Board Meeting of May 28, 1998
Statement by Juan L. Cariaga

China - Country Assistance Strategy - Progress Report

Introduction

This report on implementation of the Country Assistance Strategy (CAS) for China is welcome and we appreciate staff's detailed presentation of progress made as well as of the continuing challenges to the country's efforts at poverty alleviation and development.

We note the results of the 15th Party Congress in September 1997 and the election of a new government in March 1998, which have renewed and expanded support for continued domestic reforms and international integration. These efforts are of great importance, not only for China but also for regional and world economic development, because poverty reduction directly affects the fate of millions of persons in China and elsewhere, and the country's efforts raise a number of issues that are important for the Bank. Success in the world's most populous country will have implications beyond China's borders. As such, we welcome the willingness of the Chinese government to accelerate the pace of reform in order to prevent a weakening of economic growth.

Overall, we are pleased that the Country Assistance Strategy appears to be successful, as described in this progress report, and it receives our continued support. However, there are a number of issues raised by this progress report and we would like to offer some brief comments and questions.

CAS Progress Report and Economic Considerations

The performance of the Chinese economy during the last two decades has been remarkable. This is reflected in the 1997 figures showing 8.8% GDP growth, with inflation held to 2.7%, in spite of the effects of the East Asia crisis. As a result of such sustained progress approximately 200 million people have been taken out of absolute poverty. We would like to commend Authorities for this remarkable achievement.
Nevertheless, around 270 million people still live on less than $1 per day, indicating that the reform process also needs to be maintained and deepened. Moreover, as the progress report notes, China’s successful rapid growth and structural changes have created new challenges, as well as opportunities. Problems include employment insecurity; growing inequalities; remaining poverty and environmental concerns; and macroeconomic problems.

The Bank strategy, to support the major changes underway as China continues to move from a command to market-based economy and from a rural to urban society, appears appropriate. This includes support for macroeconomic growth and structural reform; infrastructure development, human development and poverty reduction; agricultural and rural development; and protecting the environment. We find this to be a reasonable approach to the overall issue of how best to pursue poverty reduction.

In spite of numerous successes, the magnitude of the challenges remains great. The government, for example, is planning to reduce public sector employees by 30-50% over the next three years. While we agree that this is appropriate for governance and public sector reform, we wonder if this may not be too ambitious, given expected large layoffs in the State-Owned Enterprises (SOEs) also. Is the labor market sufficiently flexible to reinsert or absorb this number of potential unemployed? We would appreciate staff comments on plans to reincorporate laid off workers into the private sector.

At the same time, acceleration of the privatization process could be of crucial importance in absorbing potential unemployed. Moreover, if foreign direct investment from traditional sources declines, as is possible, the acceleration of the privatization process seems to be even more important to the maintenance of high rates of economic growth. Can Staff comment on whether a capitalization process, as a form of privatization, has ever been considered by Chinese Authorities?

Agricultural reform and privatization were important components of earlier economic growth in China. Agriculture and rural development remain an integral part of the Bank’s strategy for development. Nevertheless, we note that the focus now appears to be on “maintaining agricultural growth while moving labor out of agriculture...” and wonder if the Bank should not be giving some additional consideration to projects that would slow rural migration as well as increase food security, as an issue. We would appreciate staff addressing this question.

World Bank Group Activities

We are pleased to see in China that EDI, FIAS, IFC and MIGA are all active and encourage this trend to continue. Of particular interest is IFC’s first restructuring project involving a Chinese SOE and a European firm. This is an area that may offer many additional opportunities, in view of the major changes that are expected in the larger SOE’s as well as the 300,000 small and medium enterprises expected to be privatized.
Lending Volume and Bank Exposure

As has been noted, if current trends continue, China is expected to become the Bank’s largest exposure in the near future. The progress report highlights some implications for the allocation of future net income. In our opinion, however, future lending should be in accord with the country’s development needs as well as the Bank’s capacity to build the required level of capital and reserves. As such, we concur with management proposal for further study of this question before the next full CAS.

Finally, we welcome the progress shown by this report, endorse continued Bank support for China’s development programs as outlined in this progress report, and wish the government continued success in their implementation.