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LRP/bi provides its clients with high-impact business intelligence. Our firm also advises clients in the creation of sustainable competitive advantage and the maximization of growth, profitability, and shareholder value.

Based in the United States in southern California, LRP/bi provides its suite of high-impact business intelligence services to public companies, pre-public companies, investment portfolio and fund managers, and investment bankers worldwide.

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Research Brief

China:

SIC Projects GDP Growth of 10.5% in 2006, 9.5% in 2007 Slow Shift Towards Consumer-Driven Economy Continues

October 16, 2006

The Economic Forecasting Department (EFD) in China's State Information Center (SIC) stated last week that China's GDP is expected to grow by 10.5% in 2006 and 9.5% in 2007. China's GDP expanded by 10.2% in 2005. The SIC EFD's Director, Fan Jianping, indicated that this double-digit GDP growth in 2006 is expected to be accompanied by consumer-level price inflation of only 1.3%.

In general, in our view, China is continuing to make important progress towards an economy that is driven more by growth in consumer demand, and less by expansion in fixed asset investment and exports. Here are the details.

- Growth in China's *nominal fixed asset spending*, says, Fan, is expected to decrease from an estimated 26.5% in 2006 to an estimated 20.0% in 2007.
- Chinese *exports*, according to Fan, are expected to increase 24.5% in 2006, a drop of 3.9 percentage points from the 28.4% growth rate registered in 2005. Export growth is expected to slow further to the 15.0% level in 2007. This anticipated decline in export growth in 2007, LRP/bi expects, will be driven, in part, by a projected decline in US economic growth.

China's *imports* are expected to grow by 21.5% in 2006, an increase of 3.9 percentage points from the 17.6% growth rate of 2005. Fan and his EFD analysts are forecasting 2007 growth in Chinese imports of an estimated 14.0%. In the view of LRP/bi, continued strength in Chinese consumer spending could result in faster import growth in 2007 than is currently expected by most economists.

The SIC EFD forecasts a 2006 *trade surplus* for China of US\$146.8 billion. LRP/bi notes, though, that slower-than-expected growth in Chinese exports in 2007, combined with faster-than-expected growth in imports could generate a downside surprise in the size of China's 2007 trade surplus.

- The EFD is projecting *retail sales* growth of 12.5% for China in 2007. Retail sales grew by 12.9% in 2005, and have expanded at a 13.0%-plus rate during 2006-to-date. In the view of LRP/bi, the most likely direction of surprise in Chinese retail sales in 2007 is to the upside. The elimination of taxes on farmers, an increase in minimum salaries, and increased welfare spending are likely to be key factors in strong retail sales growth, particularly, in our opinion, in China's rural regions where incomes have lagged significantly behind those in urban coastal areas.

Importantly, Chinese consumer spending appears to be advancing at a faster rate

than consumer incomes, indicating that China's lofty savings rate is declining. Such a decline, if sustained, could further dampen over-heated lending activity and accelerate China's shift towards a consumer-driven economy.

As always, clients of LRP/bi should contact us for additional details.

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