Board Meeting of May 28, 1998
Statement by Matthias Meyer

CHINA – Country Assistance Strategy – Progress Report

Our chair endorses the CAS Progress Report for China as we find it to be very informative and comprehensive. This well-written report reflects in a concise manner the actual situation in China and the most recent events, as well as the challenges the country is facing. Having said this, we have some comments on the discussed program:

• **Financial Sector Fragility.** It has been recognized, particularly in the wake of the recent events in South East Asian countries, that the reform of the financial sector is a crucial part of the economic restructuring process. In this respect we regret that China has made only slow progress in opening up this sector to foreign financial institutions. Foreign competition would contribute to a more efficient restructuring of the domestic financial institutions as well as to the inflow of foreign banking techniques and know-how. In this regard, we expect a stronger Bank response to this crucial issue in the next full-fledged CAS for China.

• **Environmental Issues.** We welcome the upgrading of the National Environment Protection Agency to a ministry and hope that this will add some weight when environmental concerns have to be defended against economic growth aspects. In reality, up to now the industrial development has been favored over environmental protection in China, which is of serious concern for the future. Unfortunately, the CAS progress report remains rather vague on environmental issues as well as on the response to the WB’s operational support in this field. The Bank was more explicit in earlier CAS reports, especially with regard to urban environmental questions. We would therefore be interested in hearing more about the political will in China to engage in environmental protection, the corresponding law enforcement, and the way the WB assistance contributes effectively to the reconciliation between economic growth and sound environmental management. These questions become even more urgent when considering the pressure to sustain high economic growth in order to absorb the large-scale lay-offs created by the state-owned enterprise reform, and thus maintain social stability.

• **Reduction of Poverty.** Poverty in China decreased substantially since economic reforms began in 1978. However, the WB revised the official Government of China figure and gives a bleaker picture of poverty:
270 million people living with an income of less than a dollar a day. Although poverty is mainly rural, urban poverty appears also to be emerging. Targeted measures to combat poverty will be essential. This is all the more preoccupying since IDA lending, which gave support to health and education in poor areas, will stop after FY99. This implies that other financial sources will have to be found. Future perspectives for WB lending in this regard will need to be dealt with in the next year’s full CAS.

- **Regional Development Disparities.** In contrast to the previous CAS report, the regional disparities between the interior (mostly upland regions of central and western China) and the coastal provinces are not given a high profile. We feel that this issue continues to be extremely important for China and therefore ask Management to inform us about IBRD’s assistance to the poorer provinces and the effectiveness of this assistance.

- **Fiscal Reform.** The regional disparities also reinforce the urgency to introduce fiscal reform shifting public expenditures (health, education, infrastructure) towards provincial and local governments. The progress report states that reforms, which have been announced recently by the new Government even exacerbate regional inequalities. In this context how does Management assess the capacity of Chinese authorities at all levels to finance these public programs?