Joseph Yam: The ADB challenge to help Asia return to stable and sustainable growth

Statement by Mr Joseph Yam, Alternate Governor of the Hong Kong Monetary Authority, at the 35th Asian Development Bank Annual Meeting, Shanghai, 10-12 May 2002.

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Mr President, I would like to first congratulate you on your re-election as the President of the Bank. I would also like to thank the Government and the people of the People's Republic of China for their hospitality in hosting this year's Annual Meeting in this magnificent city of Shanghai, itself a powerful symbol of tradition and modernisation. I also express my sincere appreciation to the Bank's management and staff for the excellent arrangements made for this meeting. I join others in adding our special welcome to our new member of the Bank – Portugal.

Poverty is reduced more extensively at times of fast economic growth but less so when growth slows. The past year has been a difficult one for the poor. Amid the synchronised slowdown of major industrial economies, economic growth has been slow and uneven in Asia. The terrorist attacks on the US on 11 September shocked the world. The Enron debacle and the Argentine economic crisis cast long shadows on the equity and financial markets worldwide. Against this background, the task of poverty reduction is made more daunting and pressing.

However, I must commend the Bank for meeting the challenges of last year by mapping out and implementing the Long-term Strategic Framework. The framework seeks to reduce poverty through three core areas of sustainable economic growth, inclusive social development and good governance. The strategy is a sound one as it does not focus solely on physical infrastructure, i.e. the building of roads, bridges and other "hardware", but also on the "software" of policy and institutional reform in the public and the private sectors. The Strategic Framework also attaches importance to private sector development, particularly in the fields of finance, banking and corporate governance.

The quality of the "software" of a developing economy is precisely what international investors are looking for as they return to Asia. At a time when Asian economies are showing incipient signs of recovery against an improved external environment, international capital flows are triggering back to the region but in a more cautious and discriminate manner than before. Investors are now a lot more selective about who may lend to and where they put their money. International capital flows from OECD markets to Asia, in the form of bank credits, foreign direct investment and portfolio flows, have dropped significantly in the last few years. In the case of bank credits, total flows declined by about US$200 billion during the 1997-1998 period, although the decline has been at a more moderate pace in the last two years.

In the light of this, it is important that the Bank plays a catalytic role in mobilising resources within and outside of the region. One approach to this challenge would be for the Bank to return to basics and improve the three channels of financial intermediation, namely, banking, equity and debt, through a number of measures. First, the Bank could increase investment in the **financial infrastructure** in Asia. Just as physical infrastructure, such as airports and highways, facilitates the movement of people and goods, financial infrastructure, such as the payment and settlement systems for the banking and securities sectors, facilitates the safe and efficient movement of money. The importance of a robust payment and settlement system in this region is underscored by the events of 11 September.

Secondly, the Bank could expand the technical assistance programme to assist economies in **restructuring the banking sector**. Small and medium-sized enterprises employ the most workers in Asia and they are mostly dependent on bank financing. The banking sector in Asia, devastated by the Asian financial crisis, has not fully recovered. Banks understandably are adopting a very conservative lending strategy towards companies with a lower credit rating, such as Small and Medium-sized Enterprises. The Bank's assistance in speeding up the banking sector reform would help SMEs to get back on their own feet, thereby reducing unemployment and poverty.

Thirdly, the Bank could expand assistance in building up the institutional capacity of individual economies to **improve corporate governance** in the private sector. Emphasis should also be made to improve the auditing, disclosure and transparency standards of publicly-listed companies. As seen in the Asian crisis and again in the Enron incident, good corporate governance is critical to restoring investor confidence in the equity markets.

Fourthly and lastly, the Bank could assist with **the development of the bond market in Asia**. Clearly the financial intermediation process cannot be dominated by one or two intermediaries. Earlier, in 1990, when it was the banks in the United States that seized up as a consequence of a collapse in the value of real estate collateral, the capital markets were able to substitute for the loss of bank intermediation. In Asia, there is considerable room to develop a bond market to serve as a back-up in case of any systemic disruption in the banking and equity channels.

In this connection, I fully support the Bank's Private Sector Development Strategy which aims at catalyzing private investment through direct financing, credit guarantee and development of financial intermediaries. I also note that the Bank's loan contribution to the finance sector has seen significant increase, from 3% in 2000 to 11% in 2001.

Mr President, I am confident that under your leadership, the Bank will help Asia return to stable and sustainable growth and to enjoy prosperity. Thank you.