



JAPAN

SADAKAZU TANIGAKI, Governor

1. Introduction

It is a great honor for me to address the Thirty-Eighth Annual Meeting of the Asian Development Bank (ADB). On behalf of the Government of Japan, I would like to express my gratitude to our hosts, the Government of the Republic of Turkey and the people of Istanbul, for their warm hospitality. As the regions of the world become increasingly interdependent, I believe it significant that this meeting is being held in Istanbul—a bridge between Asia and Europe.

At the outset, I would like to express my deep appreciation to Mr. Tadao Chino, former President, for his great contribution to the ADB. I would also like to express my sincere welcome to Mr. Haruhiko Kuroda as the new President of the ADB.

2. Support for Tsunami-affected Countries

The year 2005 started with emergency aid and support for reconstruction and rehabilitation efforts in countries affected by the tsunami in the Indian Ocean last December. It is commendable that the ADB has shown a proactive response by conducting prompt needs assessments and establishing the Asian Tsunami Fund with its own initial contribution of US\$600 million. For its part, in addition to emergency assistance in the form of a grant of US\$500 million, Japan has also promptly provided US\$20 million through the Japan Fund for Poverty Reduction in the ADB.

Many countries and international organizations have also committed financial assistance to the affected countries. It is essential to use their assistance in a more effective and efficient manner as we move to the medium-term reconstruction and rehabilitation phase. In this context, it is particularly noteworthy that the ADB also played a key role in collaboration and coordination among donors by hosting a High-level Coordination Meeting on Assistance to Tsunami-affected Countries in March.

3. Economic Situation and Challenges in the Region

In 2004, the Asian economy demonstrated a good performance with most of the developing economies in the region achieving an annual growth rate of over 5%. This was underpinned by robust external demand and strong domestic demand, particularly by business investment. The economic growth in 2004 is the highest since the Asian currency crisis of 1997-98. I would like to draw your attention here to the fact that the largest trading partner for Asian developing countries is no longer the USA but the Asian developing countries themselves.

While I strongly believe that the Asia-Pacific region will serve as the key engine for the future growth of the world economy, we have to recognize that the regional economy is facing risk factors such as higher oil prices, future economic trends in the People's Republic of China (PRC), and the impact of the expiration of the Agreement on Textiles and Clothing. In addition, the risk of communicable disease like avian flu still remains.

I believe now is an appropriate time to prepare preventions for such risk factors as we are enjoying continuous strong economic growth.

Looking ahead, I would like to point out five challenges for the Asian region.

The *first* challenge is to alleviate poverty. 2005 is a critical year to review progress towards the Millennium Development Goals (MDGs) at the UN General Assembly in September. Even in the Asian region, where relatively good progress in MDGs has been made, non-income-related MDGs, such as reducing the child mortality rate and ensuring universal primary education, are unlikely to be achieved at the current pace of progress. While large countries such as India and the PRC lead in reducing poverty, it has stagnated in low income countries including post-conflict countries like Afghanistan and transition economies in Central Asia. In low income countries, it is important to achieve sustainable growth led by the private sector and to strengthen public expenditure management in order to efficiently provide social services. The international community should focus its support on these countries and poverty spots.

The *second* challenge is to improve the infrastructure of individual countries to a level commensurate with their evolving economies. Even among countries with outstanding economic growth, lack of key infrastructure, such as power supply facilities and highway networks, is a bottleneck for sustainable growth. To overcome this challenge it is essential to build and expand infrastructure by promoting, in particular, private capital inflows.

The *third* challenge is to address the issues of migration to urban areas and demographic changes. While striving to achieve balanced growth between urban and rural areas and preserving the environment, it is important to increase employment opportunities and improve infrastructure to cope with the massive migration to urban areas. While population pressure remains strong in some countries, social security has become a serious issue among aging countries in the region.

The *fourth* challenge is to adapt economic structures and institutions to globalization. I welcome the fact that there has been progress in this area in recent years. I hope that policies and institutional reforms in trade and capital transactions will be carried out steadily in the proper sequencing. The current currency systems in Asia vary from country to country. I believe it desirable that study towards more flexibility in exchange rates be made for developing member countries that lack such flexibility in order to ease adjustments to economic shocks.

The *fifth* challenge is to promote regional cooperation. Regional cooperation brings significant merits to individual countries by exploiting economies of scale and scope, and stabilizing its economy. In this context, it is essential to invest in cross border networks for transport and telecommunication and to promote regional cooperation in finance, trade and investment.

4. Challenges for Japan in Asia

As a member country of the region, Japan shall act together and advance together with countries of the Asia-Pacific. Our primary focus in this respect will be on five areas.

Further strides in structural reform

The *first* task is for Japan to make further strides in reform at home. Restructuring of corporate and financial institutions is something we have pioneered. Over the last several years, Japan has advanced structural reform to overcome its prolonged deflation and to revitalize its economy. These policy initiatives are gradually paying off. Driven by increased domestic private demand, the Japanese economy has been on the track of recovery.

Japan views this recovery as a good opportunity to make further progress in government expenditure and tax system reforms as well as in the reform of the social security system, to ensure sustained growth in the future.

I hope our accelerated structural reforms and the resulting recovery will contribute to economic growth in Asia. I also hope it will offer useful lessons for other countries about how to cope with such challenges as reducing non-performing loans and revitalizing the manufacturing sector.

Prevention of financial crises

The *second* task is to prevent the recurrence of financial crises in Asia. Having learned the lessons from the Asian currency crisis of 1997-98, Japan has been, together with the East Asian countries, vigorously promoting the Chiang Mai Initiative (CMI) since 2000. By now, the network of bilateral swap arrangements (BSA) has expanded to a total of 16 arrangements among Japan, the PRC, the Republic of Korea, and five ASEAN countries, worth US\$39.5 billion.

At the ASEAN+3 Finance Ministers' Meeting yesterday, we reached an agreement to make this CMI framework even more effective and disciplined. Among others, the following three decisions have critical importance.

First, we agreed to integrate and enhance regional economic surveillance into the CMI framework. This is expected to enable us to detect irregularities at an early stage and take swift remedial policy actions, thereby more effectively preventing financial crises.

Second, we agreed to clearly define the swap activation process and multilateralize the decision-making mechanism. This should allow for collective activation of the 16 different BSAs, thereby enabling more prompt activation in the event of emergency.

Third, we agreed on a significant increase in the size of swaps. Specifically this will be achieved by (i) increasing the amount of existing bilateral arrangements; (ii) agreeing on additional BSAs, for example, among ASEAN countries; and (iii) transforming one-way BSAs into two-way BSAs. Japan is willing to, in principle, double the size of our existing BSAs, with the consent of counterparties.

Allow me to add that, in implementing these decisions, complementarity with existing international financial arrangements and disciplined conditions to prevent moral hazards should be firmly maintained.

Intermediation of long-term funds

The *third* task is to enhance intermediation of long-term funds in the region. It is essential to eliminate mismatches of currency and maturity in regional financing and to channel domestic savings in Asian countries for investment in the region. For this purpose, Japan has been promoting the Asian Bond Markets Initiative (ABMI), under the ASEAN+3 Finance Ministers' process, for developing efficient and liquid bond markets in East Asian countries.

Concrete outcomes have already been achieved in this Initiative. Examples are the issuance of local currency-denominated bonds by the ADB and IFC in Malaysia and the issuance of baht-denominated bonds with a credit guarantee by the Japan Bank for International Cooperation (JBIC). Also, under cooperation between Japanese and Korean governments, collateralized bond obligation, the so-called Pan-Asian Bond, was formulated with a guarantee by the JBIC.

Facilitation of foreign direct investment

The *fourth* task is to help attract foreign direct investment. Foreign direct investment provides stable capital inflows and contributes to knowledge and technology transfer. For this purpose, it is important to optimize the benefits of tax treaties. In this context, Japan is proactively working to revise its income tax treaties for facilitating foreign direct investment among regional member countries.

Promotion of economic partnership agreements

The *fifth* task is to strengthen economic partnerships in Asian countries. I believe that pursuing Economic Partnership Agreements (EPAs) is essential to the achievement of this goal. EPAs cover various areas including the establishment of FTAs. Japan and Singapore have been deepening their partnership through the EPA concluded in January 2002. Japan and the Philippines have reached agreements in principle on major elements of their EPA. Negotiations on EPAs with the Republic of Korea, Malaysia and Thailand are making progress. Last month, Japan and ASEAN launched negotiations on a regional EPA. Furthermore, with a view to commencing EPA negotiations with Indonesia, a joint study group has been established. The Joint Study Group is now compiling a report to be submitted to the leaders of the two nations. In addition, the Japan-India Joint Study Group is to be launched by June 2005 focusing on the measures required for a comprehensive expansion of economic relations including the feasibility of a Japan-India EPA.

5. Challenges for the Asian Development Bank

Next, I would like to talk about our expectations for the ADB. I welcome the proactive leadership of Mr. Haruhiko Kuroda who has demonstrated in promoting candid and broad-based dialogue, while clearly presenting his vision regarding the future of Asia and the role to be played by the ADB.

The ADB must remain attentive to the voices of the region, and formulate tailor-made strategies for each country, taking into account the diversity within the region. I hope that each staff member will get out of the box and act with a broader and more comprehensive perspective in mind.

Specifically, the ADB needs to focus on five points.

Steady implementation of reform agenda

The first task is to steadily implement the reform agenda. Now that ADF IX becomes effective, it is essential to carry out this important task outlined in the agreement. Some of the key policies on the reform agenda, such as reviews of the poverty reduction strategy and the performance-based allocation policy, have already been discussed and agreed. The ADB must ensure that its operations clearly reflect these key policies.

Strengthening the operations in Ordinary Capital Resource

Secondly, the ADB is expected to establish a new strategy for use of ordinary capital resources. Coupled with the ADB's strategies for low-income countries, this should allow the ADB to respond to the massive potential needs of countries in the region. With this, the ADB can play a part in addressing the enormous infrastructure needs. Developing the private sector and business environment and strengthening the financial system are also important areas. In this exercise, it is also essential to streamline operational procedures while maintaining adequate accountability.

Promotion of regional cooperation

Thirdly, the ADB is expected to promote regional cooperation. To date, the ADB has implemented cross border projects, focusing primarily on infrastructure building, as was the

case with the Greater Mekong Subregion. More recently, such cross border programs have been extended to Central Asia and South Asia.

In addition to lending operations, it is important for the ADB to support improvement in regional financial markets and monitoring of the economic situation in the region as a unique mandate for regional development banks. In this context, the Office of Regional Economic Integration is expected to contribute to boosting such support. The contribution from the ADB in this area should be commended and further increased.

Organization, personnel and procedural streamlining

Fourthly, proper management of organization and personnel is critical for the ADB to meet regional needs precisely and efficiently. To achieve this task, it is essential to steadily follow up reorganization and implement the new human resource strategy under the principle of result-based management.

While maintaining efforts to improve the operational efficiency, the ADB should secure sufficient human resources to properly respond to the demands of member countries.

Public communications policy

Finally, it is essential for the ADB to reflect broad-based opinions in its operations and to seek increased understanding of and support for its activities. In this respect, I welcome the establishment of a new Public Communications Policy. I hope to see strong leadership of the President in implementing this new policy to increase visibility of the ADB in the donor community as well as in borrowing countries.

6. Conclusion

I would like to express my gratitude to the Board of Governors for their resolution deciding that the 2007 Annual Meeting will be held in Kyoto. I am honored that the annual meeting will be held in Japan on this important occasion of the fortieth anniversary.

Like Istanbul, Kyoto is known for its depth of history and tradition. At the same time, Kyoto is a cradle of venture entrepreneurship and also a center of medicine and science. Moreover, as the Kyoto Protocol indicates, it is a city committed to achieving harmony between urban life and the natural environment. We will do our best to prepare the meeting so that this ancient capital of Japan can provide the ideal environment for discussing the future of Asia and the ADB.

Thank you.