



1. Project Data:		Date Posted : 06/30/2003	
PROJ ID: P003623		Appraisal	Actual
Project Name: Financial Sector TA	Project Costs (US\$M)	65.48	65.84
Country: China	Loan/Credit (US\$M)	60	60
Sector(s): Board: FSP - Payment systems securities clearance and settleme (68%), Banking (27%), Central government administration (5%)	Cofinancing (US\$M)	5.49	5.49
L/C Number: C2423; L4574			
	Board Approval (FY)		92
Partners involved : Japanese Grant Facility, Government of China	Closing Date	09/30/1999	09/30/2002
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2. Project Objectives and Components

a. Objectives

The move to a market economy in 1978 was followed by a decade of very rapid economic growth when the FSTA project was conceived, The Soviet-based accounting system allowed banks to show profits although they had high non-performing loans, and the paper based manual payments system resulted in inter -province transfers taking two weeks on average.

The FSTA project was to help create needed financial system infrastructure in selected areas : the execution of monetary policy, prudential supervision of banks, accounting and financial reporting, government debt management, and modern payments systems. The ICR groups these in four clusters:

(1) Central Bank (Peoples Bank of China or PBC) functions. Specifically to (i) develop prudential regulation and supervision focussing on risk appraisal and management; (ii) develop open market operations and forecast short term reserve money; (iii) strengthen research and statistics; (iv) improve central and commercial bank laws; (v) better automate PBC's head office; (vi) improve the content of the training that PBC provided its staff .

(2) Accounting framework. Specifically, to (i) help draft 28-30 general accounting standards, chart of accounts and financial reporting formats; (ii) draft accounting standards for PBC and the banks, and prepare an action plan to implement them; (iii) organizational study of PBC head office and selected branches, especially its accounting department; (iv) implement a management information system in PBC head office and prepare an accounting manual and chart of accounts; (v) draft auditing standards and manual; (vi) train staff of three agencies through workshops and study tours.

(3) Government Debt Market. To (a) improve the procedures of issuing debt instruments; (b) develop Treasury cash management capabilities; (c) develop open market operations; (d) develop a book entry system for government securities.

During implementation and following the East Asian crisis in 1997, these objectives were modified to improve various features of the government bond market to lower the cost of government borrowings and risk .

(4) National payments system. To design and implement a national payment, clearance and settlement mechanism .

b. Components

The project had more than a dozen components, but over two thirds of the funds were to create the payments system. The smaller components included measures to improve supervision and regulation, accounting and such related issues.

c. Comments on Project Cost, Financing and Dates

The ICR notes that some of the project objectives (e.g. reorganization of the PBC and its supervision functions) were unattainable in a large country like China in three years . The project was extended three times, for a total extension of three years, and a supplemental loan of \$ 8 million was made to allow Government to complete the contract on the payment system and to complete the component on Government debt market . The project was expected to be followed by others (that did not materialize).

3. Achievement of Relevant Objectives:

The national payments system, the main focus of the project, was successfully implemented based on two complex subsystems (real time inter-bank transactions and the central gross settlement system). When the project began, none of the five participating (state-owned) banks had a system wide communication network, although this was being planned. While the system was well designed for the needs at the time, China's extremely rapid growth changed the requirements. In retrospect, a more flexible implementation arrangement may have been better. The objectives in the three other clusters were largely attained in a narrow sense (e.g. developing accounting standards), but the larger goals of using them to improve the financial system's soundness is still elusive. Although the project did not emphasize supervision and regulation, the minor component that was included improved the risk based loan classification system. The ICR rates the small office automation component as cost effective and satisfactory; but most of the accounting standards have not been implemented. Most importantly, the OED evaluation of the Bank's overall activities in the banking system finds that banks continue to be unsound although they have grown spectacularly; so although the project may have made small improvements, the overall goal of a sound banking system has not been attained (although that may have required more than this single project).

4. Significant Outcomes/Impacts:

While some of the specific objectives appear to have achieved, the larger goal of the project which was to help develop a sound financial system for China was not. This project could not, of course, achieve this larger goal by itself; but it was to be the first of a series of Bank operations. These other Bank operations were delayed during their preparation and were finally cancelled, and the FSTA project continued. The selected areas improved, and while the banks grew tremendously in size, they remain unsound.

5. Significant Shortcomings (including non-compliance with safeguard policies):

The ICR notes that providing technical assistance through study tours was ineffective, but does not mention that they were included largely to ensure the cooperation of counterparts. While 16 of the planned 30 accounting standards have been issued, they have not yet been adopted. Unlisted state owned banks continue to use the old standards, some ten years after the project was approved. There are, however, significant differences between the standards issued, and international accounting standards that the MoF favors. The PBC has adopted the prudential regulations on a selective basis and then adapted them to the Chinese situation, and the regulations are not entirely consistent with each other.

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
Outcome:	Satisfactory	Moderately Satisfactory	The main component to improve payments achieved its objectives, although the ICR says that China's needs had changed substantially in the meantime. The other objectives (e.g. having banks adopt better accounting) were not substantially met.
Institutional Dev.:	Substantial	Modest	The PBC's abilities and authority has improved modestly, but improvements in other institutions (e.g. setting accounting standards, audits etc.) were even less impressive.
Sustainability:	Likely	Non-evaluable	It is difficult to evaluate whether the project's modest achievements will be sustained.
Bank Performance:	Satisfactory	Satisfactory	
Borrower Perf.:	Satisfactory	Satisfactory	
Quality of ICR:		Satisfactory	

NOTE: ICR rating values flagged with '*' don't comply with OP/BP 13.55, but are listed for completeness.

7. Lessons of Broad Applicability:

1. Technical assistance to improve one institution, like the central bank, has limited effectiveness when the institution's *de facto* (not *de jure*) role in the system is not established. Laws or the technical improvements themselves cannot establish this role.

8. Assessment Recommended? Yes No

9. Comments on Quality of ICR:

The ICR describes the various components of the project in detail with all the difficulties encountered. It could have elaborated on some of the points. For example, prudential supervision was carried out on assets of several banks, but it doesn't mention whether the scope was what had been planned at appraisal and, more importantly, whether in the seven years that have elapsed since the exercise was completed in 1996, prudential supervision has expanded

to more than one bank and selected branches of other banks and if so, to what proportion of the system? And if it has expanded to any significant portion of the banking system, what is done with the findings of the supervision? The ICR is also vague about specific changes to MoF's management of bond markets; it mentions changes, but nothing specific. Given that the project was extended three times specifically to allow completion of this component (and the payments system), it could have been more explicit about what was accomplished under the component and what the results have been .

Furthermore, it would have been difficult for an evaluator to judge the project's relevance and role in the Bank's overall assistance to China based on this ICR alone; but the discussions conducted during the Country Assistance Evaluation greatly helped .

At the risk of further lengthening the report, the ICR could have provided the context of the project better especially since this was the only Bank loan to China for the financial sector during the decade (and the largest TA loan in the Bank).