BOARDS OF GOVERNORS ● 1998 ANNUAL MEETINGS ● WASHINGTON, D.C.

INTERNATIONAL MONETARY FUND
WORLD BANK GROUP
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL FINANCE CORPORATION
INTERNATIONAL DEVELOPMENT ASSOCIATION
INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
MULTILATERAL INVESTMENT GUARANTEE AGENCY

J

Press Release No. 14
October 6 - 8, 1998

Statement by the Hon. **DAI XIANGLONG**,
Governor of the Bank for the **PEOPLE'S REPUBLIC OF CHINA,**
at the Joint Annual Discussion

Statement by Mr. Dai Xianglong
Governor of the People's Bank of China
at the 1998 Annual Meeting of the International Monetary Fund
and the World Bank

Washington, D.C., October 6, 1998

Distinguished Chairman, Ladies and Gentlemen

This Annual Meeting is conducted at a most critical moment when the global economy and financial markets are facing enormous challenges which could affect world economic growth and financial development. In many crisis-hit countries in Asia, while they are making progress in economic adjustments, the severe economic recessions experienced by these countries have, unfortunately, been far beyond our initial expectations. The recent Russian crisis has aggravated the turbulence in global financial markets, and Latin America is now also under financial strain. These financial crises, and the economic depression in some developed countries, are increasingly affecting North America and Europe. A global recession threatens. We must take the opportunity of this meeting to call on concerted actions to stem the crisis from further enlarging or spreading, and to assist the affected countries in reviving their economies. It should be the top priority of this meeting to consider how to strengthen the architecture of the international monetary system to effectively prevent and solve financial crises.

It is our view that the main cause of the crisis is that international cooperation and the evolution of the international financial system lag far behind the economic globalization and financial integration process, and the speed of their liberalization exceeded the pace of enhancing the economic management abilities of the crisis-hit countries. Since the early 1990s, the faster pace of globalization has led to substantially increased capital flows which have been beneficial to the world economy. Nevertheless, more and more capital flows and foreign exchange transactions have become dissociated from production and trade activities. Speculators with huge sums of capital are able to take large leveraged positions to control and manipulate markets for profit, accentuating market volatility. However, the international community has not come to a consensus on effective mechanisms for the monitoring and containment of risks brought about by volatile capital flows. As the developed countries push forward the liberalization of trade and capital flows, they aim at achieving a superior position in the world capital markets for themselves, thus failing to consider the impact of premature liberalization on the economic security and social stability of the countries concerned.

Capital account convertibility should be carried out in an orderly and well sequenced manner. The member countries are entitled to determine measures to manage capital flows in consideration of their specific circumstances and stages of economic development. China's experience with foreign exchange management system reform has shown that if a country lacks the conditions for full convertibility while still in need of capital inflows, it can keep foreign debts at a reasonable size with well-structured maturities through appropriate foreign exchange management. This practice not only can sustain economic development but also protect foreign investors' interests by reducing financial risks.

The major industrial countries should take primary responsibility for maintaining the stability of the international financial system and the steady growth of the world economy. Under the current circumstances, the fiscal and monetary policy stance of the major industrial countries should be conducive to maintaining world economic growth. They should strengthen the coordination of interest rate and exchange rate policies to stabilize international financial markets. In addition, they should significantly increase their financial assistance to crisis-affected countries, expand their imports from those countries, and guard against trade protectionism. At the same time, those huge speculative funds should be well regulated by the authorities. The involvement of the private sector in preventing and resolving financial crises is necessary. International financial institutions and developed countries should encourage and support the private sector debt restructuring until debt relief is attained. It is our firm belief that by strengthening coordination and mutual support within the Asian region, the economic and financial development in Asia is bound to stabilize gradually.

The Fund and the Bank have made great efforts in preventing and solving financial crises in some regions and countries, maintaining the stability of the international monetary system, and assisting member countries to develop in a sustainable manner. We hope that the Fund and other international financial institutions can play a more effective role in resolving financial crises. By encouraging the deregulation and liberalization of domestic markets, they should be vigilant to the risks posed by international capital flows; and when designing and implementing assistance programs, they should pay more attention to the specific circumstances of the countries concerned. The Fund should formulate and establish a mechanism for monitoring short-term capital flows, and the movements of speculative capital. We support the strengthening of the Fund's early warning system on the basis of enhanced information disclosure and transparency. We hope that the Eleventh General Quota increase and the NAB can take effect as soon as possible. We think that, if necessary, the GAB should be reactivated. We continue to support the implementation of ESAF programs and the HIPC Initiative.

In the face of the Asian crisis and the turbulence in international financial markets, the Chinese Government has taken a highly responsible stance.

First, China has sustained its rapid economic growth. Against the backdrop of a substantial slowdown of exports to some Asian countries and the severe flooding, we have adopted a vigorous fiscal policy and increased money supply appropriately to expand infrastructure investment. We are confident that the annual growth rate in 1998 will reach 8 percent.

Secondly, China has maintained the stability of the RMB exchange rate. Since the foreign exchange system reform in 1994, China has adopted a managed floating exchange rate regime. We have provided financial assistance to crisis-stricken countries through IMF programs and bilateral arrangements since the eruption of the Asian crisis. In the interests of regional stability and growth, we have maintained the stability of RMB and pursued a non-devaluation policy. Although the pressures and risks are still increasing, there remains a solid ground for the stability of the RMB.

Thirdly, China has taken measures to expedite structural reforms and to prevent and reduce financial risks. The Chinese Government has resolutely pressed ahead with the administrative structural reform, and successfully achieved the target of retrenching 50 percent of employees in the ministries of the State Council. The state-owned enterprise reform is proceeding progressively as planned. Breakthroughs have been achieved in financial reform. The provincial branches of the central bank will be phased out and a number of inter-provincial branches will be set up by the end of this year, with the aim of increasing the central bank's independence in carrying out its functions. The Ministry of Finance has issued Special State Bonds of RMB270 billion and the funds raised have been used to recapitalize the state-owned commercial banks. An internationally accepted loan classification system is being implemented throughout the country. The central bank has shut down some small and medium-sized financial institutions that had been noncompliant or insolvent. China's financial industry has been developing steadily in the process of reform.

It has been 15 months since Hong Kong returned to China. Over the period, the Hong Kong Special Administrative Region (SAR) authorities have made great efforts in facilitating the economic adjustment and maintaining the prosperity in Hong Kong SAR. Facing the challenges posed by the East Asian financial crisis, the Hong Kong SAR Government has successfully maintained the stability of the financial markets. According to the principles of one country, two systems and Hong Kong people ruling Hong Kong, high degree of autonomy, the central government of China supports the Hong Kong SAR's efforts in maintaining the prosperity and stability of Hong Kong and their measures to safeguard the linked exchange rate regime.

Lastly, on the Bank's pricing policy, it is highly regrettable that at a time of substantial reductions in capital inflows to developing countries, the Bank management has increased the price of IBRD loans against the will of all borrowing members. This departs from the Bank's long-standing principle of pricing loans according to the development purpose, thus sending the wrong signal to international capital markets, harming its good relations with borrowing members, and eventually hurting its own reputation. We urge that the Bank management take measures to offset the negative effects caused by the price increase.

To conclude, I believe that the international community is able to cope with the challenges in the process of globalization and that the crisis-hit regions and countries will overcome the temporary difficulties they now face and achieve a solid and sustainable growth.

I look forward to the constructive fruits of this meeting.

Thank you.