



ASIA FORUM
BEIJING
FRIDAY 26 MARCH 2010

LSE Asia Forum 2010

China and the World: the Challenges of Change

Policy Spillover and Coordination in a Globalized World

Deputy Governor Hu Xiaolian
People's Bank of China
March 26, 2010

Ladies and gentlemen,

It's a pleasure to attend this year's event and to exchange thoughts on macro policies in an ever globalized world.

During the past decades, as global economies and markets further integrate, the world is becoming smaller and smaller. China, with no exception, has been part of it. Actually, in the unprecedented efforts to counter the most recent financial crisis, market participants and policy makers have all felt the interconnection between economies and thus importance of mutual support as never before. With the cross-border influence and spillover of macro policies, especially of major economies, heightening, it has become an issue worth most serious and insightful consideration, so as to promote a better balanced and sustained path of the world economy.

I. Taking this opportunity, I would like to first brief you on China's monetary policy stance in 2010.

In 2010, the keynote of China's monetary policy remains "maintaining an appropriately easy monetary policy". With exactly the same expression as that of last year, it reflects policy continuity and stability. Meanwhile, as you may read an English sentence with accent falling on different words, the accent now is on "**appropriately**" while it was "**easy**" last year. That is, a more targeted and flexible monetary policy, in line with changing circumstances, and with skillfully managed intensity, pace and focuses:

Firstly, intensity refers to the amount of aggregate money and credit in line with a smooth and sustained economic performance. Last year, broad money supply (M2) increased 27.7% over 2008. The goal for 2010 is a year-on-year increase of around 17%. Last year, newly extended RMB loans stood at 9.59 trillion yuan, while the target for 2010 is around 7.5 trillion yuan.

Secondly, pace refers to steady supply of money and credit to meet appropriate demands of real economy, avoiding large and frequent fluctuations. In the first quarter of 2009, new RMB loans accounted for 48% of the year's total. The goal for 2010 is to keep more balanced and smooth monthly and quarterly transition.

Thirdly, focus lies on facilitating restructuring and transformation of economic growth, channeling credit to key sectors, such as the rural area, small-and-medium sized companies, as well as job-creating, consumption enhancing, environment friendly and strategic industries.

To briefly sum up, China will maintain an appropriately easy monetary policy, balancing the key tasks of maintaining a sustained and sound growth, adjusting economic structure and managing inflation expectations. At the core of these, lies the economic restructuring. As global economy continues to recover, China's economy is expected to achieve steady and fairly vigorous growth. In this context, macro policies will focus more on shifting growth pattern, while monitoring inflation expectations closely as well with remaining uncertainties.

II. Next, putting China's monetary policy in the larger context of globalization, I would like to share with you some of my personal views on macro policy spillover and global coordination.

First and foremost, soundness of domestic economy and financial market is the precondition and the "must" for positive policy spillover. Generally speaking, the coin of macro policy spillover has two sides. *On the one hand*, healthy and sustainable economic and financial development in a major economy (that is, an economy systemically important due to massive trade volume, capital flows or as an international financial center) will exert direct and positive impacts on global economy and financial markets. Through trade of goods and services, cross-border capital flows and other channels into the real economies of other countries, these will contribute to global economy and financial stability. *On the other hand*, major policy measures adopted by systemically important economies usually contain messages for future policy orientation and policy focus, thus indirectly but significantly influence market expectations as well as market confidence in other economies. *Therefore*, policy makers should first of all focus on domestic economy and financial system, taking pains to ensure stable and healthy domestic growth basing on specific circumstances and realities at home, so as to share beneficial spillover with other economies. Meanwhile, policy makers should strive to send positive, responsible and well-communicated signals, avoiding or reducing uncertainties and maintaining market confidence.

Secondly, complexity and inter-dependency of today's globalized world makes it necessary to adopt policy package instead of single

policy instrument. Globalization elaborates and diversifies a country's economic and social network, and complicates the relationships among economic variables, resulting in an enhancement in the dynamics of the multilateral interactions. Therefore, it is difficult for a traditional unilateral policy framing with single policy objective and single instrument, to achieve the ultimate goal of maintaining stable and sound economy. Framing macro policies from only one perspective makes it easier to overlook more serious risk factors. For instance, the traditional goal of the central bank policy targets inflation but neglects monitoring of asset prices, which may pave the ways to asset bubbles, high leverage of the financial system and so on. As the latest crisis demonstrates, asset bubbles and a highly leveraged financial system are serious threats not only to financial stability and real economy at home, but also to systematic stability of world economy and markets. In consequence, policy-makers need to adopt a broader vision and a longer horizon, with a package of policy measures rather than being preoccupied with single instrument, so as to both fix the current problem and to address the root causes.

Thirdly, policy spillover under globalization has to be approached from a multilateral and integrated perspective. In a globalized world, every economy is closely interconnected with each other, rather than just about bilateral links. In such a network, the same policies from a certain country will bring different impacts to countries and regions that differ in stages of development, economic patterns, or phases of economic cycle. Therefore, the same policy may exert positive spillover to some economies, but negative spillover to others; may be beneficial to a bilateral relationship, but damaging to a multilateral relationship. And conclusions from a bilateral perspective may not be sufficient to present the whole picture. Hence, only in a more macroscopic and integral way should we accurately evaluate policy spillover effects on the stability and soundness of world economy and global markets.

Finally, coordination and collaboration in macro policy-making requires deeper communication and understanding. The latest financial crisis has witnessed unprecedented coordination and cooperation between policy-makers around the world. This gives full testimony to the theory that under globalization, no single country is isolated or remote from outside problems, let alone fighting global crises on its own. At different stages of economic development and different phases of economic cycle, different countries have different understanding of macro policy spillovers and will be affected differently. The coordination and cooperation in global policies should not merely emphasize individual countries' effort, nor only focus on mutual attempts. It is important to deepen communication and mutual understanding, so as to find a common ground to enhance positive spillovers while reducing negative ones. Only with pooled strength and wisdom, can we face the challenge and promote healthy and sustainable development of the global economy.

Thank you!