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**Statement by Mr. Jin, Mr. Zhang, Mr. Bai, Ms. Zhao, and Mr. Law on World Economic Outlook; Global Financial Stability Report; Fiscal Monitor
(Preliminary)
Executive Board Meeting 21/31
March 25, 2021**

We thank staff for the set of flagship reports and broadly agree with staff's assessment of the global economy and risks.

World Economic Outlook (WEO)

COVID-19 has been an unprecedented shock to the global economy. From the second half of 2020, global recovery has been gaining momentum; however, the near-term economic outlook is still fraught with substantial uncertainties, and downside risks remain sizeable. Future containment of the pandemic depends on vaccine distribution. The pace of vaccination in most Emerging Markets and Developing Countries (EMDCs) is lagging, and many low-income countries (LICs) are facing severe fiscal constraints for vaccine procurement. Against this backdrop, we should prevent “vaccine nationalism,” and promote a cooperative, balanced, and inclusive vaccination and recognition process across countries in order to achieve a more synchronized global recovery.

Based on the baseline projection in the latest WEO, the pace of recovery in advanced economies (AEs) is picking up more rapidly than most EMDCs, and in the medium term, AEs losses are expected to be much lower than in EMDCs. Therefore, it is highly possible that the withdrawal of supportive policies in AEs is earlier than in EMDCs. History shows that when the Fed tightens its monetary policy, international capital will flow back to the US and the dollar will appreciate. This would pose significant spillovers to the EMDCs, through channels including capital flow reversals and FX markets. As observed by staff in the GFSR (more discussion below), EMDCs face daunting challenges given their large external financing needs, and signals of any change of monetary stances by AEs can quickly reverse market sentiment and lead to sharp adjustments in markets. Moreover, many EMDCs face preexisting challenges such as less developed financial markets, large foreign currency debts,

and foreign currency mismatch on their balance sheet. As such, sharp currency depreciation and capital outflow may trigger financial instability in these countries. Therefore, we welcome the IMF to closely monitor potential spillovers from policy changes in major AEs to EMDCs. The Fund also needs to work to ensure global coordination on the eventual policy normalization. In addition, as pointed out in the previous paragraph, we suggest countries with adequate vaccines share vaccines with trade partners and make vaccines a global public good, which would facilitate the convergence of global recovery and mitigate potential shocks to EMDC's FX markets and balance of payments.

To ensure adequate international financing and mitigate sovereign debt risk in LICs, we support the Fund to promote all stakeholders, especially private creditors, to participate in debt treatment to LICs during the implementation of the G20 DSSI and Common Framework for Debt Treatments. Moreover, we encourage staff to reflect on the implication of the forthcoming SDR general allocation and SDR recycling to the economic growth projection and debt sustainability analysis for LICs. Considering the huge challenges that the LICs and the global economy are facing, we call on the Fund to implement the SDR allocation as soon as possible.

To mitigate COVID-19 shocks and prevent potential scarring, China supports the economy in a balanced manner, and from both the supply and demand side. For the supply side, measures are taken to support market entities and firms, and to keep their normal operation. This has proved to be an effective way to protect employment and households in a sustainable manner. From the demand side, China promotes public investment on infrastructure, digitalization, and greener development, which will help lift productivity in the medium and long term.

Global Financial Stability Report (GFSR)

Large-scale fiscal and monetary accommodation has helped mitigate the impact on the economic and financial conditions, but the potential longer-term side effects stemming from the debt build-up and “low-for-long” monetary policy remain to be seen. With ultraloose monetary policies and increased investor optimism of an economic rebound, financial markets have continued to reach new heights since the publication of the last GFSR, further increasing its divergence from the real economy. The low interest rate environment will continue to put pressure on banks' profitability, which may motivate banks to engage in yield-searching activities in the shadow banking system to the detriment of financial stability. Meanwhile, the rapid expansion of central banks' balance sheets in the AEs could risk undermining their credibility in maintaining price stability in the longer term. The recent rise in longer-term bond yields shows that inflation expectation needs to be carefully anchored.

Financial conditions in China have remained basically stable despite the impact of the pandemic. Like many other countries, China has implemented measures over the past year to help direct credit to support the most vulnerable sectors and groups. There are inevitably

costs and tradeoffs in implementing such policies, and this is not a unique challenge for China. Because of the coordinated supportive measures together with the successful containment measures, however, the Chinese economy has recovered from the pandemic more rapidly than most other countries, as pointed out by staff in the Executive Summary and Chapter 1. The strong economic growth would alleviate and reverse the buildup of vulnerabilities in the financial system and provide the Chinese government with more resources and buffers to respond to future shocks. Our authorities will stay vigilant and continue to strengthen our financial regulatory and supervisory framework going forward.

As for the implicit guarantees to Chinese state-owned enterprises (SOEs) mentioned in Chapter 1, it is important to note that the SOEs are separate independent entities from the government. Our authorities have stated repeatedly in the past that there is no such implicit guarantee. The recent default by some SOEs is a continuation of an existing trend. It has made the pricing of SOE debt more efficient and will help SOEs to be subjected to greater credit discipline. This is a healthy development in China's SOE reform and will ultimately benefit the Chinese economy.

The recent surge in price of crypto assets had drawn many investors' attention and may pose financial stability risks. Crypto assets also raise several broader policy issues, such as AML/CFT regulation and supervision, regulatory measures to prevent tax evasion, and the need to avoid circumvention of capital controls, etc. As crypto assets are becoming more mainstream, we suggest the GFSR to have more discussion in this area going forward. *Staff's views are welcome.*

Fiscal Monitor

We take note that government debt has risen to unprecedented levels in the context of large-scale fiscal responses, with government debt for advanced countries reaching 120 percent of GDP on average in 2020. In this regard, abrupt changes in financing conditions and rising interest rates may aggravate interest burdens on government debt and even threaten debt sustainability. Therefore, we encourage staff to closely monitor the fiscal risks facing developed countries going forward. For developing countries, with relatively smaller fiscal packages and debt increase, monetary policy should play a more important role in supporting the economy and private capital should be fully motivated.

We welcome the detailed description of methodology used to estimate the public debt in China in Chapter 1. While this estimation is still different from that of the authorities, we see merit in this estimation as opposed to the approach of "augmented government debt" used in the China Article IV, as the former is more pragmatic and realistic than the latter. We also take note of the projected upward trajectory of China's public debt over the medium term. The Chinese government will take effective measures to stabilize the macro leverage and closely monitor the path of the public debt going forward.

The analysis on income inequality in Chapter 2 is very important, especially in the context that large preexisting inequalities in many countries have amplified the damaging effect of the pandemic. China has carried out various fiscal policies to support low-income groups during the pandemic through measures in securing jobs and enhancing public investment. In recent years, China has made considerable effort in addressing income inequality, with more than 10 million people lifted out of poverty each year since 2012. Around 770 million Chinese have been lifted above the poverty line since the reform and opening up in 1978, accounting for 70 percent of global poverty reduction during that period.