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The year 2007 is a very important year in China's modernization drive. The 17th CPC National Congress was convened successfully. Economic and social development showed a good momentum. The gross domestic products posted 24.95 trillion yuan, up 11.9 percent from the previous year. Grain output increased for four consecutive years. Added value of statistically-large industrial enterprises and total trade volume grew by 18.5 percent and 23.5 percent respectively. The disposable per capita income of urban residents and per capita net income of rural residents rose by 12.2 percent and 9.5 percent respectively, representing an acceleration of 1.8 percentage points and 2.1 percentage points. The official foreign exchange reserves exceeded US\$1.5 trillion dollar.

Under the leadership of the CPC Central Committee and the State Council and guided by Deng Xiaoping Theory and the important thinking of Three Represents, the People's Bank of China (PBC) implemented the scientific development approach, actively explored fresh ideas and innovative measures to perform central bank functions under the new circumstances, continued to strengthen and improve financial measures of macroeconomic management, promoted and deepened financial reform, made efforts to preserve financial stability, develop financial market and encourage innovation in the financial service, thus providing strong support to a high-quality and rapid growth of the national economy.

Financial measures for macroeconomic management were further intensified In 2007, the economy continued the momentum of a steady and fairly rapid growth. However, excess liquidity resulted from balance of payments imbalances remained a prominent problem. In addition, new problems emerged including upward pressures on prices and uncertainties in the global economy. In order to prevent rapid economic growth from becoming overheated and prevent structural price hikes from evolving into a generalized inflation process, the PBC employed a variety of policy tools to achieve forward-looking, more scientific and effective financial macroeconomic management. First, the PBC continued to use quantitative instruments to strengthen banking system liquidity management and increase the frequency and strength of policy operations to keep money and credit growth within a proper range. Open market operations were intensified and reserve requirement ratio raised for ten times by a total of 5.5 percentage points. As a result, excess liquidity supplied in the purchase of foreign exchange was by and large drained. Second, the role of price instruments was strengthened and policies on domestic and foreign currencies were further coordinated. The benchmark deposit and lending rates were raised for six times to curb price rises and stabilize expectations. The RMB exchange rate became much more flexible and played an even larger role in boosting structural adjustment and buffering against external shock. Third, policy guidance and risk alert for financial institutions was intensified. The PBC guided financial institutions to lend in a balanced pace, optimize credit structure, restrict credit provision to industries with excess capacity and highly polluting enterprises with excessive energy consumption, provide more credit support to vulnerable sectors and under-privileged groups such as the service sector, SMEs, independent innovation, energy conservation, environmental protection and etc. In particular, continued efforts were made to step up financial support to

rural areas, and improve rural financial services. The PBC encouraged financial institutions to expand fee-based services and change their profit making pattern. Despite the many constraining factors and growing difficulties in macroeconomic management, these measures effectively curbed excess growth of money and credit and played an important role in promoting steady and rapid economic growth. At end 2007, broad money M2 and local currency loans grew by 16.7 percent and 16.1 percent respectively.

Fresh progress was made in financial reform and financial stability The Industrial and Commercial Bank of China, Bank of China and China Construction Bank have put in place a modern enterprise system and improved corporate governance and risk management. As a result, there was significant improvement in their capital adequacy ratio, asset quality and profitability. Capital injected by the state produced good returns and, the value of state capital has been preserved and increased. Reform of the China Development Bank, Agricultural Bank of China, and China Everbright Bank proceeded smoothly. With the improvement and implementation of positive incentive oriented financial support policy, the rural credit cooperatives achieved progress in ownership reform, compensation of capital, mechanism transformation and asset quality improvement. The policy on individuals' foreign exchange management was adjusted to adopt an annual quota management for individuals' purchase and sale of foreign exchange. Balance management for fund inflow and outflow was introduced to facilitate trade and investment and steadily promote capital account convertibility. Research and study on the deposit insurance system was conducted to press ahead with law making for the deposit insurance scheme. The management of central bank lending for financial stability purpose was strengthened. The PBC, in cooperation with relevant authorities, properly addressed the problems in some high-risk financial institutions.

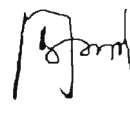
Financial market expanded in a stable and sound manner The PBC continued to encourage product innovation in the financial market, regulated the development of enterprise short-term financing bills, promoted the pilot credit asset securitization program and the issuing of RMB-denominated bonds by mainland financial institutions in Hong Kong. Furthermore, pilot RMB interest rate swap trading was deepened, and RMB foreign exchange swap products were launched. The market maker system was further improved and money brokerage business was promoted. The *Rules on the Administration of Inter-bank Lending /Borrowing* was amended. The National Association of Financial Market Institutional Investors was established. Progress was also made in the nurturing of benchmark market interest rate. The Shanghai Interbank Offered Rate (Shibor) operated soundly. The individual gold trading business was expanded in the Shanghai Gold Exchange. The pilot program for commercial banks to set up fund management companies was pushed forward.

Financial service and management yielded new results The Cheque Image Exchange System was introduced nationwide, and the individual identity information verification network was established and operated in the whole country. New business such as electronic payment was further regulated and payment environment for the upcoming Olympic Games improved. Management of currency and bullion was further

improved and rational demand for cash was satisfied. The Treasury Centralized Balancing System (TCBS) was improved and more efforts were made to introduce the Transversal Network Linking Fiscal, Taxation, Treasury and Banking Agencies in a wider geographical coverage. The state treasury direct handling of contributions to and payment by the social security fund and migrant workers pension fund was promoted. Pilot treasury service innovation such as direct payment by treasury produced concrete results. The coverage of non-bank information collection by the credit registry was expanded, and the publication system for registration of the pledge of account receivables was created. Credit system for small and medium enterprises and rural credit system building made new headways. China became a full member of the Financial Action Task Force (FATF), and the anti-money laundering regime was gradually expanded to cover the entire financial system.

International exchanges and cooperation grew further The PBC actively participated in international financial affairs, stepped up exchanges and dialogues with international financial institutions and foreign counterparts, and took an active part in the multilateral consultation on global imbalances organized by the International Monetary Fund. The PBC worked tirelessly to win understanding and support of various parties on major issues concerning national interests, promoted the regional foreign exchange reserve pooling under the ASEAN plus Three framework, a major step forward in multilateralization of the Chiang Mai Initiative. The 2007 Annual Meeting of the African Development Bank Board of Governors and the G30 Spring Meeting were held successfully.

The year 2008 is the first year in implementing the decisions of the 17th CPC National Congress and marks the 30th anniversary of China's reform and opening-up and the 60th anniversary of the PBC. The PBC will earnestly implement the decisions made by the 17th CPC National Congress and the Central Economic Work Conference, follow the scientific development approach, maintain a sound balance among various objectives of macroeconomic management and among the various central bank functions, and properly handle the relationship between improving external environment and improving the work of the central bank. Coordination and cooperation with other departments will be stepped up. The forward-looking and scientific nature of monetary policy will be stressed to improve its effectiveness. A tight monetary policy will be implemented to prevent the rapidly growing economy from becoming overheated and prevent structural price hikes from evolving into a generalized inflation process to support a healthy, balanced and sustainable economic growth.



Governor of the PBC
April 18, 2008