them more palatable by taking steps to mitigate the increased burden (income reduction) on the wealthy and state-owned enterprises. If strong resistance to these measures becomes an obstacle to the overall implementation of the plan, the government should consider delaying the implementation of measures that will increase costs or remove favorable conditions. However, efforts to strengthen the redistribution functions of the taxation and social security systems would be jeopardized if a minority of wealthy people are not required to accept any reasonable increase in their share of the burden. This would make the government's goal of achieving sustainable growth in consumption by correcting income disparities even more difficult to achieve and could lead to the uncontrolled expansion of government expenditure and the weakening of the revenue base. Excessive concessions to state-owned enterprises would have a negative effect on efforts to stimulate industrial activity through healthy competition among companies. While taking steps to mitigate opposition, the administration should remain faithful to basic principles throughout the period of the 12th Five-Year Plan.

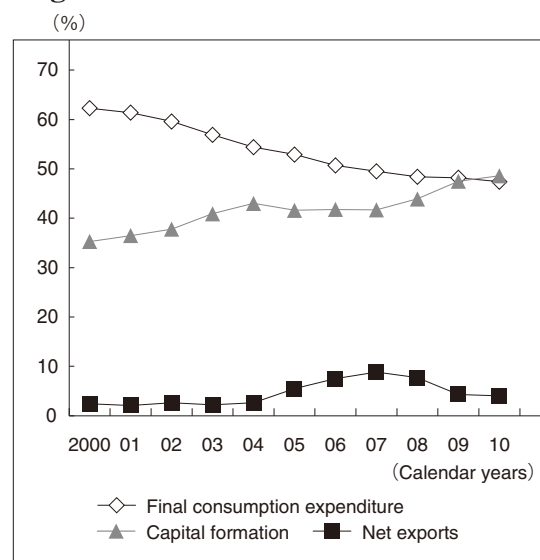
(2) The Influence of an Economic Cycle Based on Political Factors on the 12th Five-Year Plan

The biggest question will be whether the prevailing tendencies among China's leadership, including their commitment to high growth and eco-

nomical management based on investment expansion, can really be brought under control during the period covered by the plan. In reality, the Hu Jintao administration basically shelved the shift to a consumption-led growth model by giving priority to economic measures, including stimulatory measures and financial easing, amounting to 4 trillion yuan in response to the global financial crisis triggered by the Lehman shock. An analysis of GDP contributions from demand items shows that the contribution from capital investment formation has risen while that from consumption has tended to fall (Fig. 6)⁽¹⁹⁾.

If an economic cycle based on political factors emerges in the future, it could hinder China's efforts to achieve a soft landing in the form of a shift to cruising-speed growth (7%) under the 12th Five-Year Plan. Economic cycles based on political factors explain the economic fluctuations that occur in four-year cycles in the United States. These reflect the close links between presidential elections and expansionary fiscal and monetary policies. Similar analyses have been undertaken in relation to the Chinese economy. Typical of these is the analysis made by Kwan [2010], who identified the formation of an economic cycle based on factors that peak at that time of the National Congress of the Communist Party of China (Party Congress), including the use of expansionary eco-

Fig. 6 GDP Ratios for Demand Items



Source: National Bureau of Statistics, *China Statistical Abstract 2011*

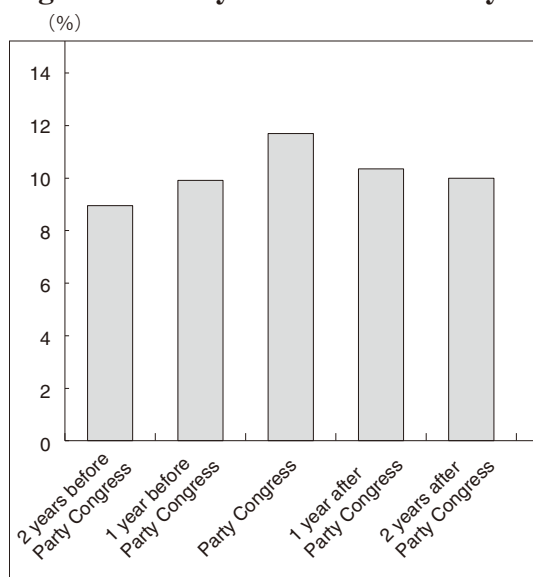
conomic policies to build support bases in the early stages of leadership changes, and the importance of the economic growth rate to assessments of the performance of senior officials⁽²⁰⁾.

Zhu [2011] also accurately describes a five-year economic cycle focusing on behavior patterns and performance assessments among senior local officials. He/She identifies a tendency to target high growth through the quantitative expansion of investment coinciding with periods during which there are major personnel changes at the central and local levels (before and after the National Congress of the Communist Party of China).

It is a fact that since 1990 average real GDP growth rates in years in which Party Congresses have been held have been higher than in years two years before, one year before, one year after or two years after Congresses (Fig. 7).

Given this kind of politically based economic cycle, it is possible that regional governments will be driven to invest more in late 2011 and during 2012, and that instead of falling, as predicted in 12th Five-Year Plan, the growth rate will actually rise⁽²¹⁾.

Fig. 7 Politically Based Economic Cycle



Notes: 1. Years between 1990 to 2011 were divided into five periods according to their relationship to years in which Party Congresses were held, and the simple average growth rates for each period were calculated.

2. The growth rate for 2011 is for January-September.

Source: National Bureau of Statistics

To prevent reckless behavior by regional governments, the Hu Jintao administration has tightened macro-control and called for the full implementation of central government directives. The policy direction in Section 1/Chapter 4 of the 12th Five-Year Plan specifically states that stronger macro-control should be used to reconcile sustained economic growth with qualitative improvement. Section 16 contains repeated calls for the proper fulfillment of professional responsibilities at all levels of government, for consistent compliance with the state's strategic intentions in the implementation of regional plans, and for the adjustment of regional plans to reflect the development strategies, key goals and priority tasks stipulated in the 12th Five-Year Plan. These statements can be interpreted as a reflection of the central government's determination to secure the cooperation of regional governments, which administer 91.9% of investment but are reluctant to implement measures to cool down the economy, for its efforts to achieve sustainable and harmonious economic development.

To gain that cooperation, the central government will need to use meetings, propaganda and other methods to deepen the understanding of senior regional officials about the need to raise the quality of economic growth. It will also need to develop mechanisms to monitor and assess progress toward key goals set down in the 12th Five-Year Plan.

Another priority, which is referred to in Section 16 of the 12th Five-Year Plan, will be the establishment of assessment and evaluation structures and specific evaluation methods that are conducive to an accelerated shift to a new economic development model. While the 12th Five-Year Plan reflects the government's awareness of the need to reduce the emphasis on the growth rate and focus on other goals, such as resource conservation and environmental protection, there is also a de facto admission that the personnel evaluation systems needed for this purpose have not been adequately developed. The government needs to ascertain the current situation accurately and then take urgent action to establish personnel assessment systems that will modify the behavior patterns of senior

officials by reflecting evaluation results in all personnel movements and punishments.

If the average GDP growth rate during the period covered by the 12th Five-Year Plan exceeds 10%, this should not be welcomed as a sign that targets have been exceeded. Instead it would be interpreted as meaning that the government had been unable to overcome the challenges described here, and that it had failed to bring the emphasis on high growth, and in particular the determination of regional governments to expand investment, under control sufficiently. Regardless of who succeeds the posts of General Secretary of the Communist Party, President or Premier, China will need to shift to a new economic development model and focus on the qualitative aspects of economic and social development. If China is to achieve sustainable economic development, it is vital that the Hu Jintao administration and the post-Hu leadership work to maintain stable growth by focusing not on the level of the growth rate, but rather on the improvement of living standards, the reinforcement of industrial competitiveness, and the sustained implementation of measures that contribute to resource conservation.

End Notes

1. See Miura [2010] Pp. 6-7 for an outline of the Scientific Development Concept.
2. Premier Wen Jiabao's analysis of the draft can be found on the Xinhua website (http://news.xinhuanet.com/politics/2010-10/28/c_12713246.htm).
3. Mr. Wen's comments at the press conference can be found on the Chinese government website (http://www.gov.cn/2011h/content_1824958.htm).
4. Vice Premier Li Keqiang's explanatory paper is available on the Xinhua website (http://news.xinhuanet.com/politics/2010-11/14/c_12773751.htm). The analysis of Mr. Li's paper in this article is based on previous research in Tanaka [2011].
5. The "middle-income trap" is a phenomenon that occurs when a developing country clings to traditional growth paths, such as natural resource utilization and policies designed to attract foreign investment, and neglects to work toward a change in its industrial structure, leading to a gradual slowing of its growth rate and failure to catch up with developed countries. See Oizumi [2011] for a discussion of the middle-income trap and the policies used by various countries to avoid it.
6. The key targets in the 11th Five-Year Plan were divided into four categories: economic growth, economic structure, population/resources/environment, and public services/national living standards.
7. The first question put to Premier Wen Jiabao at the press conference referred to in this article concerned the reasons for setting a growth target of 7%. This can be seen as evidence of a high level of interest in this aspect. In his response to this question, Mr. Wen indicated that he saw a shift to a new economic development model as the most important priority during the period covered by the 12th Five-Year Plan and in the longer-term perspective.
8. The draft of the 12th Five-Year Plan can be found on the Xinhua website (http://news.xinhuanet.com/politics/2010-10/27/c_12708501.htm). In writing this article, the author referred to the Japanese version of the Plan in the November 2010 edition of China News Service, *Gekkan Chugoku Josei* (China Situation Monthly).
9. First uttered by Deng Xiaoping during his southern tour in 1992, the phrase "Development is the only hard truth" has been used repeatedly as a slogan ever since. It has tended to be interpreted as a justification for the acceleration of growth.
10. For example, there are references in Section 2 to measures to encourage rural residents to undertake migrant work or move into non-agricultural occupations.
11. Industry figures have been used in this article because of data limitations. The data do not appear to contradict the view, as stated in this article, that manufacturing is a core industry in China.
12. The key goal of increasing the GDP contribution from tertiary industries appears to reflect the government's aim of moving away from a growth model that is overly dependent on secondary industries, and expectations that tertiary industries will generate employment.
13. An article in the November 2, 2010 edition of JETRO, *Nikkan Tsusho Koho* [Trade Information Daily] quotes a government think-tank expert as saying that strategic emerging industries currently account for about 5% of GDP. "Currently" here is thought to mean 2009 or 2010.
14. There are four types of major function zones: land space optimization development zones, priority development zones, restricted development zones, and prohibited development zones. These classifications take into account future population distribution, economic positioning, land use and urbanization structures, based on resource and environmental load capacity, development density and latent development potential. This land use concept was first introduced under the 11th Five-Year Plan.
15. South central Tibet is the only one of the 21 urban groups that is not located on any of the lines.

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16. Jiang [2010], P.123
 17. Increased opening and the promotion of multilateral economic cooperation are also included in the 12th Five-Year Plan and as key external economic policies.
 18. See Tsugami [2011] pp.77-102 for a discussion of the *guo jin, min tui* phenomenon and its harmful effects.
 19. Capital formation exceeded 40% of GDP during the high-growth eras in Japan and South Korea, but this situation did not persist for years. In this sense, the weighting of China's economic structure toward investment appears to be unsustainable.
 20. This article has emphasized the strong influence of political factors in China's economic cycle. However, it is also necessary to be aware that there were times when the five-year cycle did not emerge, because of fluctuations in external demand or differences in the intensity of tightening measures.
 21. Zhu [2011] P.180

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5. Tanaka, O. [2011], *2011-2015-Nen no Chugoku Keizai* [The Chinese Economy 2011-2015], Sososha.
6. Chinese government website [2011], *Zhonghua Renmin Gongheguo Guomin Jingji he Shehui Fazhan Dishierge Wunian Guihua Gangyao* [Outline of the 12th Five-Year Economic and Social Development Plan of the People's Republic of China] (http://www.gov.cn/201111/content_1825838.htm, downloaded September 16, 2011, referred to in this article as the "12th Five-Year Economic and Development Plan of the People's Republic of China").
7. Tsugami, T., [2011], *Kiro ni Tatsu Chugoku* [China at the Crossroads], Nihon Keizai Shinbun Shuppansha.
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10. Li, K. [2010], *Shenke Lijie Jianyi Zhuti Zhuxian Cujin Jingli Shehui Quanmian Xiediao Kechixu Fazhan* [Deep Understanding of Proposals Concerning Key Themes and Directions for the Acceleration of Comprehensive, Harmonious and Sustainable Economic and Social Development] (downloaded from http://news.xinhuanet.com/politics/2010-11/14/c_12773751.htm on September 20, 2011).