

China's Shadow Banking

May 12, 2014

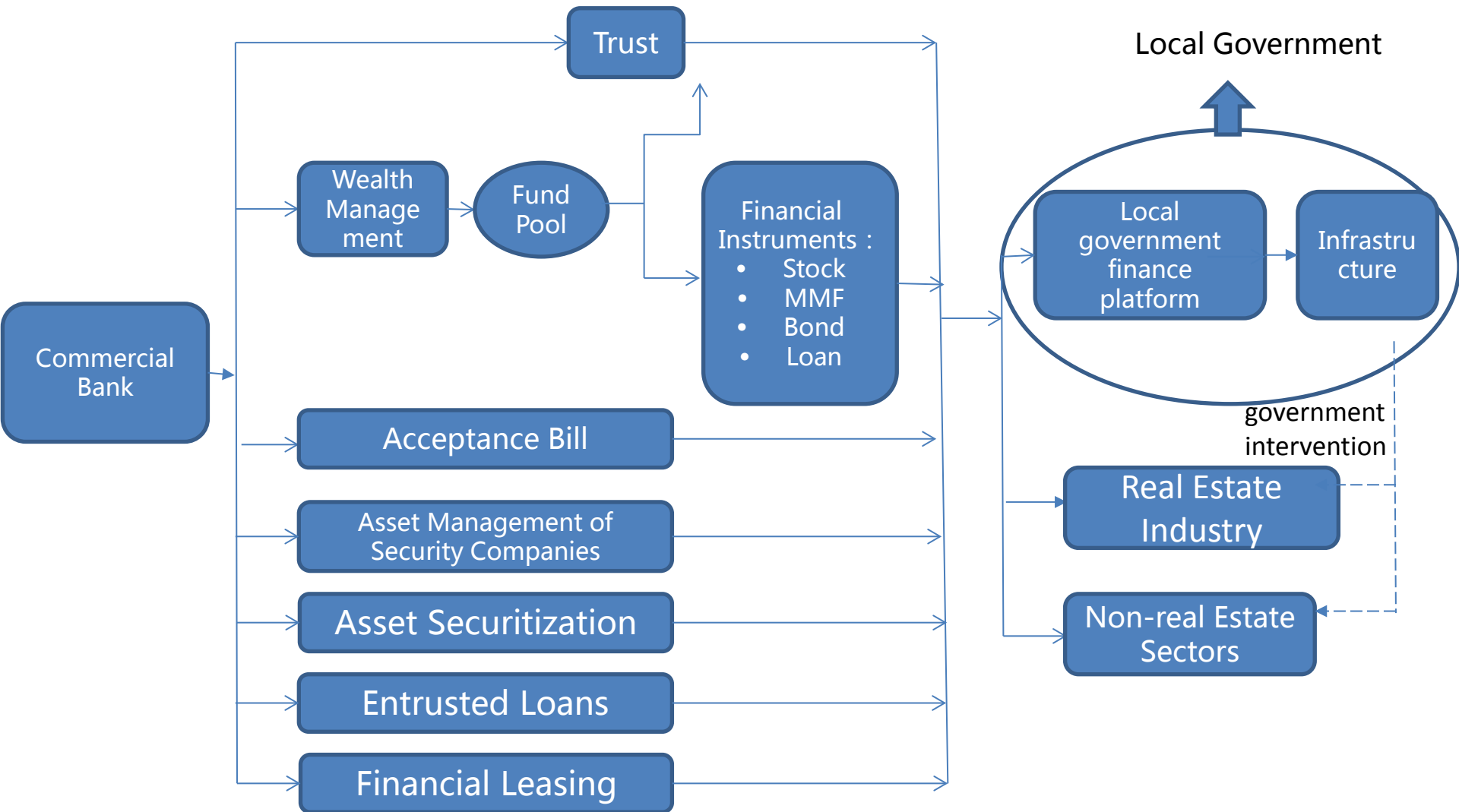
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The Problem

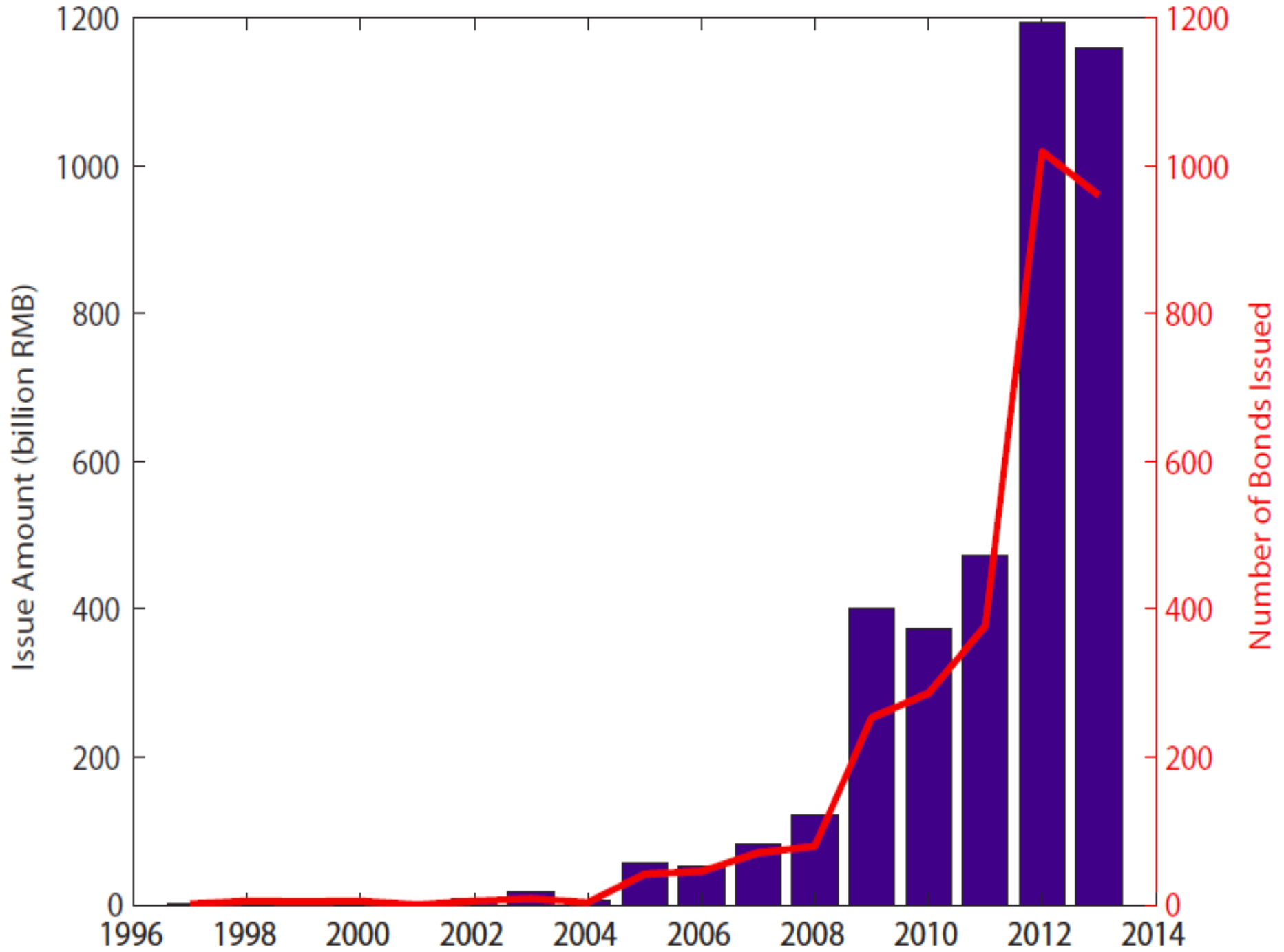
- Deceleration of growth, export, real estate
- Legacy NPL with banks from 4tn stimulus
- Particularly in the form of “Shadow Banking”
- Potential risk of default, bank-run, contagion?

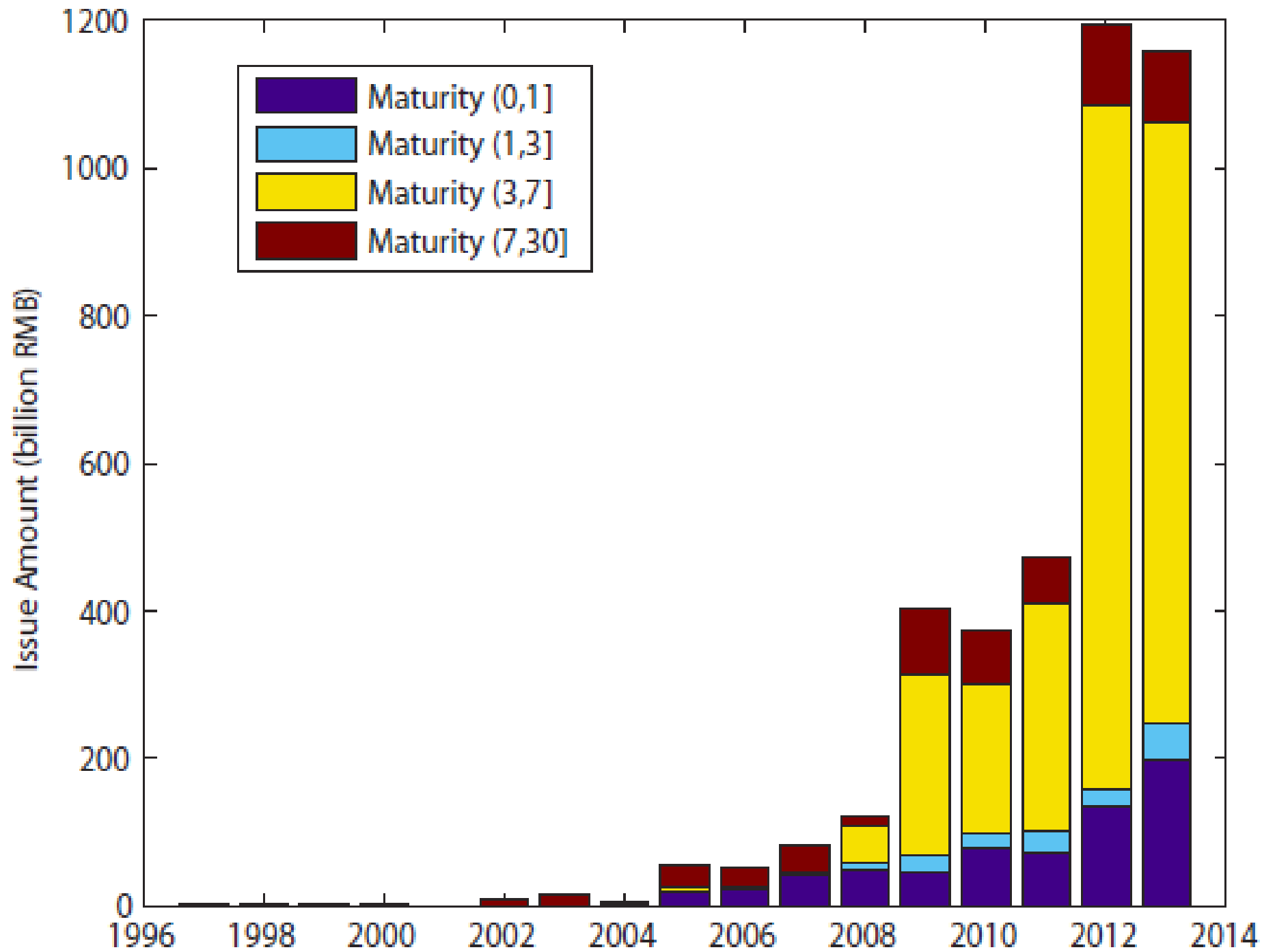
Overview of Shadow Banking System in China



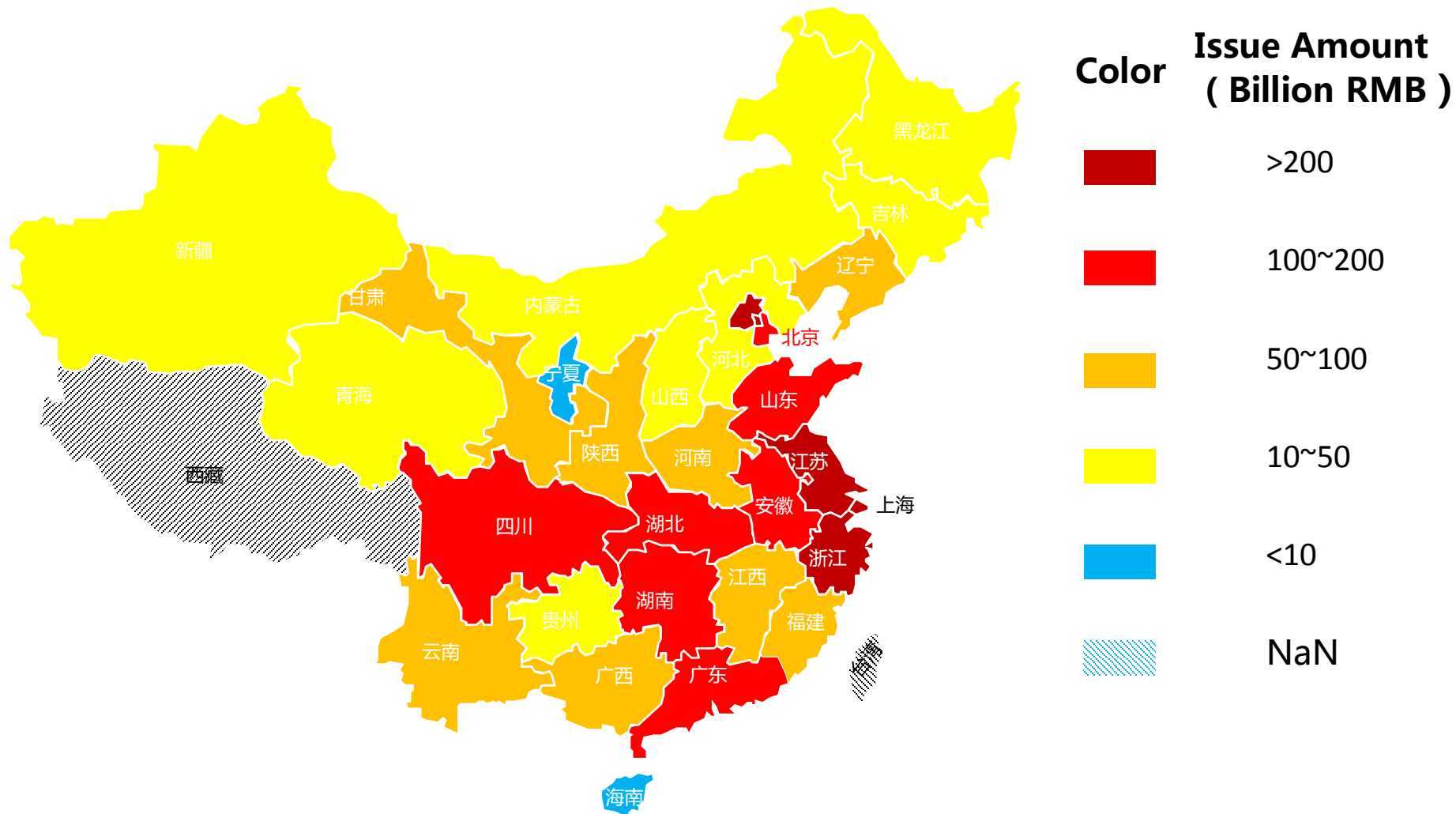
China's Shadow Banking

- Lender:
 - Wealth management: 12 tn RMB
 - “Trust”: 11tn RMB
- Borrower: local government funding platform (Audit Report: 18 tn RMB)
- Public available data, LGFP bond

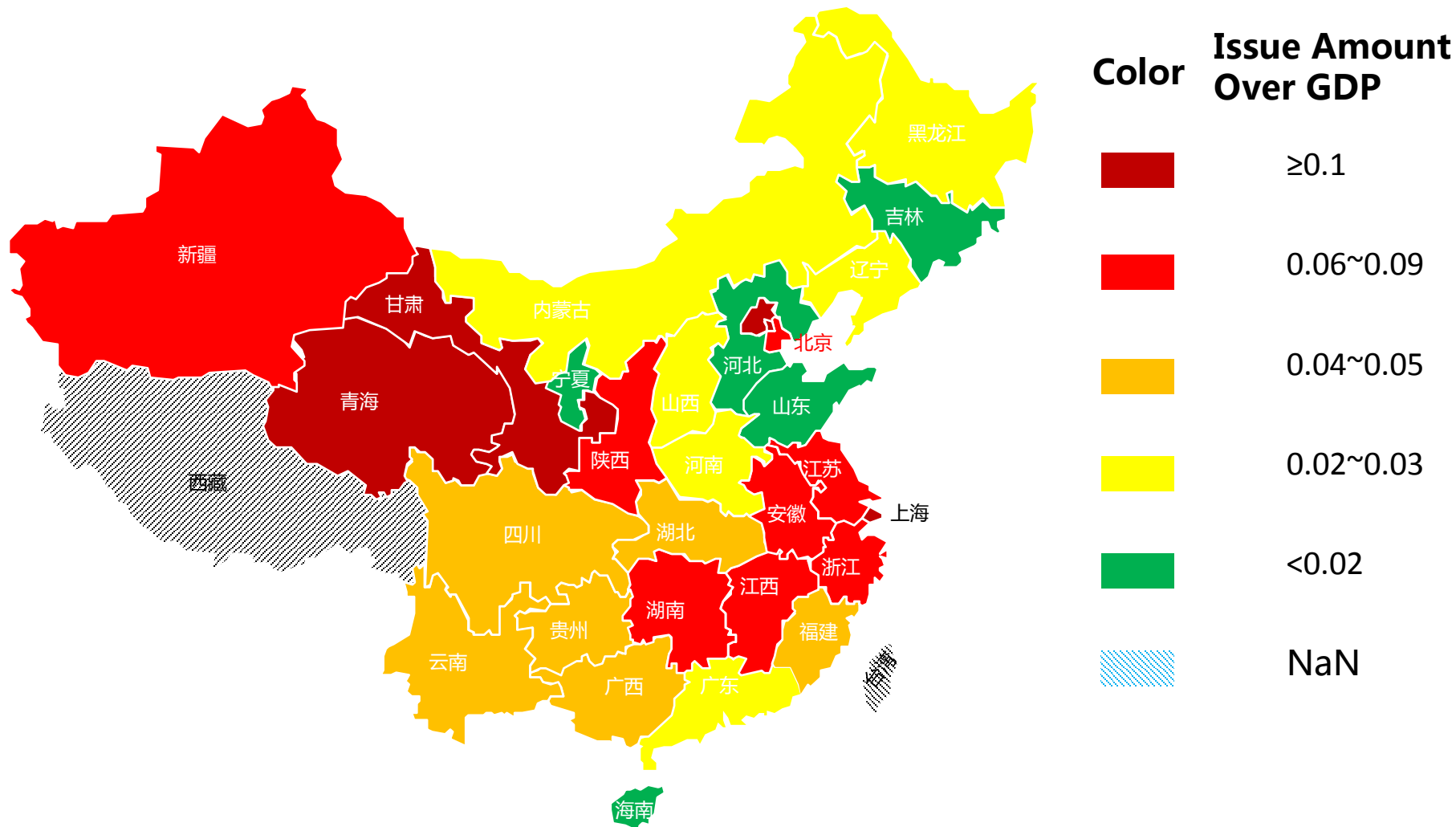




Chengtou Bond Issue Amount Regional Statistics



Chengtou Bond Issue Amount Over GDP Regional Statistics

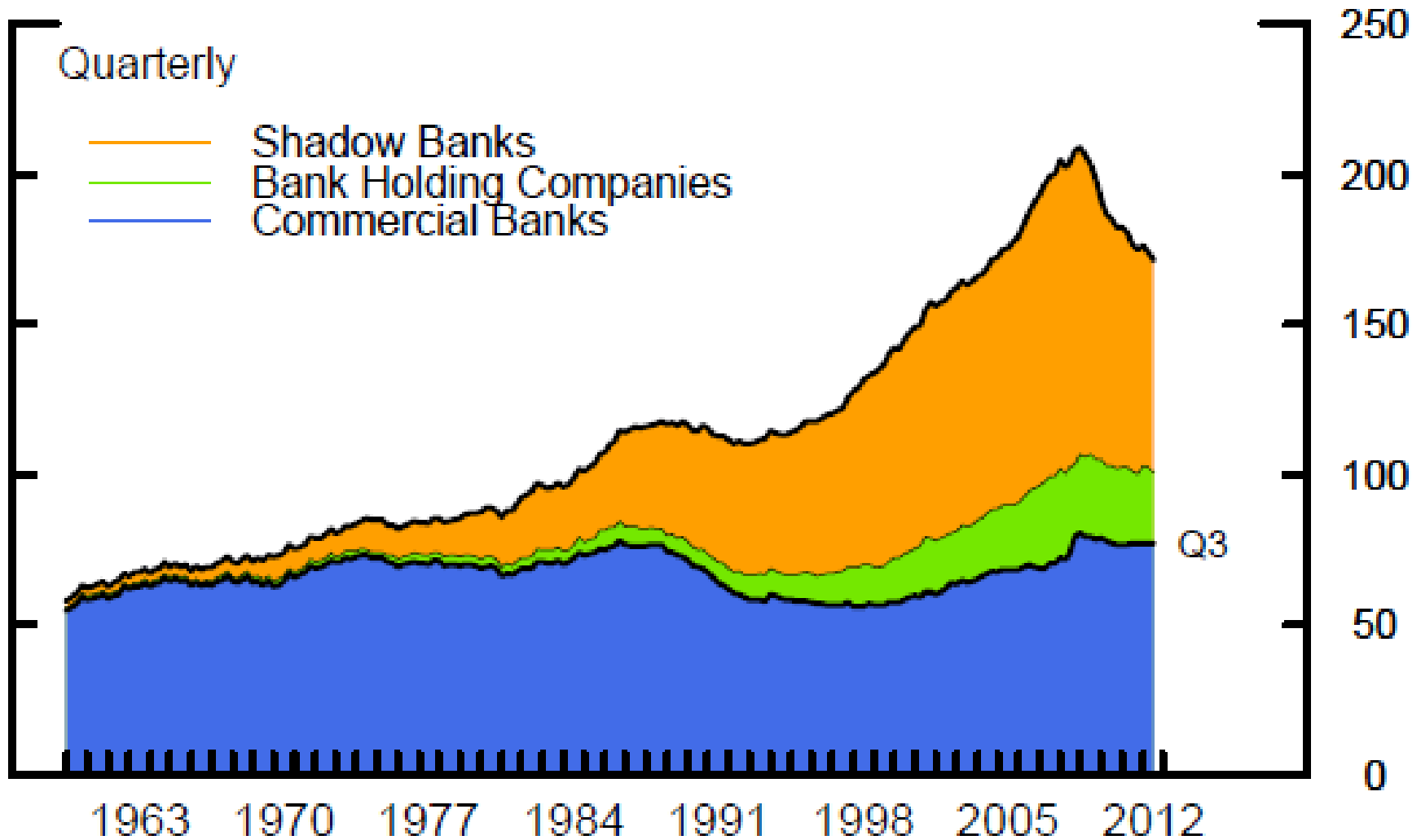


More like U.S. in 1980s

- Simple off-balance sheet
- 20-30% (last bailout 1tn U.S.)
- Implicit guarantee
- Deposit rate ceiling

Financial Sector Liabilities

Total liabilities as percent of GDP



Note: Bank Holding Company liabilities include the liabilities of Broker Dealers.

Source: Federal Reserve Flow of Funds.

Policy Remedy – Borrower Side

- Fiscal – local government in particular
 - Municipal debt, disciplined by market
 - Property tax, reducing land financing incentive
 - Less interference with banks and business
 - Possible local government restructure (U.S. history)

Policy Remedy – Lender Side

- Financial market reform
 - Interest rate liberalization, deposit insurance, private/foreign banks
- Financial – macroprudential regulation system
 - Incentive compatible, market-based regulation
 - Monitoring (strong financial stability regulator)
 - Preemptive measures (e.g., REITS in U.S.)
 - Capital/liquidity ratios for implicit guarantee (Basel III)

Great Depression v.s. Great Recession

