When the Board reviewed the China CAS report in March of 1997, this chair expressed a highly positive assessment of the economic developments in the country. This observation remains fully valid. We believe that the tremendous progress which has transformed China is of truly global importance. Recent political developments have strengthened support for reform and significantly widened their front. The authorities have embarked upon an ambitious program which must increase responsiveness of the Chinese economy to market signals, solidify its institutional framework, and make growth lasting and sustainable.

This program sounds very reassuring now, in the aftermath of economic crisis in some countries of the region. It must be pointed out in this respect that the major feature of this crisis is its selectivity – it is only some economies that are severely affected. The very fact that the current CAS forecasts for China envision only marginally lower growth rates relative to last year’s projections, and that exports are expected to grow – after dramatic 27 percent increase in 1997 – solidly in a range of 6 to 8 percent annually up to 2000, makes us believe in a bright future for the country.

It is obvious, however, that repercussions of the Asian crisis should trigger a more thorough reconsideration of the Chinese economic framework in order to capitalize on its strongest aspects and identify its weaknesses. It is clear, from this point of view, that overhaul of the banking system must be given priority in the authorities’ agenda, and this issue inevitably leads to a necessity to make large SOEs financially transparent and accountable. Fortunately, these SOEs’ share in the overall economy is not as great as in the transition economies of East Europe and former USSR, thus this reform should entail much less trouble in terms of plummeting incomes and social discontent.

Nevertheless, the mere fact that it was deemed necessary to inject as much as $32.5 bln worth of new capital in state banks reveals the seriousness of the problem. The paper correctly points to the fact that at least some of these SOEs tend to be located in areas where substitute employment is not easily found. Moreover, as the urban population is getting accustomed to new living standards, it may be expected that laid-off workers will express their grievances in a
more vocal way. The only realistic means to successfully accommodate this redundant labor force is to give more leeway to the economic initiative on the ground level. To this end, economic activity (including financial intermediation) ought to be further deregulated, government machinery ought to be streamlined, and the state ought to concentrate its creative efforts in the infrastructure and social sectors. We understand that these views are shared by the Chinese authorities.

Thus, we concur with the presented opinion about the list of areas where Bank's assistance is expected to be particularly helpful, i.e., structural reform, urban development, and poverty and rural issues. We very much appreciate the quite enviable track record of project management, correctly attributed to the strong Government ownership and local implementation capacity. While it is true that our moving to the inland areas may somewhat complicate project implementation, it would be interesting to hear from the staff whether we participate in the process of channeling knowledge from those in China who are already familiar with the Bank's practices and requirements to those who are still in need to acquire it.

We understand concerns about the cessation of IDA financing of poverty-related projects in China. The staff offers somewhat vague thoughts about this issue; it would be welcome if we were given more detailed analysis of the feasible ways to address this problem. For example, one of the ways to deal with the issues of regional backwardness seems to be to emphasize transport infrastructure development in order to make these regions more accessible to broad trade flows.

It is very interesting to learn that the Chinese authorities are now contemplating some reforms which are typical to a very mature stage of economic transformation, e.g., housing divestiture and multi-pillar pension reform. As far as the former is concerned, we strongly support introduction of market principles in the area of urban real estate which should ultimately lead to rationalization of its use and channel private demand into relevant investment. As for the latter, the authorities might be advised to act cautiously in order to avoid widespread proliferation of unfunded pecuniary entitlements. We all know that such entitlements are rather easy to introduce and very hard to reform when the social redistribution programs mature, particularly in view of changing demographic profile of the society. It would be interesting to know staff opinion about this.

With these remarks, we would like to reiterate our support of the Chinese reforms. It is the clearest case of targeted assistance by the World Bank group which has brought about tangible and highly welcome effects in terms of poverty reduction and economic growth.