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# Major Problems and Countermeasures of Foreign Trade in China under the Background of Expanding Domestic Demand

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**Abstract** Starting from China's macro-economic policy level and combining with the status of foreign trade in China, major problems in the development of foreign trade are analyzed under the background of expanding domestic demand, which is guided by the macro-economy, international finance, international trade and other related disciplines. Problems are mainly the inflation, the reduction of import, the trade protection, the increase in export costs, the reduction of export, the scale shrinkage of foreign trade, the speculation of short-term hot money, and the increase in risk of economic fluctuation. Finally, corresponding countermeasures are put forward, such as actively coping with the appreciation of the RMB, effectively increasing the anti-risk ability of RMB, firmly maintaining the currency stability of RMB, reducing the international trade friction, transforming the growth model of foreign trade, promoting the industrial and products upgrading of foreign trade, enhancing the benefits of foreign trade, forming an effective price competition mechanism, increasing the support in trade, improving the environment for trade development, correctly dealing with the relationship between government and foreign trade enterprise, controlling inflation, and restricting hot money speculation.

**Key words** Domestic demand, Macro-environment, Foreign trade, Countermeasure analysis, China

New problems appear in foreign trade due to the economic globalization and financial crisis. Expanding domestic demand and stimulating consumption help to reduce the impact of international financial crisis on Chinese economy. However, the continued expansion of domestic demand becomes adverse to the development of foreign trade through transmission mechanism and multiplier effect. Macro-economic environment in China and its major characters are introduced in this paper. Status of foreign trade in China is analyzed. Based on the perspective of expanding domestic demand, major problems in foreign trade development in China are expatiated and corresponding countermeasures are put forward.

## 1 Macro-economic environment in China and its major characters

In the year 2008, subprime crisis originated in the United States became a global financial crisis. Even the real economy in developing countries was seriously damaged. With the process of economy globalization and the further development of foreign trade, real economy in China was heavily damaged. After the reform and opening up, the United States, Europe and Japan have gradually become the most important trading partners for China. The import and export is one of the trikas for the rapid economic growth in China in recent twenty years. Economic tsunami caused by financial crisis affects the export processing enterprises in east coasts in China, leads to the lack of external demand and the decrease of income in western

and central areas which provide raw materials, energy and labor force. Therefore, to reduce the slowdown of export processing enterprises and the pressure of "soft landing", the Party Central Committee and the State Council actively implement the policy of "expanding domestic demand", accelerate the construction of infrastructure and stimulate consumption by the active fiscal policy and loose monetary policy, in order to realize the stability and progressiveness of GDP growth in China. Stimulating economic recovery by strong domestic demand has become one of the major characteristics of macroeconomic environment in China at present, as well as an important factor affecting the variation of import and export. In the year 2010, GDP growth of the first quarter reaches 11.9% in China, an increase of 5.7 percentage points compared with the lowest point since financial crisis (the first quarter of the year 2009). It is also 1.2 and 3.2 percentage points higher than the last quarter and the whole of 2009, respectively. After seasonal adjustment, annual rate of GDP is 12.2%, up by 0.9 percentage point compared with the last quarter<sup>[1]</sup>. There are also other characteristics, such as the rapid increase of industrial production growth rate, the substantial increase of enterprise benefit, the continuous expansion of price increase in upstream and downstream, the fall of actual growth rate, the decrease of growth rate of money supply, the slowdown of RMB loan, and the substantial growth in fiscal revenue. In the aspect of foreign trade, China has reached the level of pre-crisis and has greatly reduced the trade surplus. In March 2010, affected by the rapid rise of import price, the strong domestic demand and other factors, trade deficit has appeared in China for the first time since the May 2004<sup>[1]</sup>.

## 2 Status analysis of foreign trade in China

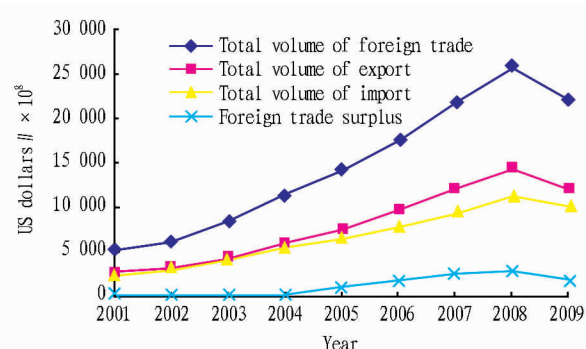
Since the reform and opening up in the year 1978, foreign trade development in China has achieved a significant breakthrough. Scale of foreign trade increases from the 34th in the world, which is 206 40 million US Dollars and accounts for 0.78% of the overall world trade volume, to the 2nd in the year 2009. Research result of Table 1 shows that foreign trade in China maintains rapid growth in the years 2001–2009 and reaches the maximum value of 2 561 630 million US Dollars in the year 2008. Trade balance of import and export gradually rises as the total amount increases (Fig. 1). And export always exceeds imports. At the same time, Fig. 2 illustrates the change trend of foreign export growth in the years 2001–2009. Result shows that except the years 2001, 2003, 2004, 2008 and 2009, increase of trade surplus in China in the years 2001–2009 has always been greater than the increase of import and export, but the range of variation is relatively unstable. In the

years 2002, 2003 and 2004, there are significant turning points; and in the year 2005, the increase reaches its maximum value. Moreover, total foreign trade has a similar shape of curve with import and export, which is smaller than the increase of trade surplus. However, affected by the financial crisis in September 2008, total export-import volume has reduced from 2 561 630 million US Dollars in the year 2008 to 2 207 270 million US Dollars in 2009, a decrease of 13.9%. At the same time, total volumes of import and export in the year 2009 have also decreased by 11.2% and 16.0%, respectively, compared with the same period last year. Although the maximum trade scale appears in the year 2008, the low external demand after September leads to the fall of total export-import volume. Trade surplus has reduced from 47.7% to 12.7% and fallen to –34.2% in the year 2009. Absolute difference of import and export is less than 200 billion US Dollars.

**Table 1** Total volumes of import and export in the years 2001–2009

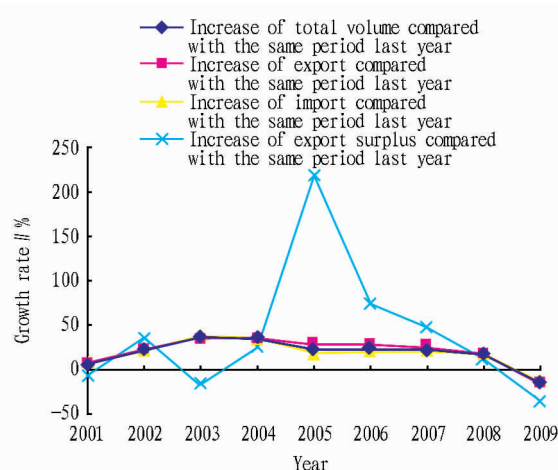
Year	Total export-import volume		Total volume of export		Total volume of import		Timport and export balance	
	Absolute value ×10 <sup>8</sup> US Dollars	Growth rate compared with the same period last year//%	Absolute value ×10 <sup>8</sup> US Dollars	Growth rate compared with the same period last year//%	Absolute value ×10 <sup>8</sup> US Dollars	Growth rate compared with the same period last year//%	Absolute value ×10 <sup>8</sup> US Dollars	Growth rate compared with the same period last year//%
2001	5 097.68	7.5	2 661.55	6.8	2 436.13	8.2	225.41	–6.5
2002	6 207.85	21.8	3 255.69	22.3	2 952.16	21.2	303.53	34.6
2003	8 512.10	37.1	4 383.70	34.6	4 128.40	39.9	255.40	–16.1
2004	11 547.40	35.7	5 933.60	35.4	5 613.80	36.0	319.80	25.6
2005	14 221.20	23.2	7 620.00	28.4	6 601.20	17.6	1 018.80	217.4
2006	17 606.90	23.8	9 690.80	27.2	7 916.10	20.0	1 774.70	74.0
2007	21 738.30	23.5	12 180.20	25.7	9 558.20	20.8	2 622.00	47.7
2008	25 616.30	17.8	14 285.50	17.2	11 330.90	18.5	2 954.60	12.7
2009	22 072.70	–13.9	12 016.60	–16.0	10 056.00	–11.2	1 960.60	–34.2

Note: Data are from the General Administration of Customs of the People's Republic of China.



**Fig. 1** Change trend of the total volume of import and export trade in China in the years 2001–2009

Research also indicates that compared with the trade scale in the year 2008, total volumes of both import and export decrease in the year 2009, which has some relations with the policy of boosting the economy by expanding domestic demand. Besides, expanding domestic demand affects the increase of import, since the consumption capacity is limited in the short term in a certain society. Expanding domestic demand improves the production capacity. But it turns into domestic de-



**Fig. 2** Change trend of the import and export increase in China in the years 2001–2009

mand due to the lack of external demand. Thus, import decreases. At the same time, expanding domestic demand may lead to inflation, dispute in exchange rate, concentration of hot money, change of trade ecology, destruction of trade balance,

difficulty and risk increase of trade industry in China, and friction aggravation in international trade. Therefore, it is necessary to solve the major problems of foreign trade under the macro environment of expanding domestic demand.

### 3 Major problems of foreign trade under the macro-environment of expanding domestic demand

**3.1 Reduction of import; increase of export cost** Expanding domestic demand means that dependence degree of economic growth on foreign trade reduces under the same total volume of export. Expanding domestic demand directly transfers the core channel of social products consumption into domestic market, inhibits the growth of total import, and even reduces the proportion of import in foreign trade. Once the import reduces, export increases due to the support of public policy and the recovery of foreign economy. Then, the imbalance of international payments will increase, and the gap between import and export will be widened. The expanding of trade surplus has become an import factor affecting the stable growth of economy at present, which aggravates the trade friction between China and main trading partners, increases the pressure on RMB appreciation, and brings along the problems of liquidity surplus in China. Besides, RMB appreciation improves the production cost and reduces the price competitive advantage of traditional trade products in China, which is unfavorable to the export.

**3.2 Reduction of export; recession of the scale of foreign trade** During a given period of time, fluctuation of social wealth maintains at a considerable amount of range according to the growth of scientific and technological level and the development and investment efficiencies of existing resources, such as land and labor force. In other words, the limited social output can not meet the needs of the expansion of both domestic market and foreign market in a short period of time. Therefore, export will decline, and there will be a recession of the scale of foreign trade, which finally affects the increase in the gross national product. At the same time, decrease of export leads to the reduction of foreign exchange reserves, the relative decline of international reserves, and the weakening of debt paying ability. Moreover, reduction of export affects the international market share of China in related fields and the economic benefit of foreign trade in China.

**3.3 Arousing inflation and trade protection** China has put forward the economic development strategy of expanding domestic demand during Asian financial crisis. Under the macro-economic situation of unstable overseas demand and poor domestic demand, it is very important to expand domestic demand. In May 2009, the State Council has made a significant adjustment of macro-control policies. Financial policy has changed from being "stable and steady" to "active". Advantage industries and new fields are given major support, and tariff adjustment is carried out in the foreign trade industry which are greatly affected by financial crisis, such as improving the export rebate rate for some products, adjusting export tariff for some products, and canceling the export tariff for steel, chemi-

cals and food. These measures not only support the sustainable development of foreign trade industry, but also is an effective approach to expand domestic demand. At the same time, traditional foreign trade in China is mainly focused in the industries of labor intensive and resource intensive. And policy subsidy and tariff means are implemented. Therefore, traditional foreign trade industry in China is very price-competitive in the international market.

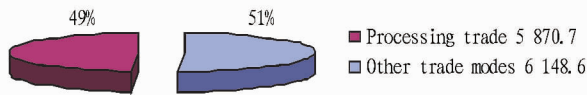
From an economic point of view, the active financial policy and loose monetary policy help to expand domestic demand. The former injects government investment, and the latter encourages the input of private capital. The two simultaneously expand the domestic market demand effectively. However, they also bring along the problem of surplus production, which can only be digested by domestic or foreign market. For a long time, economic development in China has relied on the stimulating effect of investment. Besides, supporting measures for people's livelihood are still not perfect, such as education, pension, housing and health care. Therefore, it is impossible to explore the potential of domestic market or to promote the domestic-demand economy in the short term. To promote the export, government provides export subsidy for enterprises and increases the price competitiveness for foreign trade enterprise, which leads to the anti-dumping and anti-subsidy investigation of other countries. For instance, in the year 2009, the United States implemented the special safeguard towards Chinese tyres, and the world's major trading countries criticized the trade policy of China. Table 2 and Fig. 3 show that processing trade accounts for nearly half of the proportion of export in China in the year 2009, which mainly belongs to labor-intensive enterprises. Once these processing-trade enterprises are impaired, export in China will be damaged, arousing problems in employment and benefits.

**Table 2 Value of export and proportion of processing trade in each moth of the year 2009**

Month	Value of export ×10 <sup>8</sup> US Dollars	Processing trade for export ×10 <sup>8</sup> US Dollars	Proportion of processing trade for export//%
January	904.5	387.0	42.8
February	648.9	345.9	53.3
March	902.9	436.2	48.3
April	919.3	437.1	47.5
May	887.6	424.7	47.8
June	954.1	471.1	49.3
July	1 054.2	508.3	48.2
August	1 037.1	505.4	48.7
September	1 159.4	570.1	49.2
October	1 107.6	571.0	51.6
November	1 136.5	580.6	51.1
December	1 307.2	633.3	48.4
Total	12 016.6	5 870.7	48.8

Note: Data are from the statistics of the Customs of the People's Republic of China.

From the domestic point of view, it is hard to make the best of the three, including exchange rate, interest rate and financial deficit. Taking expanding domestic demand as an example, an active financial policy will stimulate domestic de-



Note: Other trade modes include the general trade, the import and export goods in bonded warehouse, the warehouse and transit goods in bonded area.

**Fig. 3 Proportion of processing trade in the export value in the year 2009**

mand, increase financial deficit, reduce interest rate, and then improve exchange rate, and *vice versa*. At present, China implements the managed floating exchange rate regime based on market supply and demand. The global currency market is an economic subsystem, where a slight move in one part may affect the whole situation. Systemic evaluation on a strong defensive or expansionary monetary policy in a large economy is needed. After the financial crisis, interest rates all over the world have been kept at historic lows in order to stimulate economy, to reduce the risk of a double dip, and to realize recovery. China has adopted a loose monetary policy to encourage the domestic investment and consumption. Rapid pace of economic development heats up the inflation.

Inflation is closely related to trade. Inflationary pressure indicates that demand exceeds supply. Thus, export decreases. If import remains unchanged, trade deficit appears and there is

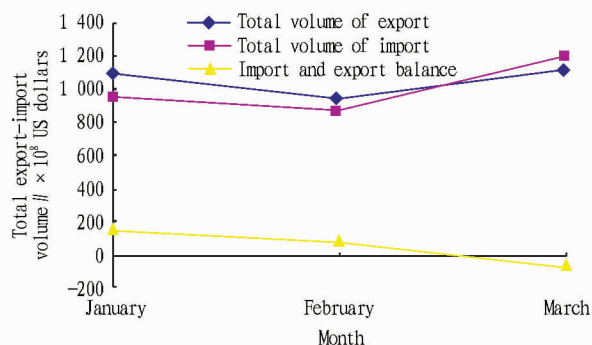
imbalance in the international payment. On the contrary, when domestic demand decreases, inflationary pressure reduces and export increases. To deal with the poor external demand and trade protectionism, exportable goods are sold in the domestic market and endogenous economic growth is achieved by expanding domestic demand. Thus, 4 trillion yuan is invested to stimulate consumption in China. However, the life mode and consumption idea in China are different from those of western developed countries. And it is hard to realize consumer-oriented model in the short term, which makes China difficult to get rid of the mode of investment-led development, and leads to inflation and trade deficit in China. At present, China is facing with the structural inflation. When aggregate demand and aggregate supply are in the state of equilibrium, economic structure change leads to the rise of general price level, causing price rise of other departments and forming the general price rise of the whole society.

In the field of foreign trade, China was in a surplus position before March 2010. But after March, China has been in a trade deficit (Table 3, Fig. 4 and Fig. 5). There are many reasons causing trade deficit. And expanding domestic demand is an important factor, which leads to inflation. At present, inflation in China is under the control of government. And the inflationary pressure at a low level is favorable to the treatment of trade balance issue.

**Table 3 Import and export statistics in the first quarter of the year 2010**

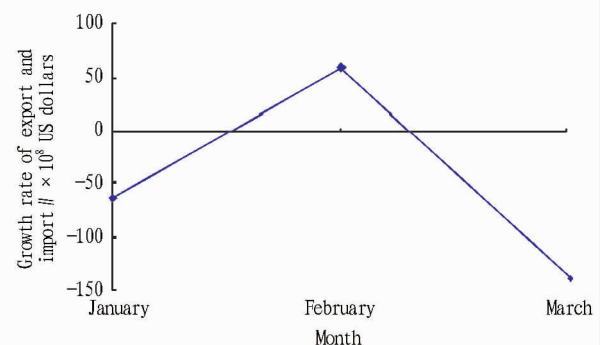
Month	Total export-import volume		Total volume of export		Total volume of import		Import and export balance	
	Absolute value $\times 10^8$ US Dollars	Growth rate compared with the same period last year//%	Absolute value $\times 10^8$ US Dollars	Growth rate compared with the same period last year//%	Absolute value $\times 10^8$ US Dollars	Growth rate compared with the same period last year//%	Absolute value $\times 10^8$ US Dollars	Growth rate compared with the same period last year//%
January	2 047.8	44.4	1 094.8	21.0	953.1	85.5	141.7	-63.8
February	1 814.3	45.2	945.2	45.7	869.1	44.7	76.1	58.5
March	2 314.6	42.8	1 121.1	24.3	1 193.5	66.0	-72.4	-139.0

Note: Data are from the Customs of the People's Republic of China.



**Fig. 4 Change of total export-import volume in China in the first quarter of the year 2010**

Besides, the improperly-implemented encouraging measures of government will not improve the international competitiveness and foreign economic benefits of foreign trade enterprises<sup>[2]</sup>, and will lead the over reliance on policy control and the reduction of innovation and efficiency. Therefore, how to deal with the relationship between government and market, as well as how to realize the transfer from import substitution to export



**Fig. 5 Change of export-import growth rate in China in the first quarter of the year 2010**

orientation, is a problem that China must be faced in the foreign trade activities at present.

**3.4 Attracting short-term hot money; increasing the risk of economic fluctuation** Expanding domestic demand requires the change of economic growth pattern from relying on investment and foreign trade to paying attention to consumption, expanding domestic demand, and vigorously developing

livelihood projects. Supply is increased due to more market demand, which improves the national income. Assuming that the proportion of consumption in national income maintains unchanged in an economic body in a certain period of time and area, scale of consumption increases as national income rises. Thus, import also increases. If export reduces and import remains unchanged in a certain period, trade deficit appears. In order to maintain the balance of international payments, it is necessary to reduce capital export and enhance capital import. Attracting capital inflow by high interest rate is the most effective way. Therefore, in order to maintain the equilibrium in balance of payments, interest rate should be changed according to the national income. Expanding domestic demand will inevitably bring along high interest rate. But high interest rate is a barrier to the domestic capital, makes foreign trade enterprise be challenged by hot money, and affects the autonomy of the upgrading of foreign trade enterprise and the policy of adjustment of foreign trade.

When economic body improves the interest rate in order to stimulate domestic demand, pressure of RMB appreciation becomes even greater. Moreover, high interest rate attracts the influx of hot money. Influence of hot money on economic operation is reflected in the inconsistency between the index of livelihood and the inflation, interest rate, and nominal GDP. Since the value of RMB is enhanced, short-term investment of overseas hot money stimulates the demand of RMB in circulation market, accelerating the circulation speed of RMB in market. At present, China strictly supervises the mechanism of additional RMB, and the influx of hot money can only enhance the value of RMB, which is not equivalent to the value of gold, but is an expectation of RMB appreciation brought by the improper speculation of financial market and the speculation of currency. At the same time, when domestic demand is stimulated, import is inhibited. Foreign trade of economic body is prone to have significant trade surplus and the surplus even enlarges in a period of time due to policy and time lag factors if export growth rate is equal to, or greater than, the decrease rate of import. Under the mask of the adjusting international payments and safeguarding the interests of national industries, some countries ask China to raise the value of RMB, which seriously affects the currency stability of RMB and the order of financial market. Therefore, Chinese government should unswervingly defend the economic sovereignty and the currency stability of RMB. At present, appreciation of the RMB is more harmful than helpful.

Speculation of foreign hot money has always been a problem for Asian emerging countries during their transformation of economic system and their development process. Jacking up price increases the economic bubble. Taking China as an example, a large number of foreign capitals improves the prices of real estate and the products of daily necessities, enlarges the industrial scale, and increases the total economy. However, in fact, these foreign capitals force prices up, such as the apartment, energy, steel, cement and other traditional industries, and enhance the living cost of residents. Moreover, there is little increase in wages, which has not kept the pace of cost index. In theory, impure behavior of speculative currency reserve of overseas hot money is an important factor causing in-

flation. And inflation usually enhances the expectation of labor force to increase wages, and leads to the improvement of production costs. Since the price of production raw material is under control, price rise of labor force makes small and medium enterprises overwhelmed. Therefore, the energy-based and labor-intensive enterprises have to extend working hours in order to save money, and to maintain the normal operation of enterprises. The harsh trading environment at the end of trade chain can not help Chinese enterprises to keep the accumulation of original capital. On the contrary, it aggravates the unreasonable old trade order. At the same time, foreign trade enterprises lacking abundant capital and advanced technology and management mode can not achieve the resource consolidation and structure upgrading of the whole foreign trade industry through innovation and transformation, which directly affects the independence of state trade planning and policy making, as well as the possibility of implementation. Once hot money controls the market price of resources through a legal means, economic authorities can not effectively promote the coordination and upgrading of industrial resources, and have to allow the hot money to change the price at will.

## 4 Countermeasures and suggestions

In view of the above questions, government should enhance the implementation of macro-economic policy, and prevent the risks in foreign trade.

**4.1 Actively coping with the RMB appreciation; effectively improving the anti-risk ability of RMB; firmly safeguarding the stability of RMB; reducing the frictions in international trade** According to the external environment and domestic situation, RMB appreciation has its inevitability in appreciation pressure and expectation. In fact, RMB appreciation is the key to the stability and continuity of economic development. And it can be achieved under the premise of export stability and economic development, which will not materially affect the export work in China. Once domestic demand meets a substantial turning point and foreign trade enterprises achieve successful transformation, pressure on RMB appreciation will be reduced.

Besides, relationship between RMB appreciation and trade friction should be treated carefully. Although stable exchange rate of RMB has greatly promoted the export, China is facing greater appreciation pressure and trade barrier due to trade frictions and trade protectionism. Further deterioration of international trade environment makes export of China become even harder. And it is necessary to find out the proper control degree. If necessary, small but steady RMB appreciation can be allowed under the condition that RMB appreciation is smaller than the incremental rate of export. At the same time, utilization rate of foreign exchange reserves should be effectively improved in order to expand import, minimize foreign trade surplus, and deal with trade frictions. For instance, in recent years, commercial large-scale purchase led by the government has been expanding, especially the import of high value-added products from developed countries, which can not only be used in research, but also reduces the imbalance in the trade. In general, the managed floating exchange rate system based on market demand and supply can not be changed, which is the

core to safeguard the stable RMB and domestic financial security, to ensure the people's living standards, and to expand the domestic demand.

#### **4.2 Transforming the growth model of foreign trade; promoting industrial upgrading of foreign trade; enhancing the trade efficiency; forming an effective price competition mechanism**

When advocating the domestic consumption, import of China will be affected. Export scale is easily reduced when productivity is stable, causing the decrease of foreign exchange reserve and the job opportunity. Primary export product and processing product can not be easily replaced and their elastic demand is relatively great, which are not predominant in export. Therefore, it is necessary to adjust foreign trade strategy, to change the development mode of foreign trade, to turn the focal point of the foreign trade development from improving development speed and scale into enhancing the benefit and quality of foreign trade growth, to accelerate the resource consolidation of both domestic and foreign markets, and to implement the "diversification strategy of export market", the "strategy of success through quality", and the "strategy of promoting export by technology". Moreover, we should explore new market based on traditional market, promote the trade prosperity and enriching of people, change the pressure of expanding domestic demand on foreign trade into a power, improve the contribution rate of technology innovation and management innovation to the quality of foreign trade industry, inconceivably extend in the value-added chain of trade products, promote the export of products with high value content, achieve a higher level of international division of labor, improve the efficiency of foreign trade enterprises, and establish a price competition mechanism for foreign trade products.

#### **4.3 Giving more finance support for trade; improving the environment for trade development; correctly handling the relationship between the government and foreign trade enterprises; actively responding to the anti-dumping and anti-subsidies investigation**

Foreign trade in future should focus on supporting the development of general trade, set up a logistics distribution platform connecting China and foreign countries, improve the living environment of foreign trade and the financing environment of medium and small-sized enterprises, increase the financial and insurance services, and help foreign trade enterprises to go abroad and to attract foreign capitals. Related departments should make reasonable export tax refund policy on foreign trade, and improve the customs duty collection system, such as maintaining the proportion of export rebates in national financial revenue at the level of 8.5% – 9.5%, which is less than the level of 10%<sup>[3]</sup>. Moreover, related departments should encourage the development of processing trade, help it to expand the home market, strengthen their ability to withstand the risks in foreign markets, and foster the domestic industries with competitive advantage at abroad<sup>[3]</sup>. Government should correctly handle the relationship among foreign trade enterprises, guide them in the aspects of development strategy and industrial transformation, and not to excessively intervene the trading activities of enterprises. At the same time, government should integrate the foreign trade strategy into expanding domestic demand and stimulating consump-

tion, encourage enterprises to produce in order to meet domestic demand, and actively deal with the trade protectionism, anti-dumping and anti-subsidies investigation, and use the WTO rules to protect the legitimate interests.

#### **4.4 Controlling inflation; curbing the speculation of hot money**

Firstly, issuing currency when supply and demand are inconsistent usually leads to inflation. Consumer Price Index (CPI) is usually used to evaluate the rate of inflation. CPI has increased from less than 2% before the year 2006 to 5.9% in the year 2008. According to the rules in economics, normal value of inflation is 4% – 4.5%. And in the year 2009, there is a trend of inflation in China. No inflation does not represent that there is no necessary to carry out the management of inflation expectation. Firstly, malicious speculation of inflation expectation should be curbed, in order to avoid the speculation, which might increase the economic uncertainties, damage the interests of the majority, lead to the cost rise of enterprises, and affect the benefits of export industry. Secondly, government should change the imbalance in exchange rate and control the total money supply<sup>[4]</sup>, adjust the credit policy, reduce the lending volume of currency, offer more preferential policies for foreign trade enterprises, and make up for the loss during inflation. Secondly, government should strictly monitor the flow of hot money, establish the investment barriers to entry and the exit mechanism, and solve the problems of excess liquidity in market. Particular attention should be paid in the centralized speculation in capital and real estate market, as well as some special products and manufacturing industries, which leads to the great fluctuation in price<sup>[5]</sup>. Cost improvement of foreign trade enterprises should be avoided, such as the improvement of labor force and the means of production. Fourthly, government should increase the subsidy in foreign trade industry, cover the unrealistically high cost due to inflation, and keep the subsidy at the level before inflation in order to avoid the anti-dumping and anti-subsidies investigation. It is worth notice that China should carefully treat with the negative effects brought about by anti-inflation measures when implementing the macro-control policy, such as the increase of the unemployment and the reduction of output. Policy for public management should be implemented, and the emergency mechanism should be made.

Speculative short-term capital has the characteristics of concealed prophase and catastrophical release, which may be a fatal blow to both national economy and financial security. Therefore, it is very important to improve the supervision of hot money. Government should adhere to the management of capital account, monitor the access path of hot money, slow down the escape rate of foreign currency after arbitrage, and steadily advance the market formation mechanism of RMB exchange rate. Secondly, government should supervise the direction of large capital flows, set up a security mechanism for the capital access of foreign trade industry, prevent the control of foreign trade by overseas hot money or domestic speculative capital, implement short-term administrative intervention or promulgate laws about speculative capital if necessary, supervise the flow of cross-border capital to stop the inflow of hot money, and guide the hot money to play a positive function.

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