Die Reform des chinesischen Finanzsektors als entscheidender Faktor für die Modernisierung der chinesischen Volkswirtschaft

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Topics

- China’s Financial System
- China’s Banking Industry
- The Internationalisation of the Renminbi
Topics

- China’s Financial System
China’s Financial System in International Comparison

- High intermediation level (disintermediation under way)
- Big State-owned banks dominate (declining market share)
- Segregate banking system (universal banks under way)
- Strong regulation and supervision (gradual liberalisation especially with regards to the interest rate)
- Still low internationalization level (internationalization under way)
- Managed exchange rate system and capital controls (Renminbi internationalization under way)
- Still underdeveloped capital markets (esp. bond market under development)
China’s Financial Sector Reform: The Last Fifteen Years

- Introduction of asset management companies for bad loans
- Spinning off of CBRC
- Opening of the market for foreign financial institutes
- Internationalization of banks
- Implementation of Shanghai FTZ

2000-2003: Recapitalization of big Chinese banks, IPOs (partial privatization), Strategic foreign investors
2004-2006: Announcement by the state council to develop Shanghai into an international financial center by 2020
2007-2009: More flexibility in interest and exchange rate
2010-2015: RMB enters SDR, Exchange rate and interest rate liberalization

2011: Implementation of Shanghai FTZ
2012/2013/2014: Recapitalization of big Chinese banks, IPOs, Strategic foreign investors

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The Main Challenges for China’s Financial System

- Further internationalization of RMB and liberalization of exchange rate mechanism and capital account
- Further development of a market driven financial system
- Further upgrade of capital markets
- Development of universal banking business model including investment banking
- Internationalisation of banks
- Further opening-up for foreign and private financial institutions
Topics

- China’s Banking Industry
The Current Business Model of Chinese Banks

- Commercial banking driven
- Mainly domestically oriented
- Profitability driven by comparatively high interest rate spread and strong loan growth
- Comparative cost advantages, esp. in staff expenditures compared to Western peers
- Still highly regulated market
- Comparative low competition from foreign banks
The Business Model of Big Chinese Banks in International Comparison (2006-2014)

<table>
<thead>
<tr>
<th></th>
<th>Size</th>
<th>Profit</th>
<th>Profitability</th>
<th>Lending business</th>
<th>Loan portfolio</th>
<th>Refinancing</th>
<th>Cost control</th>
<th>Business diversification</th>
<th>Capital strength</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total asset (million USD)</td>
<td>Pre profit million USD</td>
<td>ROAA (%)</td>
<td>ROAE (%)</td>
<td>Net interest margin (%)</td>
<td>NPL ratio (%)</td>
<td>Residential mortgage loans/gross loans (%)</td>
<td>Corporate and commercial loans/gross loans (%)</td>
<td>Other loans/gross loans (%)</td>
</tr>
<tr>
<td>Big four Chinese banks Average</td>
<td>1,402,035</td>
<td>24.053</td>
<td>1.13</td>
<td>16.23</td>
<td>2.66</td>
<td>2.95</td>
<td>15.45</td>
<td>79.18</td>
<td>5.37</td>
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<tr>
<td>International peers</td>
<td>1,608,57</td>
<td>6.209</td>
<td>0.34</td>
<td>6.93</td>
<td>1.41</td>
<td>3.54</td>
<td>35.85</td>
<td>25.44</td>
<td>34.45</td>
</tr>
</tbody>
</table>
SWOT ANALYSIS of Chinese Banks

**Strengths**
- Large customer base
- Highly profitable
- Low CIR
- Regulated market

**Weaknesses**
- Immature risk management and small product portfolio (commercial banking)
- Corporate governance (ownership)
- Organisational design (horizontal integration)

**Opportunities**
- Universal banking business model including asset management and investment banking
- International business expansion (trade finance)
- Loan business with SME’s

**Threats**
- Lower asset growth
- Decling interest rate spread
- Disintermediation and Digitalisation
The Challenges For Banking in China in the Future

**Lower macroeconomic growth:**
- Lower asset growth
- Higher NPL - ratio

**Liberalisation of interest rate:**
- Lower NIM
- Declining profitability

**Disintermediation:**
- Fin Techs
- Shadow banking
- Capital Markets
A New Business Model for Chinese Banks?

- Diversification of revenue sources towards fee income
- Stronger business units in asset management (private banking and wealth management), investment banking, and international transaction banking
- Refocus of corporate banking towards SMEs

Convergence ahead between global banking business models?
- The Internationalisation of the Renminbi
The Internationalization of China’s Financial System After the Financial Crisis

- 2008 Becoming a member of the Basel Committee and the FSB
- 2009 Up-grade in IMF in terms of positions and voting power
- 2009 Developing Shanghai as an international financial centre until 2020
- 2010 Launching the RMB as an international trade settlement currency
- 2010 Establish Hong Kong and other global financial centers as off-shore markets for the RMB as an investment currency
- 2012 Set up a free trade zone in Shanghai
- 2014 Shanghai and Hong Kong stock market connection
- 2015 Liberalise the exchange rate mechanism of the RMB
- 2015 RMB enters the SDR of IMF as a reserve currency
The Renminbi in the SDR

Acceptance into the IMF’s basket of reserve currencies was hugely significant.

Currency allocation of Special Drawing Right (%)

- Renminbi: 10.9%
- Dollar: 42%
- Euro: 31%
- Yen: 8.1%
- Sterling: 8%

Sources for slideshow: Thomson Reuters Datastream; IMF; SWIFT; Standard Chartered; BIS; HSBC
### Road Map of the Internationalization of the RMB

<table>
<thead>
<tr>
<th>Degree of Internationalization</th>
<th>RMB as:</th>
<th>Requirements:</th>
<th>Time Schedule:</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Trade currency</td>
<td>Controlled convertibility</td>
<td>Since 2010</td>
</tr>
<tr>
<td>Investment currency (FDI/ODI)</td>
<td></td>
<td>Controlled convertibility</td>
<td>Since 2011</td>
</tr>
<tr>
<td>Off-shore portfolio currency (Hong Kong)</td>
<td></td>
<td>Controlled convertibility and controlled cross-boarder capital flows</td>
<td>Since 2012</td>
</tr>
<tr>
<td>Reserve Currency</td>
<td></td>
<td>Convertibility, open capital accounts, managed or flexible exchange rate</td>
<td>Probably around 2020-2025</td>
</tr>
</tbody>
</table>
China’s Managed Exchange Rate System

July 2005
RMB 8.11
±0.3%

June 2007
(±0.5%)

April 2012
(±1%)

May 2014
(+/- 2 %)

RMB/USD 6.55
(May 2016)
A Long Policy of Renminbi Appreciation Followed...
...By Recent Depreciation Pressure That...
...Leads to Capital Outflows
Tensions Between On- and Offshore Renminbi Exchange Rate
The Currency System of the Future?

Open questions:
- Reform pace in China?
- Future of the Euro?
“The 19th century belonged to England, the 20th century belonged to the US and the 21st century belongs to China. Invest accordingly”

Warren Buffet, 2007