Perfecting China, Inc.
The 13th Five-Year Plan

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A REPORT OF THE
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Abbreviations

5YP     Five-Year Plan
CCP     Chinese Communist Party
CFDA    China Food & Drug Administration
CSRC    China Securities Regulatory Commission
FDA     Food & Drug Administration
IC      Integrated circuit
ICOR    Incremental capital output ratio
ICT     Information and communications technology
IP      Intellectual property
LSGCDR  Leading Small Group on Comprehensively Deepening Reform
LSGEF   Leading Small Group on Economics and Finance
MEP     Ministry of Environmental Protection
MNC     Multinational Corporation
MOF     Ministry of Finance
MOFCOM  Ministry of Commerce
MOST    Ministry of Science and Technology
NDRC    National Development and Reform Commission
NPC     National People’s Congress
OECD    Organization of Economic Cooperation and Development
PBOC    People’s Bank of China
PRC     People’s Republic of China
SEI     Strategic Emerging Industries
SOE     State-owned enterprise
STPCR   Science and technology progress contribution rate
TFP     Total factor productivity
TPP     Trans-Pacific Partnership
TTIP    Transatlantic Trade and Investment Partnership
VOC     Volatile organic compound
WTO     World Trade Organization
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This report was only possible because of all of these contributions. But while we received help from many quarters, the ultimate responsibility for the final report, including any remaining mistakes, are our own.
Executive Summary

Despite the explosive growth of the private sector in China’s economy over the last several decades and a concomitant diminution of the role of planning in managing the increasingly diverse economic landscape, the Chinese Communist Party’s (CCP) five-year plans (5YPs) remain the most authoritative strategic vision on the direction of the country’s economic and social policies. This report analyzes the recently released 13th Five-Year Plan to provide a window into the evolving dynamics of China’s policy process, the trajectory of Chinese economic policies, and the implications of the plan for the business community, with a particular emphasis on the information and communications technology (ICT) and health care sectors.

The drafting of the plan mirrors broader trends in China’s policy process. This very lengthy process drew on input from every ministry and level of government and the CCP, and involved a genuinely extensive review of China’s progress and challenges and possible policy options to address these issues. But the decisionmaking process was also highly centralized, and the ultimate choices on the plan’s main themes, structure, targets, and policies reflect the preferences of the country’s top leadership, particularly President and CCP General Secretary Xi Jinping.

There is a consensus in China that the old growth model, which stresses extensive investment, is out of date, and that the top priority is to rebalance the economy and make it more efficient. As a result, the plan puts a heavy emphasis on streamlining manufacturing, promoting innovation, and encouraging the development of more advanced technologies. It also emphasizes greater environmental protection, a stronger social safety net, and expanding China’s place on the global economic stage through greater investment and more active participation in global economic governance.

While these are all laudable goals, the plan does not rebalance the relationship between state and market. There is recognition of the need to strengthen a variety of market institutions, but the plan is less clear and ambitious on the specific policy steps needed to rebalance China’s governance model away from the state and toward the market. In addition, mobilizing capital for priority sectors and other interventionist tools are still central to the plan. As a result, this is a strategy to improve the current system—to strengthen China, Inc.—not to transform it.
If the plan's economic targets are met, it would represent significant progress toward avoiding the "middle-income trap." However, it is possible that many of the goals in the plan can be achieved without making the economy much more efficient. If market mechanisms are not used more consistently, and barriers to market entry for private and foreign companies not further reduced, the economic outcome for China over the medium term will likely be "growth with volatility." China may become an inefficient technology power with a highly leveraged financial system and vulnerable to wide swings in its business cycle.

Given China’s likely approach to the 13th Five-Year Plan, multinationals that feed into China’s growth machine and do not challenge prioritized Chinese incumbents have huge opportunities to do well in China. Others that compete against national champions or seek access to areas the government is not yet ready to open because of domestic weaknesses will continue to face major challenges. Because of potential structural weaknesses in the economy, everyone could be vulnerable to China’s economic volatility.
Introduction

China’s five-year plans are grand strategic visions that tell a story, a story about the country’s past and its hopes for the future. At well over 100 pages and written in curt official prose, they are not emotionally moving, but they are meant to mobilize the country’s officials with the hope that they will jointly work toward the plan’s goals. The plans are the most politically authoritative statements on the country’s core economic and social policies; therefore everyone operating inside the political system and who has important interactions with China needs to understand the visions they present.

Not everyone agrees. Writing on the eve of the issuance of the 13th Five-Year Plan’s summary proposal last fall, one longtime observer of China declared: “If you are not a Chinese government official . . . then the plan is irrelevant.”¹ She actually was charitable compared to other recent commentaries. One lobbyist for a multinational corporation (MNC) in Beijing observed that officials he speaks with have said ruefully that “plans are drawn up, then hung on the wall and ignored.” A cartoon that made its rounds on WeChat mocked the plan, substituting the Chinese word for plan, guihua (规划), with a homonym that means “lie” (鬼话).²

Of course, one should not overstate the plan’s significance. It does not serve the original purpose of guiding a centrally directed economy as in earlier years. In addition, China’s economic circumstances could change between drafting and implementation, forcing policymakers to shift course. In addition, 5YPs have no budget, nor does the Ministry of Finance (MOF), which manages China’s fiscal purse, draw up budgets to meet the precise needs of the plan.

Nevertheless, plans still matter because they are drafted through a “whole-of-government” approach that involves everyone, and the final text acts as a large blinking neon arrow pointing in the

2. This turn of phrase was used several years ago by Professor Xu Xiaonian following the release of the 12th Five-Year Plan. See “Xu Xiaonian: All Plans are All Lies” (许小年 : 所有的规划全都是鬼话), Wangyi Caijing, May 26, 2011, http://money.163.com/11/0526/16/750BJ4R500254ML2.html.
direction of the CCP’s core priorities. Central and local officials are then drawn to align their work in the same direction, which in turn attracts companies, financial institutions, and others in society to follow suit. Some adapt in name only, but many genuinely try to orient their activities in ways consistent with the plan. The government and CCP reward such alignment behavior with funding, market access, and symbolic support.

Not all plans are equally important. Plans crafted early in a leader’s tenure likely matter more than plans drawn up later in their tenure. The 9th 5YP (1996–2000) was Jiang Zemin's first chance to solidify the concept of the "socialist market economy” that had been put forward in the Third Plenum of the 14th Party Congress in 1993. Hu Jintao and Wen Jiabao used the 11th 5YP (2006–2010) to shift attention to the need for greater investment in infrastructure. The 12th 5YP was meant to carry forward the goals of the 11th 5YP and newly emphasized consumer spending and developing advanced homegrown technologies. Yet because the global financial crisis led to a more severe slowdown than anticipated, traditional infrastructure spending was still a major component of actual policy. When Xi Jinping (习近平) assumed leadership of the CCP at the 18th CCP Congress in November 2012, he inherited the 12th 5YP. The 13th 5YP is his chance to solidify a new course that he has begun to set with other policy documents and speeches.

Although five-year plans seem antiquated and can be difficult to decipher, it is worth the effort to try. The drafting process offers a unique window into the political system that is less visible by examining specific policies because five-year plans involve everyone, from top to bottom, from Beijing to Kashgar. Five-year plans also synthesize current policies, letting us know their relative importance, and identify potential new policy directions. Finally, they are a useful yardstick for measuring how effectively China is addressing its economic and social challenges. Given the growing size of China’s economy, it is not an exaggeration to say that as the economy of the People’s Republic goes, so goes the world’s.

Plans do not emerge in a vacuum but out of a specific economic context and complex political process. Understanding this environment is central to making sense of the 13th 5YP and what it means for everyone. Hence, our first task in the pages that follow is to describe the economic challenges that the plan is meant to address. We then turn to explaining the lengthy process by which the plan was drafted. This is all a preview to presenting the plan’s contents, including the quantitative targets, broader goals, and the policies meant to fulfill its vision. We then examine how the plan varyingly speaks to the information and communications technology (ICT) and health care sectors, two industries that are both central to China’s future economic success and yet have very different dynamics. We also briefly analyze and compare the plans issued by each of China’s provinces. Finally, we conclude the report by considering the implications of the 13th 5YP for China, for companies that do business with China, and for the global economy.
The Why: The Economic Context

CHINA’S ECONOMIC CHALLENGE

Anyone even vaguely familiar with current events knows that China has grown by leaps and bounds over the past four decades. It is the world’s second-largest economy and largest exporter. Less than 10 percent of China’s economic output now comes from agriculture, and a majority of Chinese are now urbanites. A visit to China, and not to just its showcase coastal cities, confirms these impressions. City skylines have been transformed, as have the lives of average Chinese. Hundreds of millions of people have been lifted out of poverty, and somewhere between 100 and 300 million are counted among China’s consumer class. China is one of only 14 countries since World War II to succeed in raising its per capita income relative to the United States by 10 percent or more.

Yet China’s amazingly successful development story is also built on a fragile foundation. As much as the country has grown, the economy is also extremely inefficient, a problem that has worsened in recent years. The broadest measure of efficient growth is total factor productivity (TFP), which distinguishes between growth achieved through improvements in human capital and technology versus simply the addition of more labor and capital. Some refer to this as the difference between growth from inspiration versus perspiration. China has registered high growth figures since the 1970s; however, the share of growth coming from TFP has been gradually eroding (see Figure 2.1). As farfetched as it may seem, if current trends continue, the contribution of TFP will resemble China’s growth profile during the late Cultural Revolution (see Figure 2.2).

Chinese workers have become much more efficient over the years as a result of expanded educational opportunities and better training. Labor productivity grew an average of 8.9 percent.

**Figure 2.1. Sources of China’s Growth, 4th–12th Five-Year Plans (%)**

Source: Asian Productivity Organization.

**Figure 2.2. Contributions to China’s Growth, 4th–12th Five-Year Plans (%)**

Source: Asian Productivity Organization.
annually between 1995 and 2010. By contrast, China’s use of capital, the largest component of the country’s growth, has deteriorated. A precise and simple way to measure the efficiency of capital is the incremental capital output ratio (ICOR), which reflects how much capital is spent to generate a unit of real gross domestic product (GDP) growth (see Figure 2.3). In 2008, it took around two yuan to generate one unit of GDP growth; by 2015, China needed almost nine yuan of capital to get one unit of growth. More broadly, China’s ICOR rate has fallen (improved) in three periods during the Reform era: in the early 1980s following land reform; in the early 1990s following Deng Xiaoping’s famous Southern Tour; and in the late 1990s and early 2000s following extensive reforms to state-owned enterprises (SOEs), including the closure of thousands of them, and China’s entry into the World Trade Organization (WTO).

As a result of declining efficiency in investment, China has had to invest ever greater sums of money to generate economic growth. Total aggregate financing has jumped from 121 percent of GDP in 2005 to 204 percent of GDP in 2015. The result is that total outstanding debt has grown rapidly, by Bloomberg’s estimate, from 166 percent of GDP in 2007 to 246 percent of GDP in 2015. Most is held by companies (165 percent), the rest by banks (19 percent), the government (22 percent), and households (40 percent). Officially, only a tiny proportion of bank loans have

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gone bad, and very few corporate bonds have ever defaulted, but this picture is likely affected by a substantial portion of loans and bonds being rolled over and the continuing growth of new credit, which dilutes the share of worrisome debt. A sign that bad debt may increase is that the stock of account receivables and the number of days companies wait to be paid have both been rising quickly.\(^7\) Inefficient investment reveals itself in many other ways, including overcapacity in a wide number of sectors, rising energy demand, inconsistent product quality, growing carbon emissions, and pollution.\(^8\)

We do not believe that a financial crisis is likely in the short term or inevitable in the long run, but there is no doubt that steps must be taken to make the economy more efficient.

**THE NEED FOR INNOVATION**

Becoming more efficient can be achieved through many routes, but there is broad consensus, in and outside of China, that a central part of the solution is to make China’s economy more innovative. Since the 1990s, China has become dominant in assembly and manufacturing, but much of this activity is low value-added and does not yield the returns available to those who either are involved at the beginning of the production process (in creating technologies) or at the end of the process (in selling products under one’s own brand). The great majority of Chinese companies occupy what Stan Shih, founder of Acer, calls the bottom of the “smile curve.”\(^9\)

China has certainly made substantial efforts toward changing this situation, as the Chinese government and industry have made innovation a mantra and put substantial energies toward developing more advanced technologies. There has been an explosion of applications for patents and copyrights in China, and China is now the world’s third-largest filer of international patents, with telecom firms Huawei and ZTE ranked first and third, respectively.\(^10\) There is now an assortment of well-known Chinese companies, including Alibaba, Baidu, Tencent, and others, who have come forward with innovative technologies, services, and business models, and have shaken up the landscape in China and elsewhere. Some of these companies are entirely homegrown, whereas others have been created by Chinese who have worked or studied overseas.\(^11\)

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8. For an in-depth analysis of the overcapacity problem, see Overcapacity in China: An Impediment to the Party’s Reform Agenda (European Union Chamber of Commerce in China, 2016).
Scholarly research shows that although there is more innovation in China, it is concentrated in a small number of regions, particularly in a few coastal cities. In addition, Chinese companies have become more adept at innovating in how they produce goods and how they adapt products to customer tastes, as opposed to achieving major technological breakthroughs that have broad commercial application.12 Although China is now expending 2.1 percent of GDP on research and development (R&D), such spending supports a relatively small number of entities. One technology expert we interviewed reports that their national large-scale survey reveals that only 5 percent of Chinese companies do any kind of R&D.

Equally important, even though some in China are investing in developing new technologies, a broader shift toward a more creative society has yet to occur. A recent global survey ranked China 62nd in terms of creativity, just behind Botswana and ahead of Malaysia. The study put China 14th in terms of technology, but only 87th in talent and 96th in tolerance, the other two components of the overall creativity index.13 These data mirror debates about why Chinese perform so well on standardized tests but have won so few Nobel Prizes, and why someone like Apple founder Steve Jobs is unlikely to emerge in China.14

THE DOUBLE REBALANCE

To address these economic challenges, it appears that China needs to rebalance itself in two ways. First, China needs to rebalance its economy away from unproductive and wasteful investments toward more efficient and productive uses, where there is greater likelihood of commercial success. This means focusing more on improving the efficiency of manufacturing processes, expansion of high value-added services, more efficient use of energy, greater protection of the environment, more effective utilization of labor and land, and strengthening the social safety net. To move forcefully in this direction, China also needs to rebalance the relationship between state and market. China’s economic governance approach utilizes industrial policy to mobilize capital and other regulatory levers to create investment in anticipation of demand and to promote the competitive chances of Chinese sectors and companies, particularly SOEs.15 In most sectors the

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Chinese government still has a large say in who participates in these markets (and who does not), where those markets are located, what products and services are available, how prices are calculated, who receives support to buy or sell these goods, how sales are transacted, how proceeds from the sales are distributed, and what happens to participants whose products do not sell well. As the regime’s priorities evolve, industrial policy is subject to frequent change over time and across the country, and information about policy can often be difficult to obtain, both during the policy drafting process and even during implementation.

China’s approach has always been controversial, but there are numerous precedents amongst its neighbors and even among Western countries of extensive government intervention facilitating development. However, intervention to shape competitive outcomes is of declining utility the closer a country approaches the technology frontier and the more its financial system becomes complex and integrated into the rest of the world. Under such conditions, the chances of government failure, as opposed to market failure, rise substantially. Hence, China needs both deregulation, in terms of reducing government intervention and liberalizing markets, and reregulation, in terms of creating and strengthening institutions to make markets more efficient and able to generate the kind of economic rebalance the country needs.

It is no mystery that rebalancing the economy and governing institutions of China is needed, but it is easier said than done. There was a great deal of optimism that Xi Jinping’s ascendance to top leader would usher in such progress. In late 2011, China’s Development Research Center and the World Bank jointly issued a report describing the reforms necessary in order for the country to avoid falling into the “middle-income trap.” Although the creation of the report was done with the approval of then president Hu Jintao, it appears that incoming premier Li Keqiang (李克强) and economist Liu He (刘鹤), who would serve as a key advisor to President Xi, supported the report as well. Moreover, a year into Xi’s term, at the Third Plenum of the 18th Party Congress, the leadership issued its famous “Decision,” which clearly stated that “handling the relationship between government and market well” was the central task of reform and that markets “should have a decisive role in resource allocation.” To emphasize the importance of reform, Xi Jinping set up a new Leading Small Group on Comprehensively Deepening Reform (LSGCDR), installed himself as chair, and created a list of over 300 tasks related to streamlining government and reforming the economy. Xi Jinping also popularized the concept of the “new normal” (新常态), which means that China has accepted slower growth as permanent and is instead focusing on improving the efficiency and quality of the economy. The notion of “supply-side reforms” (供给侧改革), first

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highlighted in November 2015, likewise emphasizes the need to reduce overcapacity in sectors related to infrastructure and real estate and expand the supply of high-tech goods and services. These broader ideas have been accompanied by a steady stream of new policies in finance, the fiscal system, family planning, international trade and investment, agriculture, transportation, the environment, advanced technology, and many other areas.

The range of new policies issued under Xi Jinping and Li Keqiang has been breathtaking, but there has been a stark difference between a clear priority to rebalance the economy away from traditional industries and toward new sectors, consumption, and services on the one hand, and the much more ambiguous, incremental, and halting approach toward rebalancing the role of state and market on the other hand. Industrial policy has not receded, nor have the practices of official discretion and policy opacity. In fact, one can safely argue that these practices have strengthened and expanded under Xi Jinping’s guidance.19

The clearest embodiment of this tendency to revert toward state control mechanisms can be seen in the recent handling of stock market volatility, the unpegging of the renminbi to the U.S. dollar, and the unveiling of SOE reforms. Preventing a stock market collapse, keeping the renminbi from depreciating significantly, and ensuring SOEs do not fail and their assets are protected were each justifications for the government to intervene as opposed to what was perceived as the riskier path of letting markets determine the preferred outcomes.

On the eve of the emergence of the 13th Five-Year Plan, observers’ judgments on China’s economic condition largely turned on which type of rebalance was more valued. Optimists tended to focus on the growing share of output from services and a measured fall in overall growth that has avoided a harder landing.20 Those who were more pessimistic instead focused on the continued use of industrial policy, barriers to market entry, and economic volatility. The U.S.-China Business Council’s “Reform Scorecard” still registered a lowly “limited” in early 2016.21 Those most worried believed that the delaying of market liberalization is the source of rising debt that makes a financial crisis much more likely.22


THE OPPORTUNITY OF THE 13TH FIVE-YEAR PLAN

Five-year plans are not typically an opportunity for the country’s economic policy to take a dramatic and unexpected turn, as the drafters are overseen by leaders who determined the policies leading up to the plan’s adoption. Nevertheless, those who believe China needs a more thorough-going double rebalance could only hope for the development of more progressive policies. A Chinese economist with whom we spoke mused that at past crucial junctures China’s political leaders advocated bold progressive ideological platforms. These included the suggestion to “seek truth from facts” in the late 1970s as a justification for allowing private farming and small-scale private business; the admonition in the early 1990s to no longer worry about whether a specific policy was socialist or capitalist, which resulted in the restarting of liberal economic reforms; and the decision made in the late 1990s to join the WTO. Aware that innovation would be the defining theme of the 13th Five-Year Plan, this economist hoped that China’s current leaders would show similar foresight in pursuing institutional reforms that would facilitate a more holistic approach to innovation, as opposed to focusing on acquiring and developing technology hardware. The starting point for determining whether his hopes might be realized begins with the drafting of the plan, the subject we turn to next.
The How: The Drafting Process

INTRODUCTION

Tucked just off Lunar Alter South Street (月坛南街) on the western side of Beijing sits an imposing institution, the National Development and Reform Commission (NDRC). Its name, internal organization, and specific tasks have changed over the years, but it still is situated at the center of China’s economic policymaking system. Its officials oversee the twists and turns of Chinese industrial policy, and they also help guide the crafting of China’s five-year plans. Their job is to develop and take measure of China’s progress toward long-term goals for the country. Although plans are issued episodically, their work is never-ending.

Five-year plans are a reflection of China’s broader economic and political environment. The economic relevance of plans changes over time. In the past, they were the cornerstone of a centrally planned economy. Now they set the direction for management of a highly regulated market economy, a system alternatively called “market Leninism,” “state capitalism,” or, in official terminology, “a socialist market economy.” Similarly, the shift in the gravity of decisionmaking authority from the government to the CCP is also reflected in how the 13th 5YP was drafted. The CCP has always been in charge, but under Xi Jinping, the CCP has asserted itself and become more involved in the day-to-day work of governance. Xi Jinping oversees every major policy decision. 1

Although he originally devoted little attention to economic affairs, the proportion of his time spent

on economic issues has risen substantially. The NDRC, the State Council, and Premier Li Keqiang were intimately involved in the process, but this is President Xi Jinping’s plan.

PLANS: A BRIEF HISTORY

The history of economic planning in China can be divided into three relatively distinct periods.²

The first plan, which ran from 1953 to 1957, was modeled on the Soviet planning process, with detailed input-output tables linking resources and raw materials to final products. The actual process was somewhat more decentralized than in the Soviet Union, but still was a close facsimile. The plan was interrupted by the twists and turns of the Great Leap Forward and the Cultural Revolution, but still guided economic activity for most of the Mao era. The fifth 5YP, adopted just as Mao was passing from the scene, was the last to support a planned economy.

The second phase, which ran from the 6th to 10th plans (1980–2005), was the era of indicative planning. The plans set targets that acted as broad goals that officials strived to reach in any way they could. They were still focused on straightforward economic production and were written by officials for officials. The third and current phase of planning started with the 11th 5YP, issued in 2006. Similar to the second, there were still broad quantitative targets, but as one expert who has participated in the drafting process for several plans said, the document has become more a “vision document” than the detailed blueprint or action plan of earlier years.³ This shift in approach was reflected in the change of the Chinese name from jihua (计划) to guihua (规划), which is still translated into English as “plan,” but implies a less detailed, more macro plan. In addition, beginning with the 11th 5YP, plans began to distinguish between “predictive” (预期性) and “mandatory” (约束性) targets, with the latter in principle more important for officials to meet. Finally, the plan’s scope has expanded beyond traditional economic issues to incorporate the environment, culture, economic diplomacy, governance, and even the relationship between the military and civilian economies.

The difference between the second and third phases has been substantial but not absolute. Further changes in the future could move the plan in the direction of being more like a party platform than an economic planning document. Such changes might involve shrinking the length of the plan, removing the economic growth target, having no mandatory targets, having a broad balance between economic and noneconomic issues, expanding access to the drafting process for those outside the government and CCP, and explicitly linking the plan to national and local budgets.


3. A planning official told us that the 5YP is now best considered as “a strategy.”
Of course, the ultimate change would be to eliminate 5YPs altogether, but that seems unlikely given how central the process is to how the entire system reviews and sets major goals. Maintaining the plan also is consistent with the decidedly more Marxist policy lens President Xi has brought to his stewardship of the CCP. One insider told us, for example, that there has been no discussion inside the leadership about getting rid of plans for precisely these reasons. Another longtime participant in the process jokingly warned that China definitely wants there to be a 14th 5YP in part because the Soviet Union collapsed in the middle of its 13th 5YP.

**HOW A PLAN BECOMES A PLAN**

The path to a plan is long (over two-and-a-half years) and involves the mobilization of the entire political system, including central and local officials, thousands of experts, SOEs, industry associations, the media and propaganda system, and others. It is this extended “whole-of-government” approach that gives plans their political weight and authority.

The process begins with a midterm review of the progress toward fulfilling the goals of the current plan. This is largely a quantitative exercise, but also involves measuring how effectively the policies associated with meeting these targets have been pursued. On that basis, there then ensues extensive research on the whole range of topics related to the plan. The NDRC, other central government ministries, and local governments commission projects from experts in and out of government. In addition, research institutes and universities also take their own initiative to put forward research when they feel strongly about a certain issue.

The results are then shared with the NDRC and the CCP’s Leading Small Group on Economics and Finance (LSGEF), and the party’s leadership then decides the forthcoming plan’s “basic idea” (基本思路), essentially the plan’s key themes and initiatives. It is on that basis that the party, through the LSGEF, drafts the plan’s “proposal” (建议), which is issued in the party’s Fifth Plenum, typically held in the fall. At the same time, the NDRC is responsible for managing the drafting of the full plan. The drafting groups for the proposal and full plan have overlapping membership, but are separately managed. The earliest drafts of the full plan are actually completed before the proposal is issued, and then the full plan is further revised in light of the proposal and additional meetings and debate. The penultimate draft of the full plan is then put before the annual gathering of China’s legislature, the National People’s Congress (NPC), held in March of the following year. The NPC’s deputies debate and suggest changes, which are then incorporated into the final version of the plan, which the deputies approve on the last day of their session. The leadership then releases the plan to the public several days after the conclusion of the NPC session.

When we say “the plan,” we are referring to the national plan, which is called, somewhat confusingly, “The Outline of the xth Five-Year Plan for National Economic and Social Development of the People’s Republic of China.” But there are actually several hundred five-year plans, which Oliver

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4. There is really no parallel in the American political system or other democracies. The closest may be political party platforms, but those are drafted by a committee, and typically candidates are not bound by what is drafted, either during the campaign or if they are elected.
Figure 3.1. Drafting Process for the 13th Five-Year Plan

Melton appropriately explains are issued as a "cascade of plans." Each province, county, and city has its own plan. The provincial proposals and full plans are drafted in reference to the national proposal and plan, but provincial plans are written, approved, and released before the national plan. There are also dozens of "specialty plans" (专项规划) that address a wide variety of specific functional issues, everything from technology development to the environment to food safety. These plans are primarily drafted and released in the weeks and months after the full national plan is issued in order to ensure consistency and to elaborate on certain elements of the full plan. Finally, large SOEs and industry associations also craft their own five-year plans, which are loosely based on the national and provincial plans.

PREPARATORY WORK ON THE 13TH 5YP: EXTENSIVE CONSULTATION

The drafting of the 13th 5YP was in some ways a very open and consensual process, with input from many quarters, particularly in the beginning phases. The review of the 12th 5YP started in mid-2013 and took the rest of the year. It involved a pedestrian check of the status of the quantitative targets and related policies. In 2014, attention turned toward conducting more in-depth research on various aspects of China’s economic and social circumstances. The NDRC commissioned reports in May 2014, but other government agencies sought out additional reports as well. Xu Lin, the director-general of the NDRC’s Planning Division, the government office directly responsible for managing the drafting process, reported that there were 80 commissioned research projects. The vast majority went to domestic research groups in and outside the government, but some went to domestic companies, such as Alibaba, Fosun, and the Hang Seng Bank.


Three foreign organizations—the Organization of Economic Cooperation and Development (OECD), the Asian Development Bank, and McKinsey Global Institute—were also hired to carry out projects. Beyond these studies, there were hundreds of unsolicited studies drafted and sent to government and party authorities on an even broader array of issues. Finally, the NDRC also turned to social media and in mid-2014 set up a WeChat feed to receive suggestions from the public.8

The other key mechanism for outside input was a formal committee of experts established to offer ideas and review drafts during the entire process. The 55-member group was headed by former NDRC deputy director Wang Chunlin, and its deputy chair was former World Bank chief economist Justin Lin Yifu. Most members are leading experts on the plan’s core topics, including macroeconomics, science and technology, finance, the environment, regional development, the fiscal system, international trade and investment, and social welfare.9 The group also included the chairmen of the board of four major Chinese companies: Ning Gaoning of COFCO (a large agricultural firm), Tian Guoli of the Bank of China, Dong Mingzhu of the Gree Group, and Wang Chuanfu of BYD.10 This was an intellectually diverse group; there were advocates for thoroughgoing economic liberalization and others who historically have stressed the value and necessity of extensive government intervention. At the same time, it was composed of only three women. As with the initial research projects, foreign input was also sought further along in the process. For example, in December 2015, Premier Li Keqiang hosted a discussion on innovation and the plan, which included former World Bank chief economist and Columbia University professor Joseph Stiglitz and the World Bank’s country director for China, Bert Hoffman.11

Consistent with this image of a big tent, experts who participated in the process reported in interviews that there was genuine extensive debate on a wide range of issues, and that experts were called on to play a larger role than in past, with some helping with the actual drafting. One source emphasized that, consistent with the norm of “democratic centralism,” prior to the passage of the proposal in late October 2015, “no clear line was set,” and so any views could be shared. There were, for example, a full range of opinions about the economic growth target, not just at what level it should be, but whether there should be a target in the first place. Similar discussions occurred on finance, SOEs, innovation, and many other topics.

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9. The 11th SYP’s expert group had only 37 members. There were 13 people who participated in both groups. The full list of experts for the 11th SYP is here: http://www.ndrc.gov.cn/fzgggz/fzgh/zhdt/200510/t20051026_47170.html; and the full list of experts for the 13th SYP is here: http://ghs.ndrc.gov.cn/135tz/135fzghwyh/. We did not find a list of experts for the 12th SYP.
DRAFTING THE PLAN: THE PARTY’S ROLE RISES

As work turned from research to drafting, particularly following the adoption of the proposal, the scope of those involved narrowed and the broader political dynamics of the current leadership, with the CCP and Xi Jinping playing a more direct role than in the past, became more visible.

The appointment and location of personnel are central to this story. The key to Xi’s increased role was the LSGEF and its general office director, Liu He. During the Hu Jintao era, Liu was an expert at the Development Research Center, the State Council’s official think tank, but when Xi came to power, he was made both a deputy director of the NDRC and the head of the LSGEF’s main office. He is likely President Xi’s closest economic advisor. The NDRC is officially under the purview of the State Council and should take direction from Premier Li Keqiang. In earlier times, if the LSGEF wanted to give instructions or share an opinion with the NDRC, it would be normal for it to do so via the State Council. However, with Liu He’s dual hat and the greater interest in the plan by Xi Jinping, there essentially was a “dotted line” from the LSGEF directly to the NDRC. Similarly, according to an interview source, Premier Li Keqiang’s primary confidant during the process was Ning Jizhe (宁吉喆), who is also a deputy director of the NDRC as well as director of the National Bureau of Statistics. Ning reportedly spent time in his youth with Li Keqiang in rural Anhui. He was brought onto the State Council Research Office when Li became premier, and he accompanies the premier to most important meetings and trips. As a consequence of such ties, it appears that NDRC director Xu Shaoshi (徐绍史) has had his authority undercut.

It is possible that observers with whom we spoke are inflating the significance of personal ties and that the CCP and government clearly divided their responsibilities and collaborated as they had previously, but there are several signs that personal dynamics did play some difference in the outcome. The seemingly greater influence of specific individuals—rather than institutions—in the most recent planning process is also broadly consistent with the unmistakable trend under President Xi toward more personalized politics and decisionmaking.

As usual, the CCP leadership set the plan’s basic line, but it appears this step was completed later than usual. For the 12th FYP, the basic line was established in March 2010; the basic line of the 13th should have been done in March 2015, but may not have been fully completed until the summer. It is unclear why, but one possibility is that Xi Jinping did not turn his attention to economic affairs and the plan until 2015 because he previously was fully preoccupied by the anticorruption campaign and other issues. In 2015 Xi reportedly chaired 13 meetings on the plan within nine months.

12. For his biography, see http://www.chinavitae.com/biography/Liu_He%7C1291.


As usual, the proposal was drafted primarily by the LSGEF and then discussed and passed during the Fifth Plenum of the 18th Party Congress in late October 2015. This was the first time that the plan’s overall goal was made available. This goal was having China fulfill its aim of achieving a moderately prosperous society by 2020 and doing so by pursuing development in five ways: innovation, regional integration, green development, international openness, and shared social benefits. An equally interesting element of the proposal’s unveiling is that Xi Jinping himself did the honors of explaining its contents to the plenum participants, a task which previously had always been performed by the premier.

The drafting of the full plan was an odyssey. The initial draft was carried out in the summer of 2015 in a hotel near the Fragrant Hills in far western Beijing and involved upward of 200 pens. Over time, the number of drafters shrunk, perhaps to as few as 10 people, and work shifted to inside the Zhongnanhai leadership compound, where the CCP and State Council are both headquartered. There were over 20 drafts from beginning to end. Once an initial draft was complete, there were two more important turning points in the process. The first came after the proposal was issued in late October. Up to that point drafts reportedly did not include the five development themes, and the plan’s structure mirrored those of recent plans, organized by a long list of individual topics. But, given the proposal’s themes, the plan was apparently given an overhaul, with a reorganization according to the themes. According to one source, this required a lot of “cutting and pasting” to move contents around into their new proper locations.

The second turning point was the addition of a key policy focus, “supply-side reforms.” Even though there was discussion of the need to restructure the economy toward higher value-added sectors, the original proposal lacked any discussion of supply-side reforms. In late 2015 China’s economy was showing significant signs of strain, and the problem of addressing overcapacity seemed more urgent than ever. The idea of supply-side reforms, which appears to have been developed by Liu He, was first put forward as a coherent idea in early November 2015. Its profile was raised substantially at the CCP’s Central Economic Work Conference held the following month. Over the next two months, the concept was inserted into the plan. At least eight drafts of the plan were completed after the start of China’s Spring Festival in February 2016, and one of the key changes made during that month was the addition of what became Chapter Five, which is dedicated to supply-side reforms.


18. Chinese experts understand that their use of the term differs from its use by President Ronald Reagan, for whom supply-side economics was about cutting taxes to free up capital for investment and consumption. The Chinese version is about reducing excess capacity in basic infrastructure-related sectors and expanding capacity in higher valued-added technologies. See Zeng Zheng, “The Starting Logic Point of Policy in ‘13-5’ Period China,” in Comprehending 13-5 (读懂十三五), ed. Wu Jinglian, Li Yining, and Lin Yifu (Beijing: China CITIC Press, February 2016), 251–270.
Once the annual NPC session opened in early March 2016, the main task for the leadership was to explain the plan’s contents and receive feedback, hopefully positive, from the assembled deputies. Deputies put forward a range of changes, and over 50 were accepted into the final draft. Three of these changes were related to public health, with clauses on the need to improve the quality of milk, ensuring “health care security,” and reforming both the payment system and management of the social health insurance system (yibao, 医保). The most important change to the document during these two weeks was the tempering of plans to create a third stock market board for companies from strategic emerging industries (SEIs), an idea meant to help innovative companies without a long track record raise funds they likely could not obtain from China’s more conservative banks. This sudden reverse course was initiated by Liu Shiyu (刘士余), who Xi Jinping chose to replace Xiao Gang (肖钢) as head of the China Securities Regulatory Commission (CSRC), the scapegoat for the past year’s market volatility. Liu apparently was worried that the new board might threaten the stock market’s fragile stability and so had the initiative pulled.19

Although this move was unpopular because it was another step away from marketization, the NPC really did not have much say on specific elements of the plan. When it came time for them to vote, 93.9 percent of the deputies gave their assent. Only a day after the close of the annual session, on March 17, 2016, the State Council released the final plan to the public.

Although the plan’s general themes were announced in the proposal, and more details were revealed in Li Keqiang’s Government Work Report given at the start of the session, the only way to know whether the plan sufficiently pursued the rebalancing of the economy and the relationship between state and market would be to go through the text word for word.

The What: The Plan’s Targets and Policies

INTRODUCTION

To say that the 13th 5YP was introduced with little fanfare would be a major understatement. Whereas the proposal and Government Work Report were heralded in the Chinese official and unofficial media, the final plan and all of its details were quietly issued on a Thursday night (March 17, 2016), and almost no one took notice. One reason may be that many of the details had been aired twice before, and there appeared to be little that was new. But in addition, one journalist told us that because of the recent economic volatility, the media might have believed that, in the short-term, the lofty goals of the plan took a backseat to the more urgent issues of addressing overcapacity and keeping up growth.

This is certainly a legitimate concern, but despite the urge to focus on just the here and now, there is value in analyzing the plan in its entirety because it reveals much more than the proposal or snippets of the plan. One element lost in any summary is the plan’s organizational structure (see Table 4.1). Chinese official documents never leave the best for last; instead, the most important priorities are placed first, and the more an issue is discussed or a word is used, the more important it is. As usual, the plan’s opening section provides a brief analysis of the country’s economic circumstances, lays out its main goals, and then provides the specific quantitative targets, the most commonly recognized part of any plan. The main body of the 13th 5YP, though, differs from past documents in that it is primarily organized around the five themes or “concepts” (理念) first described in the proposal. These macro sections are not explicitly identified, but you can infer them from the section and chapter titles and their contents. Discussing innovation first and for so long (38 pages) makes clear that this is the most important component of the plan. By contrast, the section on international openness is further back in the plan and quite brief, sending the opposite signal.

Of course, the content of the plan matters more than organization. We now break down the plan by examining, in order, its quantitative targets, its broader goals for the economy, and the policies
proposed to achieve them.\(^1\) We rely heavily on the text but also situate the document within the context of current policies and ongoing debates about potential forthcoming policies. Our bottom line conclusion is the plan does seek a fundamental rebalancing of the Chinese economy but does not pursue with equal vigor a concomitant rebalancing of the relationship between state and market.

There is a consensus in China that the old growth model based on extensive investment is out of date and that the top priority is to rebalance the economy and make it more efficient. This is exactly how the plan in its opening pages frames the economy’s core dilemma, with the now familiar reference to adapting to the “new normal.” As a result, the plan puts a heavy emphasis on streamlining manufacturing, promoting innovation, and encouraging the development of more advanced technologies. It also emphasizes greater environmental protection, a stronger social safety net, and expanding China’s place on the global economic stage through greater investment and more active participation in global economic governance.\(^2\)

\(^1\) “The Outline of the 13th Five-Year Plan for National Economic and Social Development of the People’s Republic of China” (中华人民共和国国民经济和社会发展第十三五年规划纲要), March 17, 2016, http://www.sdp.gov.cn/fzgggz/lfzgh/gwhb/gj201603/P020160318564052484034.pdf. Hereafter, “Outline of 13th 5YP.” We were unable to locate an English translation of the full plan.

\(^2\) Ning Jizhe colorfully put the plan’s goals as: “We want every percentage point of GDP to have more sci-tech content, employment content, ecology content, standards content, and brands content.” Ning Jizhe, “Comprehending ‘13-5’,” in This Book Writing Group, *Comprehending 13-5* (读懂十三五) (Beijing: China People’s Press, March 2016), 14.
While these are all laudable goals, the plan’s approach to governance reform is less decisive. There is recognition of the need to strengthen a variety of market institutions, but the plan is less clear and ambitious on the specific policy steps needed to forcefully move in this direction. In addition, mobilizing capital for priority sectors and other interventionist tools are still central to the plan. As a result, this is a strategy to improve the current system—to strengthen China, Inc.—not to transform it.

Hence, one’s confidence in the plan turns on one’s confidence in state intervention. Those who have faith in the CCP’s ability to direct resources and strategically utilize regulation in favor of priority sectors and issues, and to pursue governance reform in an incremental and gradual way, will welcome this plan. Those more skeptical of such an approach, who believe in a more rapid and full-sweeping change of the state’s posture toward regulation, will find the plan more problematic.

THE TARGETS: CHANGE IS IN THE AIR

Even after the start of the Reform era, when China shifted to indicative planning, 5YPs focused heavily on standard economic growth issues. According to one expert, fully 60 percent of the sixth 5YP’s targets were related to promoting rapid development. As Table 4.2 shows, the plan’s targets have evolved dramatically, with a drop in the number of targets related to growth and a consistent increase in those related to the environment and resources. Relatedly, the overall number of targets has increased; some entirely new targets have been added, but just as often a single target has been separated into more detailed components.

Multiple sources stated that drafters made it a point to include only achievable targets. Even if a target is not officially mandatory, not reaching it reflects poorly on the relevant officials, including those at the top, as it suggests the government made a mistake. Since more than 35 percent of the targets in the 10th 5YP were not fulfilled, planners and implementing officials have made fulfilling the plan’s targets a higher priority.

Looking at the 13th 5YP, the composition and value of its targets reflect a desire to continue the transformation of China’s economy away from heavy industry and investment and toward services, high technology, a healthier environment, and a stronger social safety net. If the goals are met, 60 percent of Chinese will live in urban areas by 2020, and well more than half of the economy’s growth (56 percent) will come from services. In addition, the trend within industry toward more advanced technologies will continue. If R&D expenditures reach 2.5 percent of GDP, this would put China squarely among OECD nations, and, given the China’s size, the absolute value of China’s R&D spending would surpass almost every other country. China hopes that such spending will result in almost a doubling of the per capita rate at which technologies are invented and patented (from 6.3 to 12.0 patents per 10,000 people), which should translate into greater commercialization of homegrown products. New to this plan are ambitious targets for Internet penetration. To some
extent these goals reflect a desire to bridge the Internet divide for individuals, but equally important is how connecting individuals and companies to the Internet could raise productivity and expand business opportunities for Chinese companies. One official explained to us how the Internet, for example, had made small, private manufacturers in Shenzhen able to pursue contracts for custom manufacturing with clients around the world.

The targets for social welfare also point to continued progress along a number of paths. Several stand out. China hopes to move over 55 million people out of poverty by 2020. The current figure for those in poverty stands somewhere between 70 and 85 million people.4 Considering China’s inability to modernize in the late Qing dynasty (in contrast to Japan’s more successful Meiji Restoration), hyperinflation and destitution during the late Republican era, and massive suffering during the Great Leap Forward and the rest of the Mao era, it is hard to overstate how historically significant this achievement would be, especially since one in every 12 people on the planet lives in the Chinese countryside. At the same time, China plans to create an additional 50 million jobs in urban areas, expand educational opportunities, and raise access to pensions for retirees.

Perhaps the most impressive quantitative targets are those related to the environment and resources. Not only do they account for almost half of all targets, but every single one is mandatory, meaning we can be sure that extensive bureaucratic resources will be invested to ensure they are achieved. It was only in the 11th 5YP that China began to seriously address the environment, adding targets for reducing energy consumption, total discharge of major pollutants (such as sulfur dioxide, SO2), water used in industry, and cultivated land. That plan also called for increasing forest coverage, efficient use of irrigation, and better treatment of industrial waste. What was a sea change is now a tidal wave. The targets are higher, more detailed, and cover a wider range of


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<td>The Economy</td>
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<td>5</td>
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<td>Sci-Tech</td>
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<td>2</td>
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<td>5</td>
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<tr>
<td>Environment</td>
<td>3</td>
<td>8</td>
<td>12</td>
<td>16</td>
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<td>Social Welfare</td>
<td>8</td>
<td>8</td>
<td>9</td>
<td>7</td>
</tr>
<tr>
<td>Total</td>
<td>22</td>
<td>23</td>
<td>28</td>
<td>33</td>
</tr>
<tr>
<td>Total Fulfilled</td>
<td>14</td>
<td>20</td>
<td>28</td>
<td>—</td>
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issues. The number of major pollutants to be tackled has been raised, and, for the first time, the target for proportion of waterways classified as suitable for drinking and fishing (grades I–III) has been raised to 70 percent, while the amount of water only suitable for agriculture and landscaping (grade V and V+) is targeted to be kept under 5 percent. But the most ambitious new target is the goal to substantially improve air quality, measured by the now infamous statistic, PM 2.5. Reducing PM 2.5 nationally will mean limiting SO$_2$, carbon, ammonia, and volatile organic compounds (VOCs), which are emitted from gasoline, solvents, and industrial processes. As mentioned previously, drafters will not set targets that are unlikely to be met, and so they could be even more ambitious; but this represents a substantial expansion and strengthening of environmental protection goals.

Although the great majority of targets reflect genuine progress, how the plan handles the headline target of economic growth is somewhat disappointing. There was debate early in the planning process about whether to put aside this target in light of China’s entry into the “new normal,” in which the quality of growth should matter more than the absolute amount. However, it was felt that removing this target would have been too radical a step, and that local governments, if left without a national target constraint, would come up with wildly varying targets, making the national economy harder to manage. The main disagreement centered around what the target would be. Experts close to Xi Jinping reportedly pushed for 7.0 percent, while Li Keqiang’s experts favored 6.5 percent, mainly because it would be easier to reach. The final decision, “greater than 6.5 percent,” was a compromise put forward by the NDRC; it bridges the differences and, if met, would result in China doubling the size of its GDP from 2010 to 2020, a politically important goal the CCP leadership has advocated for several years.

The key to whether or not reaching this target will cause an unsustainable bubble turns on how efficiently China can grow. One source said that the NDRC has determined that 6.5 percent growth is eminently sustainable if total factor productivity can be raised from a quarter to one-third of the source of growth. For the first time, raising labor productivity was included in the plan, with a goal of 6.6 percent annual improvement. But since the main source of TFP in China’s case must come from improvements in the use of capital, adding labor productivity is not a huge win for advocates of efficiency, who argued that TFP itself should be included.

Proponents of using TFP were opposed by officials at the Ministry of Science and Technology (MOST) who were concerned that not only would calculating TFP be hard mathematically, but they would have a difficult time ensuring that the target would be met. And because there is comparative data for TFP, the official TFP statistic would be vulnerable to nitpicking by outsiders. MOST successfully persuaded the CCP leadership to adopt instead an alternative statistic as a proxy for TFP, the “science and technology progress contribution rate” (STPCR) (科技进步贡献率), which is included within the “Innovation” category of targets. STPCR is meant to capture the


Table 4.3. 12th Five-Year Plan Targets

<table>
<thead>
<tr>
<th></th>
<th>Target By 2015</th>
<th>Growth* (%)</th>
<th>Actual Performance By 2015</th>
<th>Growth* (%)</th>
</tr>
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<tbody>
<tr>
<td><strong>The Economy</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GDP (trillion yuan and %)</td>
<td>–</td>
<td>7</td>
<td>67.7</td>
<td>7.8</td>
</tr>
<tr>
<td>Services/GDP (%)</td>
<td>47</td>
<td>[4]</td>
<td>50.5</td>
<td>–</td>
</tr>
<tr>
<td>Urbanization (%)</td>
<td>51.5</td>
<td>[4]</td>
<td>56.1</td>
<td>–</td>
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<td><strong>Science and Technology</strong></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>R&amp;D spending/GDP (%)</td>
<td>2.2</td>
<td>[0.45]</td>
<td>2.1</td>
<td>–</td>
</tr>
<tr>
<td>Enrollment in high school (%)</td>
<td>87</td>
<td>[4.5]</td>
<td>87</td>
<td>[4.5]</td>
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<tr>
<td>Nine-year compulsory education rate (%)</td>
<td>93</td>
<td>[3.3]</td>
<td>93</td>
<td>[3.3]</td>
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<tr>
<td>Invention patents/10,000 people</td>
<td>3.3</td>
<td>[1.6]</td>
<td>6.3</td>
<td>–</td>
</tr>
<tr>
<td><strong>Social Welfare</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Population (billion)</td>
<td>&lt;1.39</td>
<td>&lt;0.72%</td>
<td>1.375</td>
<td>–</td>
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<tr>
<td>Per capita disposable income of urban residents (yuan)</td>
<td>&gt;26,810</td>
<td>&gt;7%</td>
<td>–</td>
<td>7.7%</td>
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<tr>
<td>Per capita net income of rural residents (yuan)</td>
<td>&gt;8,310</td>
<td>&gt;7%</td>
<td>–</td>
<td>9.6%</td>
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<td>New urban jobs (million)</td>
<td>–</td>
<td>[45]</td>
<td>–</td>
<td>[64.3]</td>
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<tr>
<td>Registered urban unemployment rate (%)</td>
<td>&lt;5</td>
<td>–</td>
<td>4.05</td>
<td>–</td>
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<tr>
<td>Coverage of urban basic old-age pension (million)</td>
<td>357</td>
<td>[1]</td>
<td>377</td>
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<tr>
<td>Increase in average life expectancy (years)</td>
<td>74.5</td>
<td>[1]</td>
<td>76.34</td>
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<td><strong>Environment and Resources</strong></td>
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<tr>
<td>Reduction of major pollutants (%)</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>[12.9]</td>
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<tr>
<td>Chemical oxygen demand</td>
<td>–</td>
<td>[8]</td>
<td>–</td>
<td>[18.0]</td>
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<tr>
<td>Forest growth</td>
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<td>Forest coverage (%)</td>
<td>21.66</td>
<td>[1.3]</td>
<td>21.66</td>
<td>[1.3]</td>
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<td>Forest coverage (billion sq. meters)</td>
<td>14.3</td>
<td>[6]</td>
<td>15.1</td>
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<tr>
<td>Reduction of energy consumption/GDP (%)</td>
<td>–</td>
<td>[16]</td>
<td>–</td>
<td>[18.2]</td>
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<td>Effective use of irrigation water (utilization coefficient)</td>
<td>0.53</td>
<td>[0.03]</td>
<td>0.532</td>
<td>–</td>
</tr>
<tr>
<td>Total acreage of cultivated land (billion square meters)</td>
<td>1,212</td>
<td>[0]</td>
<td>1,243</td>
<td>–</td>
</tr>
<tr>
<td>Nonfossil fuel/primary energy consumption (%)</td>
<td>11.4</td>
<td>[3.1]</td>
<td>12</td>
<td>–</td>
</tr>
</tbody>
</table>

* Brackets [ ] indicate numbers are cumulative over the five-year period.
### Table 4.4. 13th Five-Year Plan Targets

<table>
<thead>
<tr>
<th>Target By 2020</th>
<th>Growth*</th>
<th>Predictive or Mandatory</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The Economy</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GDP (trillion yuan and %)</td>
<td>&gt;92.7</td>
<td>&gt;6.5%</td>
</tr>
<tr>
<td>Services/GDP (%)</td>
<td>56</td>
<td>[5.5]</td>
</tr>
<tr>
<td><strong>Urbanization (%)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Resident population</td>
<td>60</td>
<td>[3.9]</td>
</tr>
<tr>
<td>Registered population</td>
<td>45</td>
<td>[5.1]</td>
</tr>
<tr>
<td><strong>Labor productivity (yuan/person)</strong></td>
<td>&gt;120,000</td>
<td>&gt;6.6%</td>
</tr>
<tr>
<td><strong>Innovation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>R&amp;D spending/GDP (%)</td>
<td>2.5</td>
<td>[0.4]</td>
</tr>
<tr>
<td>Sci-tech progress contribution rate (%)</td>
<td>60</td>
<td>[4.7]</td>
</tr>
<tr>
<td>Internet penetration (%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fixed broadband (households)</td>
<td>70</td>
<td>[30]</td>
</tr>
<tr>
<td>Mobile broadband (households)</td>
<td>85</td>
<td>[28]</td>
</tr>
<tr>
<td>Invention patents/10,000 people</td>
<td>12</td>
<td>[5.7]</td>
</tr>
<tr>
<td><strong>Social Welfare</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Per capita disposable income (%)</td>
<td>-</td>
<td>&gt;6.5</td>
</tr>
<tr>
<td>Development of affordable housing in units (million)</td>
<td>-</td>
<td>[20]</td>
</tr>
<tr>
<td>New urban jobs (million)</td>
<td>-</td>
<td>[&gt;50]</td>
</tr>
<tr>
<td>Poverty alleviation in rural areas (million people)</td>
<td>-</td>
<td>[55.75]</td>
</tr>
<tr>
<td>Coverage of urban basic old-age pension (%)</td>
<td>90</td>
<td>[8]</td>
</tr>
<tr>
<td>Average years schooling for working-age population (years)</td>
<td>10.8</td>
<td>[0.57]</td>
</tr>
<tr>
<td>Increase in average life expectancy (years)</td>
<td>-</td>
<td>[1]</td>
</tr>
<tr>
<td><strong>Environment and Resources</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reduction of major pollutants (%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chemical oxygen demand</td>
<td>-</td>
<td>[10]</td>
</tr>
<tr>
<td>Ammonia nitrate</td>
<td>-</td>
<td>[10]</td>
</tr>
<tr>
<td>Sulfur dioxide</td>
<td>-</td>
<td>[15]</td>
</tr>
<tr>
<td>Forest growth</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Forest coverage (%)</td>
<td>23.04</td>
<td>[1.38]</td>
</tr>
<tr>
<td>Forest coverage (billion sq. meters)</td>
<td>16.5</td>
<td>[14]</td>
</tr>
<tr>
<td>Recently developed land (billion square meters)</td>
<td>-</td>
<td>[&lt;21.7]</td>
</tr>
<tr>
<td>Reduction of energy consumption/GDP (%)</td>
<td>-</td>
<td>[15]</td>
</tr>
<tr>
<td>Reduction of water consumption/10,000 yuan GDP (%)</td>
<td>-</td>
<td>[23]</td>
</tr>
<tr>
<td>Reduction of CO₂ emissions/GDP (%)</td>
<td>-</td>
<td>[18]</td>
</tr>
<tr>
<td>Cultivated land (billion square meters)</td>
<td>1.243</td>
<td>[0]</td>
</tr>
<tr>
<td>Nonfossil fuel/primary energy consumption (%)</td>
<td>15</td>
<td>[3]</td>
</tr>
<tr>
<td>Air quality (%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Days of good-moderate air quality in cities at &amp; above prefecture level</td>
<td>76.7</td>
<td>&gt;80</td>
</tr>
<tr>
<td>Decrease in PM2.5 concentration in cities at &amp; above prefecture level</td>
<td>-</td>
<td>[18]</td>
</tr>
<tr>
<td>Surface water quality (%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equal or better than Grade III water</td>
<td>&gt;70</td>
<td>-</td>
</tr>
<tr>
<td>Grade V water</td>
<td>&lt;5</td>
<td>-</td>
</tr>
</tbody>
</table>

* Brackets [ ] indicate numbers are cumulative over the five-year period.
relative contribution of science and technology to economic growth, but it appears to be prone to exaggeration. It could, for example, include the construction of buildings that house cloud-computing facilities. This figure has continued to rise, even though TFP’s contribution to growth has continued to decline. Critically, China is the only country that calculates this statistic, and so, for better or worse, there is no comparative data against which to benchmark China.

If increasing efficiency were such a critical goal, and using TFP would be too controversial, drafters could have chosen other alternative measures, such as the ICOR data cited earlier in this report, as well as the return on assets, corporate profitability, and limits on the growth of government or corporate debt. The modest steps toward creating productivity targets pales in comparison to the other goals and hints at larger challenges with the plan’s design.

PROMOTING INNOVATION: A DICHOTOMOUS APPROACH

When one looks at the 13th 5YP’s detailed discussion of its major themes and related policies, one continues to see mixed messages. On economic substance, the plan proposes ambitious steps forward at a relatively rapid rate on each of the five major themes. The plan envisions China becoming an innovation power, pushing forth the boundaries of the technological frontier and moving up the value-added chain in a wide range of sectors. It foresees transforming China regionally by expanding national and intraregional transportation and communication linkages, reforming the household registration system, creating several macro regions (including Beijing-Tianjin-Hebei and along the Yangtze River), and making cities more service-oriented for all of their residents, including migrants. It envisions creating a more ecologically sustainable economy by making more effective use of agricultural land; expanding the conservation of energy, water, and other resources; strengthening disincentives to pollute; upgrading environmental restoration efforts; contributing to the global effort against climate change; and promoting green-technology sectors. The plan envisions a China that makes its domestic markets more accessible to foreign goods, services, and investment, and also expands opportunities for Chinese industry to itself export and invest abroad, in no small part through the “Belt and Road” initiative, an ambitious plan to connect China by land and sea to the rest of Asia, Europe, and Africa. And the plan seeks to raise the standard of living for Chinese society by taking steps to radically reduce poverty, modernize the education system and make access easier for low-income populations, improve public health through the “Healthy China” campaign and other efforts, expand the availability of public housing, reduce the gap between rich and poor, expand coverage of public health insurance and pensions, and better protect the rights of women, children, and the disabled.

7. For an explanation of multiple technology innovation indicators maintained by the Chinese government, see National Bureau of Statistics, “2013 China Innovation Index was 152.8” (2013 年中国创新指数为 152.8), March 2, 2015, http://www.stats.gov.cn/tjsj/ztbgb/201503/t20150302_687853.html.

However, in each area, the plan is more hesitant when it comes to reforming the regulatory role of the state. This dichotomy between economic and political ambition is most clearly visible in the plan’s most important section, on innovation, but applies throughout the plan.

The most important way in which this difference between economic and regulatory change exhibits itself in the innovation space concerns how clearly the plan identifies priority technologies. As in earlier plans, the 13th provides lists of technologies and sectors in which China needs to advance. But compared to earlier plans, the 13th is incredibly ambitious (see Table 4.5). The plan highlights nine general initiatives to promote technologies in different sectors, including the “Sci-Tech Innovation 2030—Megaprojects,” “Made in China 2025,” and Strategic Emerging Industries (SEIs). Altogether there are approximately 75 priority technologies, more than the 57 highlighted in the 12th 5YP. (There is also a long list of 90 trans-sectoral initiatives.) Moreover, each of these 75 technology areas actually includes a range of more specific technologies and products. For example, there are six general SEIs—new-generation information technology, biotech, spatial information and intelligent perception, energy storage and distribution, advanced materials, and new-energy vehicles—but there are at least 50 specific technologies that fall within these categories.9 The detailing of such specific technologies is the most important signal that the Chinese state is still not a passive observer focused solely on providing public goods.

These are not just empty wish lists. The government plans to spend billions, if not trillions, of yuan supporting the development and commercialization of these technologies. Some financing will come through the fiscal system via grants and subsidies; Li Keqiang said the government has budgeted RMB 500 billion to spend on 13th 5YP projects in 2016.10 However, an increasingly large proportion of financing will be funneled through state-controlled banks and investment funds.11 By the end of 2015, China had 780 government-connected investment funds, with a total value of RMB 2.18 trillion. Almost 300 funds, with RMB 1.5 trillion in capital, were created in 2015 alone.12 One economist from the experts committee reaffirmed that investment in technology should not simply be left to the market, citing NASA in the United States as a good model for China’s advanced technology programs.

A second sign of a state commitment to support domestic technologies is the reemergence of the term “indigenous innovation” (自主创新). The expression was originally promoted during the

9. SEIs were first defined by Premier Wen Jiabao in 2010. Longtime observers of China will notice that the number of SEIs has changed, from seven to six. The “environmental protection” industry has been removed and is affiliated with other initiatives, and the advanced manufacturing sector has been subsumed under the “Made in China 2025” initiative. For more details on the original SEI initiative, see Scott Kennedy, “Indigenous Innovation: Techno-Nationalist Retreat?,” China Policy Watch (GaveKal Dragonomics, March 2, 2012).
11. For example, see “Outline of 13th 5YP,” 40, 42.
Hu-Wen administration to emphasize encouraging domestic firms to invent new technologies, modify existing ones, and acquire foreign technology. It quickly became associated with technonationalist policies such as supporting unique domestic technology standards and mandating that government procurement prioritize domestic technologies. Following the resolution of several conflicts with foreign governments and businesses, Chinese officials stopped using this term at least as far back as 2012 and instead started to use the phrase “innovation-driven development” (创新驱动发展). But surprisingly, “indigenous innovation” appears six times in the 13th 5YP; it received only four mentions in the 12th 5YP. It is unlikely that its rehabilitation has no material significance. Instead, it suggests that achieving technology self-sufficiency is an important, even if unachievable, goal for much of the leadership.

The third sign that the plan does not fully break with past habits of interventionism is its extended but cautious discussion of improving regulation to better facilitate technological innovation. To its credit, the plan’s discussion of regulation is couched in a general framework supporting stronger market mechanisms. We heard the same calls from officials in many of our interviews and

### Table 4.5. Industrial Policy Redux: Targeted Sectors and Projects

<table>
<thead>
<tr>
<th>Sector-Specific Projects</th>
<th>Trans-Sectoral Projects and Plans</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Sci-tech Innovation 2030–Megaprojects (15)</td>
<td>• Mega Talent Projects (6)</td>
</tr>
<tr>
<td>• Agriculture Modernization Megaprojects (8)</td>
<td>• New-Model Urbanization Construction Megaprojects (8)</td>
</tr>
<tr>
<td>• Made in China 2025 (8)</td>
<td>• Special-Form Regional Development Megaprojects (6)</td>
</tr>
<tr>
<td>• Advanced Equipment Innovation Development Projects (8)</td>
<td>• Ocean Megaprojects (4)</td>
</tr>
<tr>
<td>• Strategic Emerging Industries (6)</td>
<td>• Resource Conservation Megaprojects (5)</td>
</tr>
<tr>
<td>• Informatization Megaprojects (8)</td>
<td>• Environmental Treatment Megaprojects (6)</td>
</tr>
<tr>
<td>• Advanced Transportation Key Projects (10)</td>
<td>• Mountain Ecology Projects (8)</td>
</tr>
<tr>
<td>• Energy Development Megaprojects (8)</td>
<td>• Belt and Road Initiative</td>
</tr>
<tr>
<td>• Water Security Guarantee Projects (4)</td>
<td>• Production Capacity Cooperation</td>
</tr>
<tr>
<td>• Address sectors with overcapacity</td>
<td>• Poverty Reduction Key Projects (8)</td>
</tr>
<tr>
<td></td>
<td>• Education Modernization Megaprojects (9)</td>
</tr>
<tr>
<td></td>
<td>• Healthy China Action Plans (8)</td>
</tr>
<tr>
<td></td>
<td>• Basic Public Service Project List (8)</td>
</tr>
<tr>
<td></td>
<td>• Promote Employment Action Plans (5)</td>
</tr>
<tr>
<td></td>
<td>• Society Care Action Plan (4)</td>
</tr>
<tr>
<td></td>
<td>• Culture Megaprojects (8)</td>
</tr>
</tbody>
</table>

Note: number of more specific sectors and projects in parentheses.
meetings for this project, and this is a standard part of official rhetoric. Yang Weimin, the deputy director of the LSGEF and a key drafter, made extensive remarks after the proposal was issued in October, in part saying: “There certainly are new growth points; the key is to depend on the market to discover them.” Yang echoes the sentiments of Chinese economists, many of whom in the internal debates pressed for greater market liberalization. It is far from clear, though, that they got their way.

The 13th 5YP delves into 10 areas of regulatory reform (see Table 4.6), and in each there are explicit calls for expanding market-oriented policies. Nevertheless, the discussion is either too vague to be meaningful or is partial and hedged in one way or another. Two “canaries in the mine” are the plan’s treatment of SOEs and the financial system.

It is tempting to exaggerate how dominant SOEs are in China’s economy. As Nicholas Lardy and others have shown, their share of output, sales, exports, and loans have all fallen significantly in the last three decades. Despite the relative growth of the private sector, there are still 150,000 SOEs, and their total assets have continued to rise, while their productivity has continued to fall, the main source of China’s corporate debt problems. Many SOEs essentially have administrative monopolies for certain products and in certain localities, and their corporate governance is highly opaque. Fully aware of these problems, the CCP and State Council issued a landmark document last summer sketching the framework and boundaries of potential reforms. Since then, they have issued a series of pilot reforms encouraging more powerful boards of directors and corporatization, allowing SOEs to receive minority investment from private sources, and having SOEs in commercial sectors face more competition. These policy moves are perhaps the most tentative of all reforms.

The 13th 5YP breaks no new ground on SOEs. It repeats the need for reforms to SOEs’ internal governance and their competitive environment and encourages SOEs going forward to invest more of their resources in public services and national security–related sectors. There are vague calls for modifying how the state manages SOE assets and capital, which may be an oblique reference to proposals to give SOEs more internal control along the lines of Singapore’s Temasek. But the likelihood of the CCP allowing genuinely independently run SOEs seems quite low. The plan is crystal clear that the main purpose of these adjustments is to strengthen SOEs as national champions at home and abroad and protect their assets. This is why there is no discussion about

Table 4.6. Promoting Innovation through Institutional Reform

<table>
<thead>
<tr>
<th>Issue</th>
<th>Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>R&amp;D</td>
<td>Promote R&amp;D among companies, corporate alliances, and universities;</td>
</tr>
<tr>
<td></td>
<td>strengthen national laboratories; create regional innovation and</td>
</tr>
<tr>
<td></td>
<td>development zones.</td>
</tr>
<tr>
<td>Mass</td>
<td>Facilitate the creation of start-up firms, ease access to funding.</td>
</tr>
<tr>
<td>entrepreneurship</td>
<td></td>
</tr>
<tr>
<td>Talent</td>
<td>Strengthen innovation training, links to industry, allow flow of labor</td>
</tr>
<tr>
<td></td>
<td>across sectors, improve salary and benefits across the country,</td>
</tr>
<tr>
<td></td>
<td>improve permanent residency system for international talent.</td>
</tr>
<tr>
<td>SOEs</td>
<td>Allow independent operations in commercial sectors, introduce market</td>
</tr>
<tr>
<td></td>
<td>mechanisms in public services, reform corporate shares system and</td>
</tr>
<tr>
<td></td>
<td>management governance, expand private-sector competition.</td>
</tr>
<tr>
<td>Property</td>
<td>Strengthen property rights related to SOE assets, real estate, and</td>
</tr>
<tr>
<td>rights</td>
<td>intellectual property.</td>
</tr>
<tr>
<td>Pricing</td>
<td>Reduce government intervention for pricing and sale of land; free up</td>
</tr>
<tr>
<td></td>
<td>pricing for commercial goods and services, utilities, and telecom.</td>
</tr>
<tr>
<td>Fair</td>
<td>Improve competition policy, expand market entry, improve market exit,</td>
</tr>
<tr>
<td>competition</td>
<td>enforce environmental and product safety rules.</td>
</tr>
<tr>
<td>Government</td>
<td>Simplify government, decentralize authority.</td>
</tr>
<tr>
<td>regulation</td>
<td></td>
</tr>
<tr>
<td>Fiscal</td>
<td>Reform tax system and budgeting process.</td>
</tr>
<tr>
<td>system</td>
<td></td>
</tr>
<tr>
<td>Financial</td>
<td>Further reform interest rates, securities markets, Internet finance,</td>
</tr>
<tr>
<td>system</td>
<td>financial regulatory institutions, regulatory structure.</td>
</tr>
</tbody>
</table>

Note: Listed in order of discussion within the 5YP.

privatization or bankruptcy in this part of the 5YP. Failure for SOEs is not an option.\(^\text{17}\) It appears that, in the final analysis, SOE reform will only be measured by one criterion—if SOEs are successful—not if they are managed better or if unsalvageable ones are properly disposed of. This may be why one participant in the drafting process told us that his personal measure of success is if by 2020 the number of SOEs in the Fortune 500 doubles from 54 to 108 companies, and if some

\(^{17}\) The plan’s chapter on SOEs begins by repeating the long-existing official rhetoric: “Maintain public ownership as the core, jointly develop the multi-ownership economy.” And the closest the plan comes to mentioning failure is encouraging the principle of “survival of the fittest” (优胜劣汰). “Outline of 13th 5YP,” 21.
SOEs develop famous brands, hold more patents, and pay more taxes than now. If he represents mainstream Chinese official views, China’s approach to SOEs has not changed.

The clarion call for financial reform seems a little less out of tune, but could be sharper. The challenges with SOEs are mirrored in China’s highly leveraged financial system. Unlike with SOEs, there have been regular changes to the financial system under Xi Jinping, reforms pushed by central bank governor Zhou Xiaochuan (周小川). Nevertheless, China’s state banks still dominate the financial landscape, and the securities markets are still subject to regular intervention.

To its credit, the 13th 5YP continues the recent trend of liberalizing reforms. It calls for improving the commercial banking system, expanding private investment in the banking sector, developing microfinancing, and standardizing Internet finance. There is also language calling for continued improvement of market mechanisms related to interest rates and setting the foreign exchange rate, better usage of the yield curve for treasury bonds to serve as the benchmark interest rate, and pushing forward markets for interbank lending, repos, commercial paper, foreign exchange, gold, commodity futures, and derivatives.

But the leadership and financial regulators are highly concerned about maintaining outward financial stability, not to mention continuing support for priority sectors. One financial sector official told us that state banks, borrowers, and securities investors are still not prepared to fully accept and price risk or engage in sophisticated hedging activity; and hence, government intervention in the financial sector is still necessary until sector participants develop a stronger “market consciousness.” Such circular logic is an argument for continuing this hybrid system. And so, although the direction of change is clear, it is qualified in the plan with less than emphatic terms such as “expand,” “make sound,” “standardize and develop,” “safely promote,” and “explore.” This explains the plan’s watered-down call for a standardized initial public offering registration system and a third board for high-tech firms, as well as recent policy steps to slow down the growth of Internet banking, essentially condone debt swaps by local governments to become bailouts, have the NDRC directly monitor corporate bond issuers instead of depending on credit rating agencies to do that task, and intervene in the foreign exchange market.

The mixed message of gradual improvement of market mechanisms is equally visible in the discussion of other elements of regulatory reform. The discussion of maintaining fair competition is brief and anodyne, with little that is objectionable. This single paragraph calls for, among other things, improved competition policy, open market access, better market exit mechanisms, and developing a “market supervision and antimonopoly law enforcement system.” These are well-meaning goals, but they are not ironclad promises to radically change behavior by 2020. For example, there is no call to make SOEs chief targets of antimonopoly law enforcement; quite the opposite, the policy trend is to encourage SOEs to merge to help them avoid collapse or grow stronger regardless of the competitive consequences for private and foreign companies. The euphemism “market exit mechanisms” is used instead of “bankruptcy,” a term that only appears once in the plan, in the discussion on possible ways to address the short-term problem of

overcapacity. Given this, one cannot expect bankruptcy to shift from being a state-dominated and highly exceptional route to closure to a company-driven process to dissolve or reorganize a firm, sell its assets, and prioritize handling the claims of creditors.

One longtime industry leader in China who has grown cynical watching promises fail to materialize summed up his reaction to the proposed regulatory changes in the 13th 5YP: The plan is composed of “beautiful words,” he told us. “But they say one thing and do another. . . . In China what the government says goes.” We are less cynical and see a more mixed outcome, but he would be right in not expecting too much change in the near term.

THE ENVIRONMENT AND THE GLOBAL ECONOMY:
A CLIMATE FOR LIMITED CHANGE

The other components of the 13th 5YP have the same dual character of advocating a substantial economic transformation while being much more hesitant with governance reform.

As mentioned earlier, the plan’s treatment of the environment and resources is impressive. The number and breadth of targets reflects a significant jump forward in the prioritization of the environment. Although the quantitative targets could be set higher, they needed to be achievable to be accepted by the leadership and included in the plan. Beyond the numbers, there is an extensive list of supporting policies to expand conservation efforts, increase energy efficiency, reduce pollution, and be on a path to a reduction in carbon emissions. Again, more could be done, but the shift from earlier 5YPs is stark.

Who deserves credit for this progress? To some extent, it is a natural evolution to pay greater attention to environmental concerns as the country becomes wealthier, a pattern from other countries that China is repeating. But no change happens without actors taking bold steps. In China’s case, some credit goes to the grassroots environmental movement as well as the bureaucrats in the Ministry of Environmental Protection (MEP), all of whom have worked tirelessly to explain the importance of addressing pollution and climate change and offer practical measures. Green technology firms also have shown how improving the environment supports economic growth. Efforts by the international community to bring China into the global conversation to deal with climate change have also been important. Not to be missed was the small but important step of the U.S. Embassy in Beijing in 2008 installing a PM 2.5 meter on its roof and reporting the readings over social media, an action originally opposed by China but then later accepted and integrated into its own system.20 But the addition of new targets and extended discussion of “green development” in the 13th 5YP most likely occurred only because of the personal interest of Xi Jinping himself. According to an environmental policy analyst, when Xi was party secretary of Zhejiang (2002–2007), he developed a strong appreciation for the environment, in part as a result of the challenges of addressing the polluted water of Lake Tai, in the northwestern corner of the

province.\textsuperscript{21} He brought that concern with him to Beijing. It appears that the MEP did not have to overcome Xi’s resistance, but was in fact empowered by him. He reportedly installed a political ally, Chen Jining, as the MEP’s minister, to carry out his preferences.\textsuperscript{22}

Nevertheless, as with other elements of the 5YP, these goals are expected to be achieved primarily by state intervention and regulatory fiat. Markets on their own are not driving greater environmental protection anywhere in the world, but they are even less effective in China. To promote green technology, the government is subsidizing R&D and providing incentives for companies and consumers to purchase green goods, such as electric vehicles. The government is raising fines for pollution and threatening to shut down large polluters, both to achieve environmental targets and reduce overcapacity. China is developing a cap-and-trade system for carbon and has created pilots in a small handful of cities. But, like all pollution markets, it operates in an artificial way. China is supposed to launch national pollution markets in eight industries in 2017, and the likelihood of market participants being sufficiently sensitive to “market” prices for pollution is not high, and hence, the government may be forced to mandate market sensitivity, a contradiction.

The treatment of the global economy in the 13th 5YP likewise has a dual character, but of a slightly different sort. The plan advocates substantially reducing trade and investment barriers, but primarily for Chinese industry going abroad, and only secondarily for foreign industry seeking access to China’s market and, in that case, only in so much as such access serves China’s economic priorities. The dominant focus in this section is facilitating Chinese exports and investment abroad. The text calls for expanding domestic export platforms and helping enterprises across different regions collaborate to be more internationally competitive. Under the umbrella of “cooperation on international production capacity and equipment manufacturing,” it advocates investing in heavy industry and transportation sectors globally, and, in the process, to “promote the going out of equipment, technology, standards, and service.” A full chapter is devoted to promoting the “Belt and Road” strategy, and utilizing the Asian Infrastructure Investment Bank (AIIB), the New Development Bank, the Silk Road Fund, overseas Chinese, and other sources of international capital.

The discussion on expanding market access to China is shorter and more qualified. The plan encourages “opening” investment in preschool education, construction design, accounting and auditing services; “expanding” market entry for banking, insurance, securities, and senior care; and “encouraging greater foreign investment” in advanced manufacturing, high tech, conservation and environmental protection, modern services, and in central, western, and northeastern China; and establishing R&D centers. There is discussion of improving the commercial environment for foreign businesses by creating a “fair competitive market environment, highly efficient and clean governing environment, just and transparent legal and policy environment, and open and inclusive cultural environment.” In addition to expanding construction of experimental free-trade zones, it suggests fully implementing a “pre-establishment national treatment negative list management

\textsuperscript{21} For comments by Xi when he was chair of Zhejiang’s leading small group on ecological construction, see Bao Hongjun, “Zhejiang Party Secretary Xi Jinping: Blue Water and Green Hills Are Silver and Gold Mountains” (浙江省委书记习近平：绿水青山就是金山银山), People’s Daily, April 4, 2016, http://politics.people.com.cn/GB/14562/4322248.html. Also see “China’s Xi Vows Reform to Make Environment Watchdog More Independent,” Xinhua, November 3, 2015.

system.” It also calls for improving forex management service, expanding international e-commerce, and strengthening intellectual property rights protection and antitrust enforcement.

The discussion of greater liberalization of China is accompanied by several caveats in the plan. Investment is encouraged only in those sectors where China is seeking to develop domestic capacity to move up the value-added chain or in areas required by previous commitments. In any case, “expanding” market access does not mean granting full access. The plan also calls on China to “perfect” its foreign investment national security review system. In finance, the plan calls only for China to open its capital account in an “orderly” way and “raise the convertibility level” of the renminbi and “steadily promote the internationalization of the renminbi.” Finally, there is language calling on the protection of the multilateral trading system and the strengthening of regional and bilateral trade and arrangements, but priority is placed on arrangements along the Belt and Road, the Persian Gulf, and East Asia. The plan calls for only “continued advances” in investment agreements with the United States and European Union.

Finally, as with the 12th 5YP, the 13th calls for improvements in global economic governance. But the 13th is more precise about what needs to be improved, and for the first time it expands the discussion to include international security issues. It calls for making the global economic governance system fairer by reforming the international monetary system and international financial regulation, as well as strengthening international coordination of monetary policy and other steps to promote financial security and steady economic growth. It expects China to actively participate in international rule making related to the Internet, oceans, the Arctic and Antarctic, and space. The plan also calls on China to “accept more international responsibility” by expanding foreign aid, implementing the 2030 Sustainable Development Agenda, and addressing security problems such as terrorism, proliferation, cybersecurity, and corruption. The confident discussion of global governance reinforces the impression that greater openness should serve China’s interests and that China should be a “rule maker,” not just a “rule taker.”

**CONCLUSION**

The 13th 5YP is an impressive document of strategic import. It has a relatively sober assessment of China’s economic problems and a clear vision for the kind of economic transformation China needs to undergo in the coming years. However, this ambitious vision is not matched by a concomitant change in the role of the state. Whether it is in regard to developing new technologies, reforming regulatory institutions, improving the environment, or engaging the global economy, although the plan is replete with calls for further utilizing market mechanisms, the visible hand of the state continues to play a major role in determining winners and losers and regulating behavior.

The sense that market institutions may regularly give way to state intervention is reinforced by other areas of governance, only some of which are mentioned in the plan. In the past several years, there have been greater constraints placed on domestic and foreign civil society groups, the

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media, lawyers, and scholars. At the same time, controls on the Internet have expanded. The anticorruption campaign has made officials risk averse. This is the first 5YP to have a chapter dedicated to strengthening the leadership role of the CCP in society. Lastly, in various places the plan emphasizes the need to protect China’s economic, cyber, and national security. It is likely that the collective consequence of these efforts to strengthen political control and national security are not supportive of the strengthening of unbiased market institutions, the free flow of information, and risk-taking by companies and individuals that is helpful in improving efficiency and promoting the creativity that lays behind innovation. And so, even though the 13th 5YP calls for greater use of the market, the broader political environment may discourage the realization of those plans.
Variations on a Theme: Sectoral and Regional Patterns

INTRODUCTION

Five-year plans are mammoth documents that touch upon every aspect of China’s economy and society. The themes and priorities of the 13th 5YP inevitably treat different industries and regions in different ways. To provide more nuance to the analysis in the previous chapter, we first look at what the plan likely means for the information and communications technology (ICT) and health care sectors, and we then provide a thumbnail sketch of variation across provinces. The ICT and health care sectors are both highly important to the Chinese economy and are prioritized in the 13th 5YP, yet they are quite different in several ways. The ICT sector is thriving and growing rapidly and is relevant to both industrial policy and national security concerns. By contrast, China’s health care system is struggling: China’s domestic pharmaceutical and medical equipment capacity is just beginning to emerge, and the health care service experience for most Chinese is far from ideal.

Obtaining adequate information for this part of the report was particularly challenging. As noted above, beyond the national plan, there are a series of specialty plans on different issues. There were 134 specialty plans related to the 12th Five-Year Plan. According to interview sources, there will be no more than half as many this time because the leadership concluded that fewer plans could be managed more effectively. Unfortunately, specialty plans are mainly issued after the national plan, and in some cases not until the end of the year. Among them, there are specialty plans being drafted for SEIs, innovation, and health care, but these are unlikely to be issued before June 2016. As a result, our sectoral analysis depends on the national plan and interviews about trends in these sectors. The provincial plans are completed before the national plan, but they are not all issued in a timely way. Hence, our analysis is based on a review of 21 provincial plans available at the time of this report’s writing, along with information on other provinces gleaned from local media reports and government websites. Sorting through these sources yields the

conclusion that intervention across sectors and regions varies in type and scope, rationale, and consequences.

**ICT: HELPING THE HOME TEAM, HELPING CHINA**

ICT has been a priority sector for the Chinese government for many years. Several preceding 5YPs have emphasized the importance of the industry to the Chinese economy, and there has been a long series of technology plans, policies, and regulations directed at strengthening the capacity of domestic companies and diffusing ICT widely in society.\(^2\) China has come a long way from the early days in the 1980s, when it took months to install a fixed-line phone in one’s apartment and creating a document meant writing it by hand or using a clunky Chinese typewriter. Computer ownership rose from 9.7 PCs per 100 households in 2000 to 87 in 2012, and mobile phone ownership rose from 19.5 per 100 households in 2000 to 213 in 2012. By 2014, China had installed over 20.6 million kilometers of fiber-optic cable, and that year telecom services generated RMB 1.8 trillion in business.\(^3\) Other data on the spread of consumer products and equipment are equally impressive. The corporate landscape has changed dramatically since the 1980s, when the Beijing Stone Group was making word processors and the Legend Group (now Lenovo) was distributing foreign-made personal computers. China now has major players in telecom equipment (Huawei and ZTE), optical fiber (Yangtze Optical Fiber & Cable), cloud computing (Alibaba and 21Vianet), servers (Langchao and Inspur), social media (Tencent, Sina, and Baidu), and mobile phones (Huawei and Xiaomi).

But ICT in China is still a work in progress. ICT has diffused into personal lives and company offices, but its penetration into manufacturing is still relatively limited. There are many areas of Chinese life, from education to health care, where information technology has had only limited reach. In addition, although Chinese companies have gradually moved into telecom equipment, consumer products, and services, companies from elsewhere still dominate the upper reaches of the industry. For example, China’s semiconductor industry has grown to have over 900 firms and China’s share of global semiconductor revenue reached 13.4 percent in 2014, but China is still dependent on imports for most types of advanced integrated circuits.\(^4\)

It is safe to say that ICT is the highest priority sector in the 13th 5YP. ICT has three attractions that are highlighted in different parts of the plan. First, there is a great deal of value to be created and gained for companies who are successful in design and branding (the high points of Stan Shih’s smile curve). The rise of wages in China is making low value-added assembly and manufacturing, even if done in high volumes, a less attractive business strategy. Second, ICT has multiplier effects\(^5\).

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2. For a detailed look at policies in a number of technologies, including ICT, see Yu Zhou, William Lazonick, and Yifei Sun, eds., *China as an Innovation Nation* (Oxford: Oxford University Press, 2016).
by helping to improve efficiency and create new opportunities in many other areas of the economy, through automation, smart manufacturing, finance, urban planning, health care, and transportation. Third, ICT has important implications for China’s domestic security and national security, which animates the desire to control the population’s access to information and ideas from the global Internet and to ensure the security of Chinese government and corporate networks.

Hence, it is no surprise that China seeks to promote the domestic ICT sector. Industrial policy goals originally dominated official thinking, but in the last five years, particularly since the revelations from Edward Snowden, national security concerns have changed China’s calculus. The propaganda and national security elements of China’s political system have had a larger voice in shaping recent policy. Chinese business executives have also utilized officials’ fears to advocate for domestic technology solutions.

The 13th 5YP includes the ICT sector in many of its priority projects. Foreign observers are most aware that the first of the SEIs’ six sectors is “new-generation information technology,” which includes integrated circuits, artificial intelligence, smart hardware, new displays, mobile smart terminals, 5G mobile telecom, and advanced sensors and wearable equipment.5 But several other major initiatives (see Table 4.5) also highlight ICT, among them:

- **Sci-Tech Innovation 2030–Megaprojects**: Quantum telecom and quantum computing, smart grids, big data, smart manufacturing
- **Informatization Megaprojects**: Broadband China, Internet of Things, cloud computing, Internet-Plus, Big Data, e-government, e-commerce, guaranteeing Internet security
- **Made-in-China 2025**: Advanced information technology, automated machine tools
- **Agriculture Modernization Megaprojects**: Internet-Plus
- **New-Model Urbanization Construction Megaprojects**: Smart cities
- **Poverty Reduction Key Projects**: Internet-plus (online business, raise money, tourism)
- **Education Modernization Megaprojects**: Education informatization (K–12, long-distance, and online education)
- **Healthy China**: Smart health care (electronic health files, big data, online health care)
- **Culture Megaprojects**: Literacy for villagers via digital libraries

Beyond including ICT in these priority projects, one can expect that the regulatory mechanisms cited in the plan will be utilized to assist the sector’s growth, including the support of “backbone enterprises” (骨干企业). Government funding, loans from state banks, stock listings, bonds, and investment funds will all be mobilized. By the summer of 2015, there was not only a national Integrated Circuits Fund, headed by former Ministry of Industry and Information Technology (MIIT) official Ding Wenwu (丁文武), there were 24 provincial and city Integrated Circuit (IC) funds as well. The number and range of funds will certainly climb. The plan also highlights the importance of

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5. According to one source, the specialty plan on SEIs could choose different sectors as SEIs from those in the national 5YP.
strengthening a variety of regulatory regimes, including standards, intellectual property, competition policy, the development of free-trade zones, and overseas green-field investment and acquisitions. The phrase “secure and controllable” (安全可控), used over the past year by China to explain the need to localize technology in banking and other sectors, does not appear in the 5YP. However, the plan does call for the development of “indigenous and controllable operating systems.”

HEALTH CARE: HELPING EXPAND ACCESS

Since the beginning of the Reform era, indicators for the quality of health of Chinese have gradually risen, but improvement has not kept pace with the rise in per capita incomes, and access to quality care is highly uneven. China’s health care sector is also a poor performer. Few of China’s pharmaceutical and medical equipment firms, hospitals, and health insurers have been consistently profitable. Unlike in ICT, there are few “national champions” to protect, and national security is essentially a nonissue. Nevertheless, the significance of market mechanisms is far more limited in health care. Instead, the state intrudes into virtually every aspect of the sector. This is the result of entrenched interests, but also reflects a deep-seated fear that greater use of market mechanisms would make health care provision worse, not better. This lack of consensus about the place of markets has not stopped a long series of market-oriented reforms from being issued, but it has hindered their effective implementation. The 13th 5YP reflects these tensions, and as a result, it puts forward plans for significant, but still incremental change. The tepid treatment of markets and the dominant role of government is visible in each aspect of the system.

China’s domestic pharma sector could at best be called “nascent.” This is largely because pharma is an R&D-intensive sector in which it often takes billions of dollars and several years to develop a drug and introduce it into circulation, a particularly risky proposition, considering China’s historically weak intellectual property (IP) regime and the relative ease of the high-volume, low-margin business strategy available in other sectors. Officials have tried to overcome this obstacle by subsidizing domestic R&D, strengthening IP rules and enforcement, setting up biotech parks, and encouraging global pharma leaders to invest in China and set up R&D facilities. The efforts have borne some fruit, as there have emerged a small number of successful domestic pharma firms, such as WuXi PharmaTech, and a growing number of R&D firms that specialize in carrying out contracted research for the global giants.

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8. In order to highlight the contrast with ICT, this chapter has only limited discussion of medical devices and equipment. This subsector shares more characteristics with ICT, as there are a small number of well-supported and successful companies, such as United Imaging, a leading domestic producer of MRI machines.
If pharma companies overcome the funding, manpower, and IP issues, they face another daunting obstacle, having their drug approved by the China Food & Drug Administration (CFDA) and then added to the National Drug Reimbursement List, an essential step if a drug is to be made widely available in China. CFDA, though, acts at a glacial pace. According to interview sources, it takes five to eight years to have one’s drug approved in China, compared to two to three years in the United States. One reason is that the CFDA is woefully understaffed, having around two dozen employees to review applications; the U.S. Food and Drug Administration (FDA) has over 1,000 such staffers. Moreover, even if one’s drug is approved for sale, the reimbursement list has not been updated since 2009. Finally, until recently, drug prices were strictly controlled by a central authority. In May 2015, prices were officially liberalized, but bureaucratic power merely switched to provincial governments, who set up a drug procurement process that encourages companies to price their drugs as low as possible.

China's hospital system is also highly controlled. Public hospitals, which numbered over 13,000 in 2014, have more staying power than typical SOEs, as they face very little competition and are not permitted to fail (see Table 5.1). The central and local governments have officially encouraged private hospitals, and as of 2014, there were over 12,500 private hospitals around the country. Yet private hospitals are far smaller than their public counterparts, with an average of only 67 beds per facility compared to 310 in public hospitals. In 2014, less than 17 percent of total beds in the country were in private hospitals, and in 2015, private hospitals only accounted for 10 percent of all hospital revenue.

China’s almost 3 million doctors have been prisoners in this state-controlled system. They are not classified as regular workers, and they are tied to their hospitals just the way SOE and government employees used to be fixed to their official work units. As a result, hospitals have gotten away with providing meager wages to their doctors of only a few thousand yuan per month. Not surprisingly, it is hard to attract promising minds to consider medicine as a profession. As Table 5.1 shows, China has only 2.1 doctors per 1,000 residents, far below the rate in the United States (2.6) and Japan (2.8). Because of their terrible pay, some of those who do become doctors have been driven into corruption, taking bribes (masked as commissions or event fees) from drug companies and distributors in the hopes they press their hospitals to acquire certain drugs and encourage their patients to use them. Several sources reported that doctors also earn a large portion of their actual take-home pay from bribes from patients hoping to receive their care.

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14. Parallel data show that China’s shortage of nurses is even more severe. China’s figure of 2.2 nurses per 1,000 pales in comparison to the United States (11.1) and Japan (8.2). Organization for Economic Cooperation and Development, Health Statistics 2015.
Table 5.1. China’s Health Care Sector

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Health Care Expenditures</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total (RMB, billions)</td>
<td>865.99</td>
<td>3,531.24</td>
</tr>
<tr>
<td>% GDP</td>
<td>4.66</td>
<td>5.55</td>
</tr>
<tr>
<td>Out-of-Pocket (%)</td>
<td>52.21</td>
<td>31.99</td>
</tr>
<tr>
<td><strong>Health Care Facilities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hospitals (#)</td>
<td>18,703</td>
<td>25,860</td>
</tr>
<tr>
<td>Total Beds (#)</td>
<td>2,445,000</td>
<td>4,961,000</td>
</tr>
<tr>
<td><strong>Public Hospitals</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Facilities</td>
<td>15,483</td>
<td>13,314</td>
</tr>
<tr>
<td>% of Total</td>
<td>82.78</td>
<td>51.48</td>
</tr>
<tr>
<td>Beds</td>
<td>2,300,910</td>
<td>4,125,715</td>
</tr>
<tr>
<td>% of Total</td>
<td>94.11</td>
<td>83.16</td>
</tr>
<tr>
<td>Beds/Hospital</td>
<td>148.61</td>
<td>309.88</td>
</tr>
<tr>
<td><strong>Private Hospitals</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Facilities</td>
<td>3,220</td>
<td>12,546</td>
</tr>
<tr>
<td>% of Total</td>
<td>17.22</td>
<td>48.52</td>
</tr>
<tr>
<td>Beds</td>
<td>144,102</td>
<td>835,000</td>
</tr>
<tr>
<td>% of Total</td>
<td>5.89</td>
<td>16.83</td>
</tr>
<tr>
<td>Beds/Hospital</td>
<td>44.75</td>
<td>66.56</td>
</tr>
<tr>
<td><strong>Beds</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Per Capita Avg (/1,000)</td>
<td>2.83*</td>
<td>4.85</td>
</tr>
<tr>
<td>Urban Per Capita</td>
<td>4.90</td>
<td>7.84</td>
</tr>
<tr>
<td>Rural Per Capita</td>
<td>2.00</td>
<td>3.54</td>
</tr>
<tr>
<td><strong>Licensed Doctors</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>2,042,135</td>
<td>2,892,518</td>
</tr>
<tr>
<td>Per Capita (/1,000)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1.56</td>
<td>2.12</td>
</tr>
<tr>
<td>Urban</td>
<td>2.46</td>
<td>3.54</td>
</tr>
<tr>
<td>Rural</td>
<td>1.26</td>
<td>1.51</td>
</tr>
<tr>
<td><strong>Registered Nurses</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1,349,589</td>
<td>3,004,144</td>
</tr>
<tr>
<td>Per Capita (/1,000)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1.03</td>
<td>2.20</td>
</tr>
<tr>
<td>Urban</td>
<td>2.10</td>
<td>4.30</td>
</tr>
<tr>
<td>Rural</td>
<td>0.65</td>
<td>1.31</td>
</tr>
</tbody>
</table>

*For 2007.
To round out this picture, the financing of health care is also state-controlled. In one way, this is progress; the end of the work-unit system in urban areas and dissolution of communes in rural areas left urbanites and peasants, respectively, with little-to-no state support. Under Hu Jintao and Wen Jiabao, the central government radically expanded funding and coverage of state-based social insurance (yibao, 医保). The proportion of health costs covered by yibao has risen steadily, but funding is still inadequate for many. In addition, most private hospitals have had difficulty being approved as part of the yibao system, a large reason private hospitals have not grown further. Finally, the government has permitted the emergence of domestic private health insurance, but few take advantage of it since private insurance is expensive, and customers have difficulty being reimbursed because of limitations over coverage (the kinds of procedures) or facilities that take their insurance. As a result of these various factors, total health care spending in China is still only 5.6 percent of GDP, far lower than in the United States (17.1 percent) or Japan (9.1 percent).\textsuperscript{15}

A series of reforms have been issued during the past year following the uncovering of entrenched corrupt drug distribution practices by domestic and global pharma companies. In the last year there have been a series of policy measures aimed to liberalize drug prices and strengthen the approval process, to give doctors more latitude to move hospitals, and to make health insurance more portable.\textsuperscript{16} Drug companies and distributors have curtailed some of their activity, at least outwardly.\textsuperscript{17} Despite these initial steps, the core of the original system is still in place: drugs face a long approval process, their pricing is still subject to government intervention, public hospitals still are well protected, doctors still have difficulty changing positions at will, and the private insurance sector still faces huge hurdles to being adopted by consumers.

These reforms have not gone further for several reasons. First, the current arrangement serves a lot of special interests: ministries, commissions, local governments, domestic drug manufacturers, drug distributors, domestic equipment makers, public hospitals, and doctors who cumulatively earn a decent income. Even many consumers benefit from a system where government provides substantial funding and service is rationed to keep costs low.

The second reason is that there is no consensus that a fully market-oriented health care system would yield better health care outcomes for Chinese society. Some worry that if things were made easier for foreign pharma, private hospitals, doctors, and private insurers, the cost of health care would rise, and many who now are well treated would be priced out of the market. In addition, regulators need to consider what constitutes appropriate health care for China’s population. Supporting innovative new drugs may be less important than accessibility to drugs already known to address the kinds of health issues most common amongst the country’s population. In addition,


\textsuperscript{17} One longtime analyst extremely familiar with the distribution system believes that corrupt behavior is still endemic in what is still a highly bureaucratic system.
according to one source, the Ministry of Finance is worried that if private insurance expands too quickly, it may lead to greater demand for all kinds of health care, thereby requiring greater government spending via the yibao system than would be fiscally prudent. And finally, officials believe that vaccines are so important to the population’s health that the state needs to intervene to either have these drugs sourced domestically or to press for low prices. In short, in this view, government rationing of health care yields a better outcome than the free market.

Market advocates in China respond that the current system is delivering suboptimal care for many people. They suggest that given the high expense of developing new drugs, innovators need to be compensated sufficiently; otherwise, innovation will decline. They also suggest that although a more liberal market could result in higher prices for some types of services, these costs would be borne by those in society most able to afford them, and leave cost structures relatively unchanged for most. Moreover, they believe liberating doctors from their home hospitals is central to them being better compensated and not turning to drug companies and patients for additional income, which is itself a form of discrimination that disadvantages the neediest in the population.

The 13th 5YP tries to split the difference among the two sides to this debate. The plan identifies biotech as a strategic emerging industry and identifies several specific priorities: applications for genomes on a mass scale, customized health care, new drugs, breeding technologies and services, and gene pool and cell bank platforms. One industry insider suggested that the government’s ultimate aim is for the successful development domestically of two to three new drugs and the approval of at least one Chinese drug by the U.S. FDA by 2020. At the same time, authorities will encourage foreign investment and collaborative R&D in these areas. There are also clear calls in the plan for further promoting the liberalization of drug prices and speeding up the approval system for innovative drugs that have yet to be marketed anywhere in the world.18

The 5YP calls for reforming the public hospital system in several ways. It seeks to improve the internal management of hospitals and develop a strong multtier hospital system and clinics so that patients do not overburden top-tier hospitals. The plan also “promotes the equal treatment of nonprofit private hospitals and public hospitals.”19 These all count as only modest changes. The internal reforms for public hospitals are much like those planned for standard SOEs; it is hard to see how they will make a difference unless the broader competitive environment in which hospitals operate changes and unless public hospitals that consistently run deficits or are managed poorly are vulnerable to bankruptcy and closure. That is unlikely as long as all private hospitals, not just nonprofit ones, are unable to compete head-to-head. There is also no mention of encouraging investment by foreign companies in the hospital industry.

Reform of the medical profession is more promising but still qualified. The 13th 5YP calls for the creation of a new, more liberal salary system, efforts to attract more people to become doctors, and increased spending on training. While these are all positive steps, the plan could have gone

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further and entirely untethered doctors from any organization and allowed them and hospitals to
determine what kind of relationship would be mutually appealing.

The plan’s steps regarding insurance seem the most promising. It calls for fully unifying the rural
and urban *yibao* insurance schemes and having the system cover 95 percent of the population by
2020, encouraging private insurance companies to contract to manage the *yibao* system, promot-
ing the development of commercial health insurance, and facilitating the portability of public and
private insurance within a locality and between localities. This represents progress, but it will likely
take much longer than five years for private health insurance to substantially expand its contribu-
tion to China’s overall health care bill.

Would more thoroughgoing marketization serve China much better? It is hard to know for sure,
given that there are both successful and failed examples of privately-based, market-oriented health
care systems. It is likely that a more liberal system, coupled with appropriate regulation of the various
actors, could conceivably generate greater efficiencies and be widely accessible. One Chinese health
care expert suggested that perhaps the best benchmark of whether the various reform proposals
would actually transform the system would be to focus on the proportion of hospital beds that are
in private hospitals. In order for that figure to rise dramatically, for example, to 60 percent, it would
likely require changes in the other areas of the system, including the development and marketing of
drugs, the professional status of doctors, and the availability of private insurance. Only time will tell if
such analysis is justified or is overstating the benefits of market-oriented reforms.

**REGIONAL RESPONSES TO THE “NEW NORMAL”**

Provinces are supposed to draft five-year plans that are consistent with the national plan, but there
is always a gap between them, as well as variation across the country. This is in part because of
differing economic and political circumstances, but also because provincial plans are drafted and
issued ahead of the national plan. Central government officials tried to increase coordination
between Beijing and localities for the 13th 5YP. They were somewhat more successful than in the
past, but there are still significant differences across the country. Several areas stand out.

It is common practice that provinces pursue and report higher GDP growth figures than the na-
tional government. That is the case again with the 13th 5YP. The 31 provinces on average set an
annual growth target of 7.7 percent, 1.2 percentage points higher than the national rate of just over
6.5 percent. However, this gap is trivial compared to the gap in the 12th 5YP, when the national rate
was 7.0 percent and the provincial average was 10.3 percent, a whopping difference of 3.3 percent-
age points. Moreover, the variation across provinces is smaller than in the past. Chongqing,
Guizhou, and Tibet set the highest target, at 10.0 percent GDP growth, and Shanxi and Liaoning the
lowest, at 6.0 percent, but on the whole, there is a close clustering around 7.0–8.5 percent. Even if
these targets seem unachievable without substantial stimulus, provinces do appear to have ab-
sorbed the message that under the “new normal,” they should pursue lower growth targets.

Provinces have tried to varying degrees to emphasize the importance of markets, reduced govern-
ment intervention, and innovation. Every single plan uses the key phrases “negative list” and
“innovation driven,” and all encourage foreign investment. But there are substantial differences, with southeast coastal provinces’ plans more liberal than plans elsewhere. A comparison of the Shanghai and Zhejiang plans relative to those from Heilongjiang and Shanxi is instructive. The former are more resolute about the need to remain open and engage in reforms. They put more emphasis on reducing intervention, and they have more detailed descriptions of their reform plans compared to Heilongjiang and Shanxi. In Shanghai, officials stressed they have been given the authority from Beijing to be trailblazers and push the boundaries of what is permissible in order for the municipality to achieve its goals of being an international center for the international economy, finance, shipping, trade, and technology innovation.20 And, in Zhejiang, officials gave the impression that although the planning process is important, they recognize that the most successful industries in Zhejiang are those where government has intervened the least, and hence, where no detailed plans are necessary.21 Nevertheless, one should not overstate how liberal individual provinces’ plans are. Even in well-developed coastal provinces dominated by the private sector, government intervention is still commonplace.22 Promoting higher-value-added exports, outward investment, and high technologies are priorities throughout the country. All provinces follow the national guidelines of differentiating between SOEs in commercially competitive industries and those in utilities and public services, with SOEs in the latter sectors still heavily protected from the full winds of competition. In addition, every province has identified important SEIs that will be the recipient of their support. Most provinces identify the six national SEIs (though only half identify spatial information and intelligent perception), but the number of and the specific SEIs vary widely across provinces. Sichuan has the most, with 10: the six national SEIs, plus advanced manufacturing, nuclear power equipment, railways, and ocean technology. Shandong has the fewest, with just two: energy storage and distribution and new-energy vehicles. As with the national plan, the extent to which provinces are more or less liberal will not be determined by the text in their plans, but by how they implement the plans and other policies.

CONCLUSION

When we go beyond the general national perspective, we again find that there is no consensus for marketization. Provinces in coastal China have a stronger preference for more robust markets than those elsewhere, particularly in the northeast. But the difference is relative. The CCP and the government intervene in economies around the country. The story is similar when viewed through the prism of sectors. Officials in both the ICT and health care sectors have developed different but complementary justifications for intervention.

21. One Zhejiang official frankly told us that the main obstacle to good commercial practices is government intervention.
22. Nine provinces neglected to mention the key phrase of the Third Plenum Decision, which is also in the national 13th 5YP, that “the market should play a decisive role in the allocation of resources”: Beijing, Tianjin, Liaoning, Heilongjiang, Jiangxi, Gansu, Chongqing, Sichuan, and Fujian.
Conversely, the economic performance of the two sectors is vastly different; the problems in ICT pale in comparison to those in health care. We would propose that this difference is likely due to a greater (though still constrained) amount of competition in ICT, with both domestic private and foreign companies deeply involved in the industry. The major foreign pharma companies are all active in China, but compared to ICT, the extent of foreign and domestic private activity in the sector is relatively limited. Certainly a comparison with more sectors is necessary to reach any definitive conclusions, but the analysis in this chapter suggests that diversifying the ownership composition of companies in a sector is helpful in expanding competition that yields better products and services.
Implications for China, MNCs, and the Global Economy

Having combed over every inch of the 13th 5YP, one cannot but feel some measure of admiration for its drafters. China is a massive, sprawling economic and political organism. Quickly changing directions is no easy task, and it entails a tremendous amount of risk. Given the success of the last 38 years, the argument for “steady, careful, and incremental” can be justly defended.

Nevertheless, the dichotomy in the plan between its vast ambition to remake the economy and its far more modest adjustments to the regulatory landscape is stark. The confidence in the effectiveness of intervention seems like hubris, and the emphasis on innovation without liberalization of the social context translates into a narrower technology development program. Chinese officials in different settings have developed a range of rationales—industrial policy, national security, providing public goods—for their approach. Of course, these actions are not entirely homegrown. As one MOST official told us, even the United States has “protected its domestic industries for a period before opening up.” The question, though, is not whether others have done the same, but whether this approach is economically functional as China approaches the technology frontier and its financial system becomes more complex and connected to the global financial system.

To the extent China faithfully pursues the strategic vision of the 13th 5YP, it likely will have important effects not only on China, but on the life chances of MNCs that do business with China, and on the trajectory of the global economy more broadly.

If China maintains this approach, the likely pattern will be of growing volatility, with higher highs and lower lows. China will likely succeed in developing some technologies among the long list of priority sectors it has created, but the rate of success is unlikely to be high. Developing technology and moving up the value-added chain may make an economy more efficient, but not necessarily. It depends on how much is invested, where, and with what return. A dynamic of massive but misappropriated investment would likely result in China becoming a bloated technology powerhouse, with an economy not much more efficient than it is today. Misplaced investment has implications not only for those sectors, but also for China’s ability to address its environmental challenges in a sustained manner and to raise the social welfare of its citizens by raising incomes,
Reducing inequality, and providing a stronger social safety net. If these elements are interconnected, China would not fall into the middle-income trap, but instead would dig a tunnel sideways into it.

MNCs have four potential postures toward China. Some operate in precisely those areas where China wants to develop domestic capacity quickly or already has a large market presence. An example would be certain kinds of semiconductors. A second alternative is a sector that is a moderate priority for China, but is consumer-driven, and hence difficult for Chinese officials to dictate taste, such as in autos. The third option is a technology that complements or facilitates other technologies the Chinese are trying to make. Three good examples would be the nickel from Indonesia that goes into Chinese stainless steel, the avionics that go inside a Chinese commercial airliner, and the big-data analytic technology and cloud-computing capacity that helps China build smart cities to improve its urban planning. The fourth option is focusing on products and services the Chinese benefit from and where they either have no strategic interest or the market is large enough to comfortably accommodate multiple players, such as restaurants, hotels, and apparel.

The challenge for MNCs is to identify where their technologies and products fall on this list and then prepare accordingly. There are no fixed points on this list because Chinese capabilities and goals evolve over time. The 13th 5YP is a useful guide to the current landscape. The biggest challenge occurs when one occupies a space the Chinese covet, and the biggest opportunity is when one has a technology that serves as an input or complement to a priority technology for China. It may be appropriate for MNCs to genuinely or superficially shift strategy to align with the plan, but it is important that they at least go through the analytical exercise.

If China pursues the goals of the 13th 5YP in the manner described in these pages, it will put more stress on the global economy. China as an inefficient technology powerhouse will create opportunities for companies and countries to benefit as it grows (akin to the third posture mentioned above), but these entities will conversely face substantial challenges when China’s economy slows down because of excess capacity. Additionally, Chinese rapid expansion into new products and technologies could be a boon to those sectors, as it helps absorb costs to allow the scaling up of technologies that otherwise would not be affordable. Alternatively, China could over-invest in technologies and make it unaffordable for other participants to make it through dark times because they face tighter budget constraints. Put most simply, if China does not properly manage the scale of its investment, it could do for semiconductors and other high-tech sectors what it has done for steel and to some extent aluminum. The extent of this effect may be highly limited during the 13th 5YP period, but it worth monitoring.

The final question worth pondering is: What are the chances that China could put aside the 13th 5YP and pursue a double rebalance, using regulatory liberalization in service of a more comprehensive approach to improving efficiency beyond developing high technology? Could China, as Xi Jinping famously suggested, actually restrict “power within a cage of regulations”?1

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One way this could occur is if the 13th 5YP approach is not effective and, in fact, generates enough problems, including perhaps a financial crisis, that policymakers reassess their path. It is possible that the recent interview in the CCP’s flagship newspaper People’s Daily signifies the emergence of such worries, but it could also simply be an effort by one leader or another to shift blame for the current economic difficulties to someone else without actually embracing fundamental policy changes.2

A second source of change would be foreign pressure, either stepped-up trade remedies or the creation of new international rules that give China greater incentives to rebalance both its economy and regulatory system. The Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP) could both potentially fill that role. However, TPP has yet to be ratified, and negotiations over TTIP have not concluded. Bilateral and multilateral trade remedies have had some effect in constraining Chinese industrial policy excesses, but when taken too far often end up hurting MNCs and foreign economies as much as China. The effect of these “points of leverage” should be measured in years, or even decades, not months.

The final way in which China may take a detour from the 13th 5YP is if many companies, financial institutions, and localities in China dismiss the plan as inappropriate and adopt a more liberal approach in their daily activities, with companies pursuing a wide range of strategies and partnerships based on their own business calculations and without regard for the plan’s priorities. Of course, this happens every day in China, and many just feign compliance with Beijing’s guidelines. The further one is from Beijing, the more possible a strategy of superficial alignment or outright dismissal becomes. But as much as we like to believe in businesspeople purely as businesspeople, we should not overstate their ability to escape the gravity of Beijing’s orbit. Those whose job it is to see the plan through have a great deal of funds and other sources of leverage to gain a sufficient level of compliance to achieve their plans. They have done it at least 12 times before. The betting here is that the 13th time will be no different.

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Prior to joining CSIS, Kennedy was a professor at Indiana University (IU) for over 14 years. From 2007 to 2014, he was director of the Research Center for Chinese Politics & Business, and he was founding academic director of IU’s China Office. From 1993 to 1997, he worked at the Brookings Institution. Kennedy received his PhD in political science from George Washington University and his MA in China studies from Johns Hopkins School of Advanced International Studies.

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