

Rebalancing, Restructuring and Recreating

--The New Dynamics for Chinese Economy

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Songzuo Xiang
Chief Economist, Agricultural Bank of China
Professor of Economics and Finance, Renmin University of
China

- What does **PRC** (People's Republic of China) stand for?
- 1. Before 1990s, PRC stands for **People, Relationship and Cash.**
- 2. From 1990s to 2000s, PRC stands for **“Prefer Real Cash!”** (make quick money and cash out everything)
- 3. Now PRC Must stand for **“Produces Real Creativity”** (from Made in China to Created in China)

- Rebalancing of Chinese Economy:
- 1. From investment-reliance to consumption-reliance
- 2. From export demand reliance to domestic demand reliance
- 3. From intensive labor reliance to intensive technology and human capital reliance
- 4. From environmental sacrifice and damage to environmental protection and recreation.
- 5. Rebalancing income disparity or inequality

- **Restructuring of Chinese Economy:**
- 1. restructuring of industrial structure particularly increasing contribution of services industry to GDP growth.
- 2. restructuring of investment structure particularly reducing entry barrier for private and foreign capital to services industry, infrastructure and key industries.
- 3. restructuring of wealth portfolio structure particularly encouraging overseas investment by Chinese individuals and enterprises.

- Recreating of Chinese Economy:
- 1. Recreating new competitive advantages because of declining or disappearing of traditional comparative advantages (**Three Lows**: low cost labor, low cost environment, low cost resources)
- 2. Recreating international economic, financial and monetary order particularly reducing Dollar reliance, promoting Chinese overseas investment and guaranteeing a just international trade order.

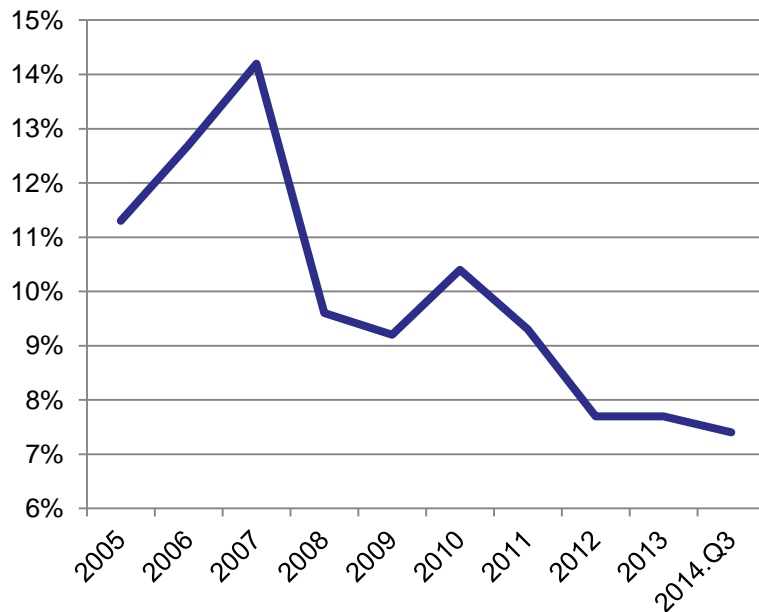
First of all, China's growth slowing down is welcome for industrial restructuring and economic reforming.

China's outlook and main challenges

- China's growth slowdown is welcome as a move toward a more balanced and sustainable growth
- Vulnerabilities rising but still manageable
- Key reform areas
 - Reforms to move toward a new growth model
 - Local government debt and the augmented fiscal position
 - Financial sector, especially "shadow banking"

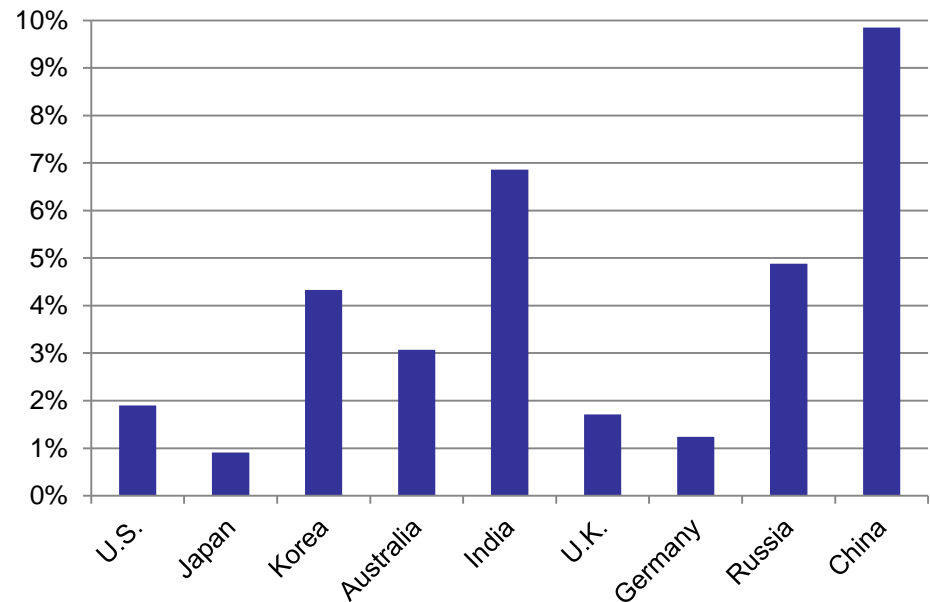
Growth stabilizing at lower level

GDP Growth Rate for China



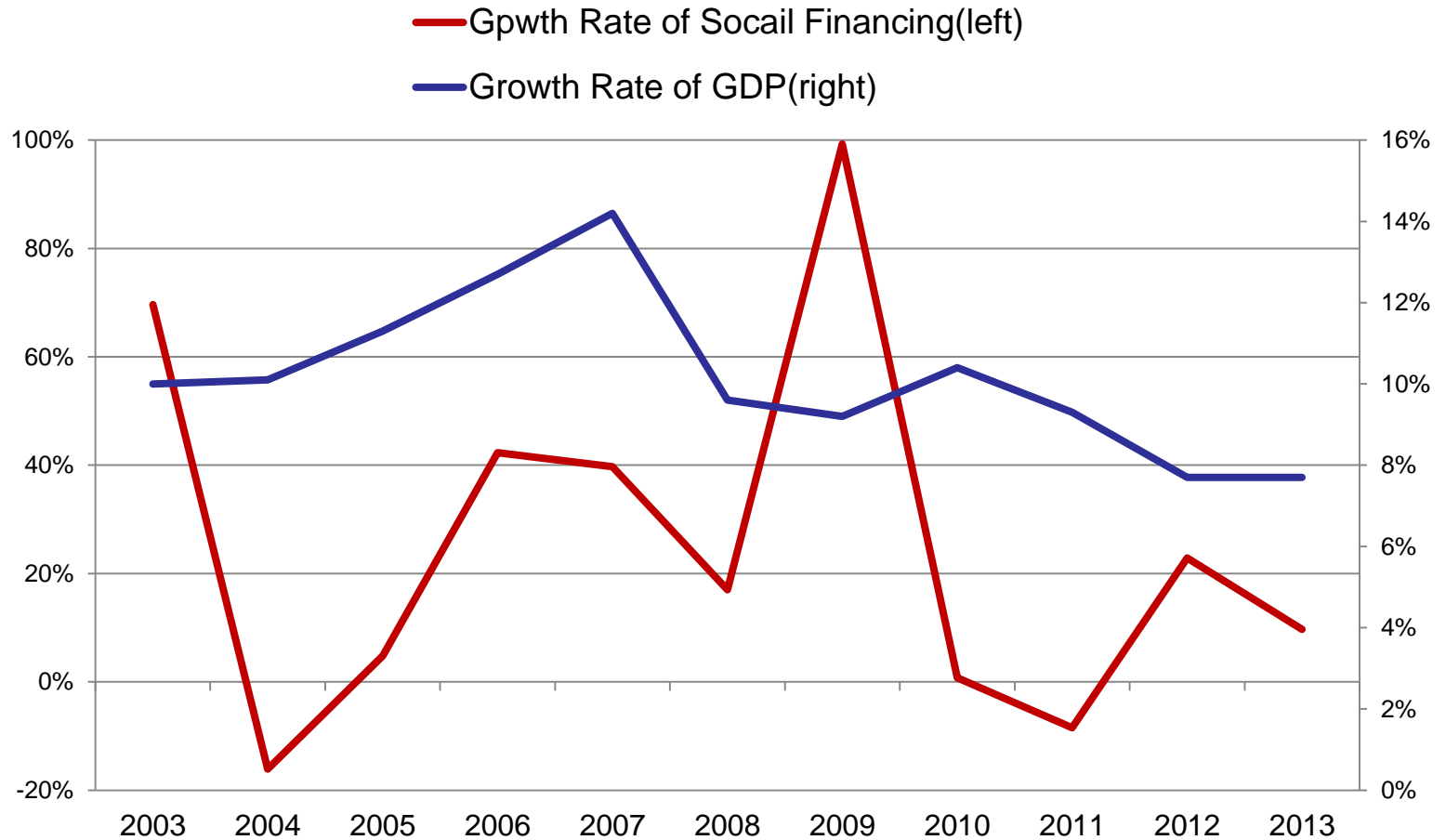
Source :National Bureau of China

Median GDP Growth Rate
(from 2000 to 2013)



Source :World Bank

Limits of the growth : signs of diminishing returns



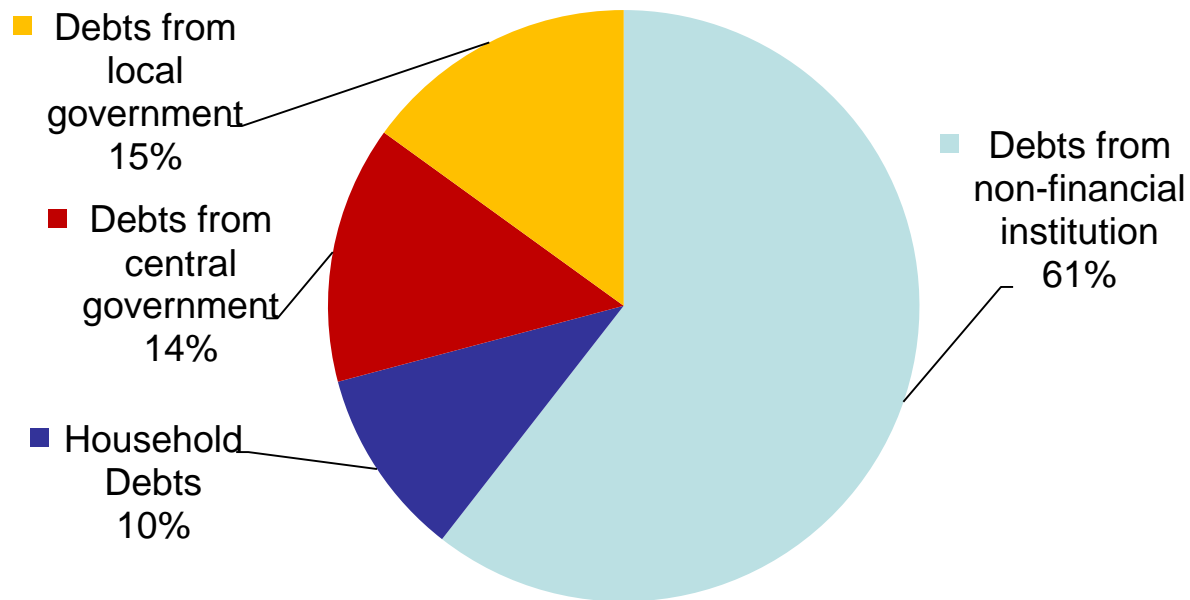
Source :National Bureau of China

Second, Financial risks are rising but still manageable. There is no possibility for hard-landing of Chinese economy and systematic financial crisis

Major financial risks in China:

1. Fast increasing in debt aggregate and leverage ratio of non-financial enterprises and local governments.
2. So along with slowing down of economic growth and slowing down of fiscal revenue growth, NPL of banking system has been increasing significantly since 2010. Local governments and industrial companies find more and more difficult to pay back principal and interest of their liabilities.
3. Asset bubble in real estate market is a very important concern.

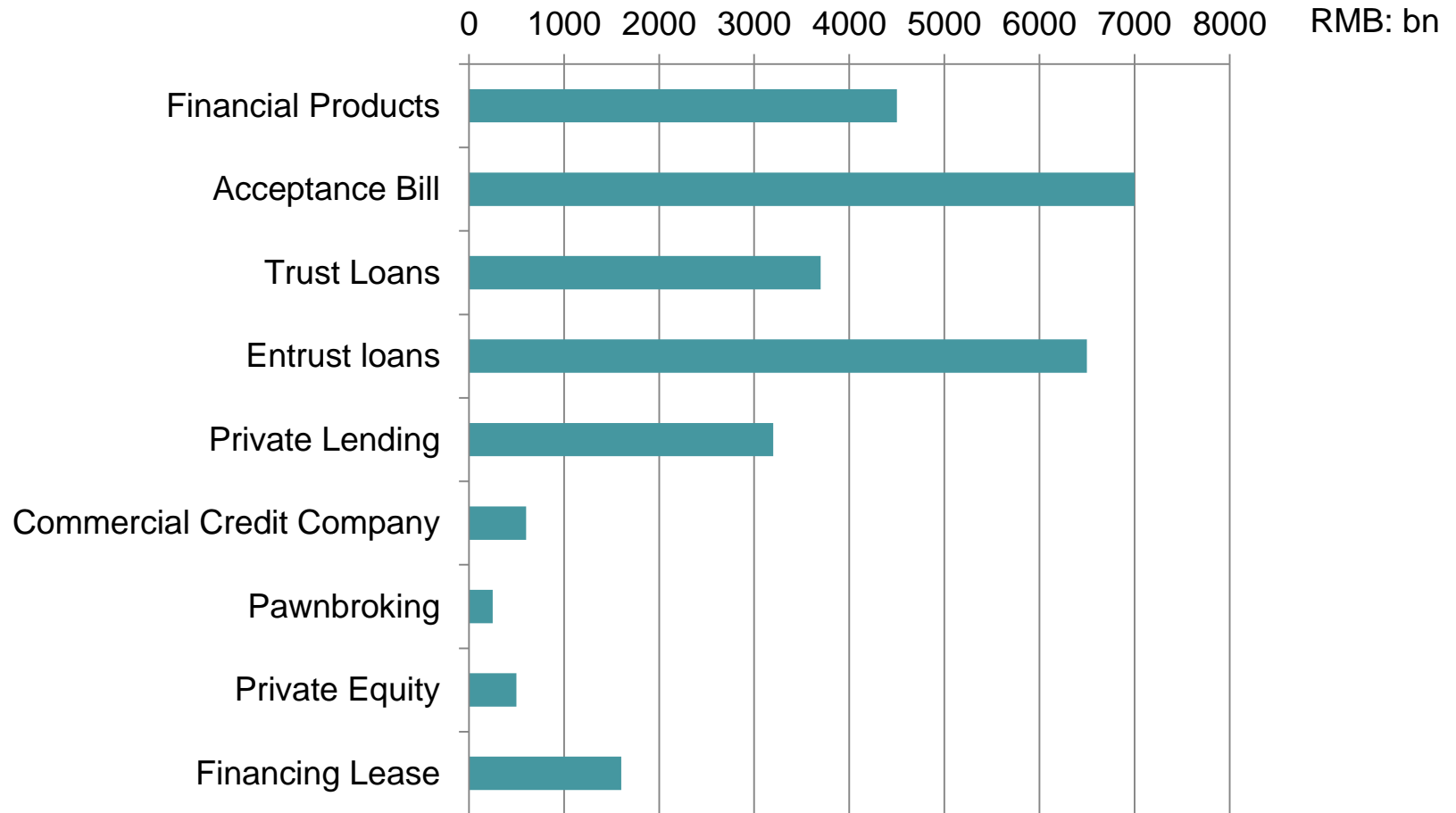
Debts in China's Economic System (As for debtors)



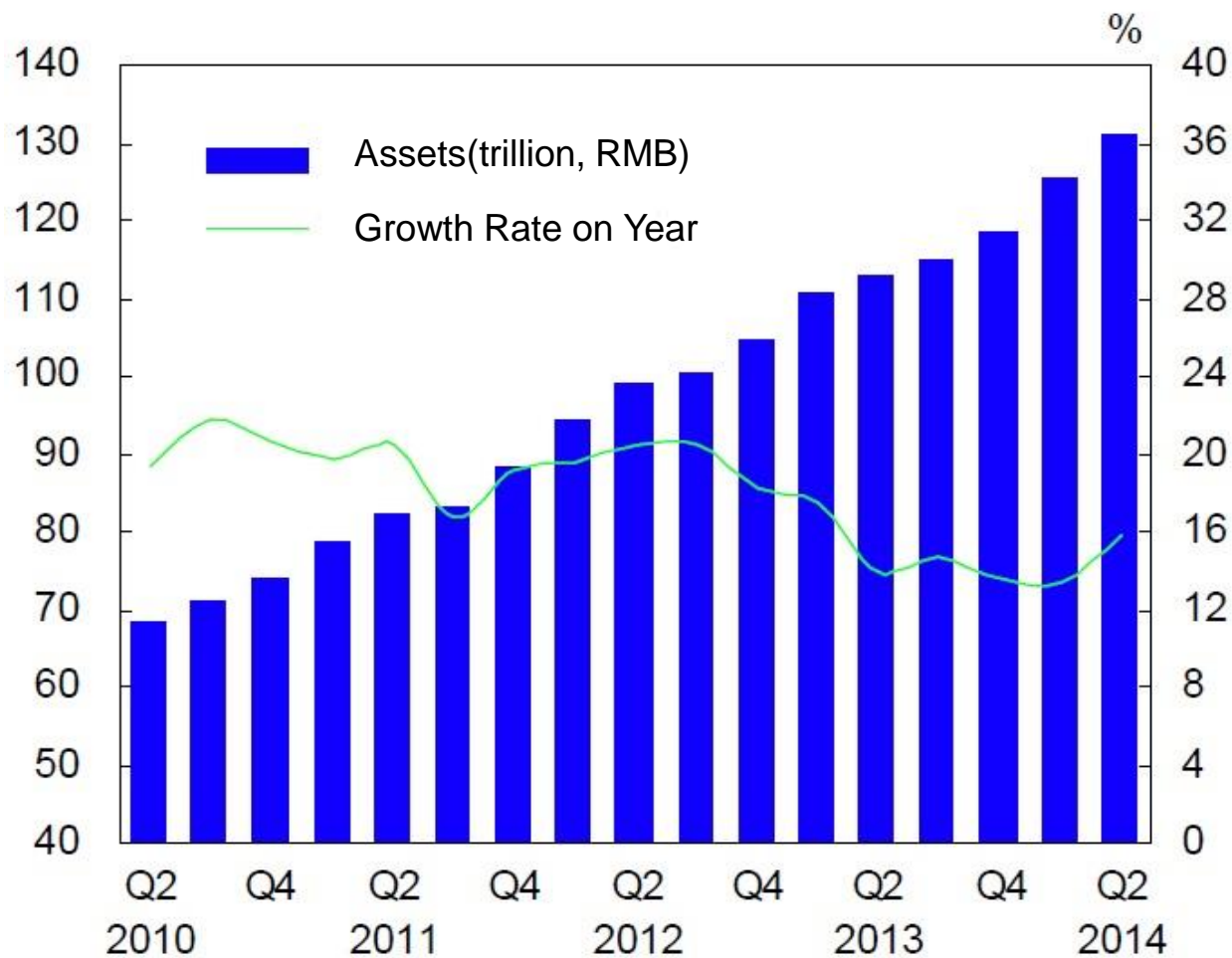
Source :The People's Bank of China & China Banking Regulatory Commission

$$\begin{aligned}\text{Debt} &= \text{Debts from non-financial institution (64.4t)} \\ &+ \text{Household Debts(11t)} \\ &+ \text{Debts from central government(15t)} \\ &+ \text{Debts from local government(16t—20t)} \\ &= 106.4—110.4\text{t}\end{aligned}$$

Composite of Chinese Shadow Banking System (roughly total: 27.8t)

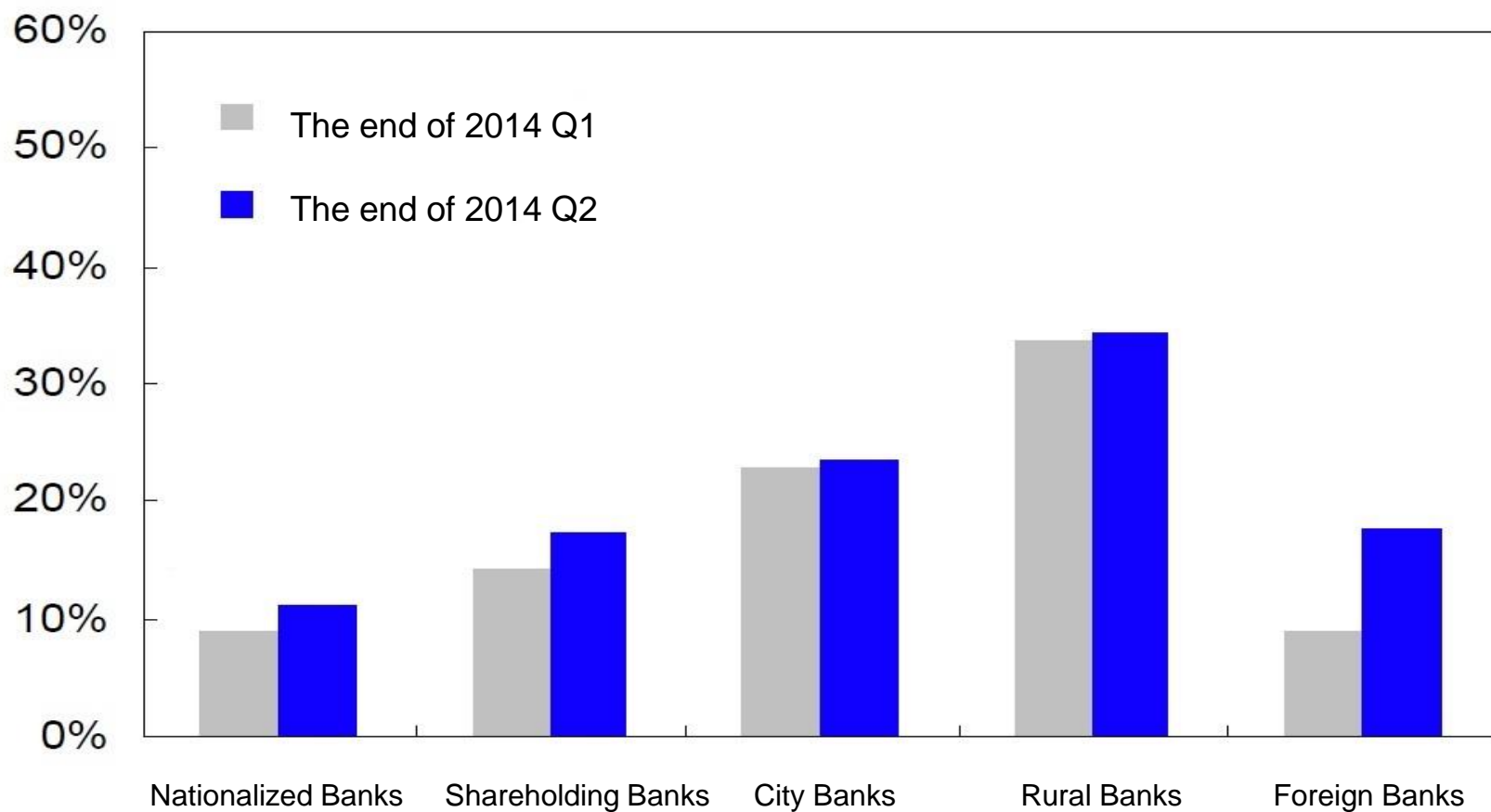


Growing Trend of Total Assets of Chinese Commercial Banking System



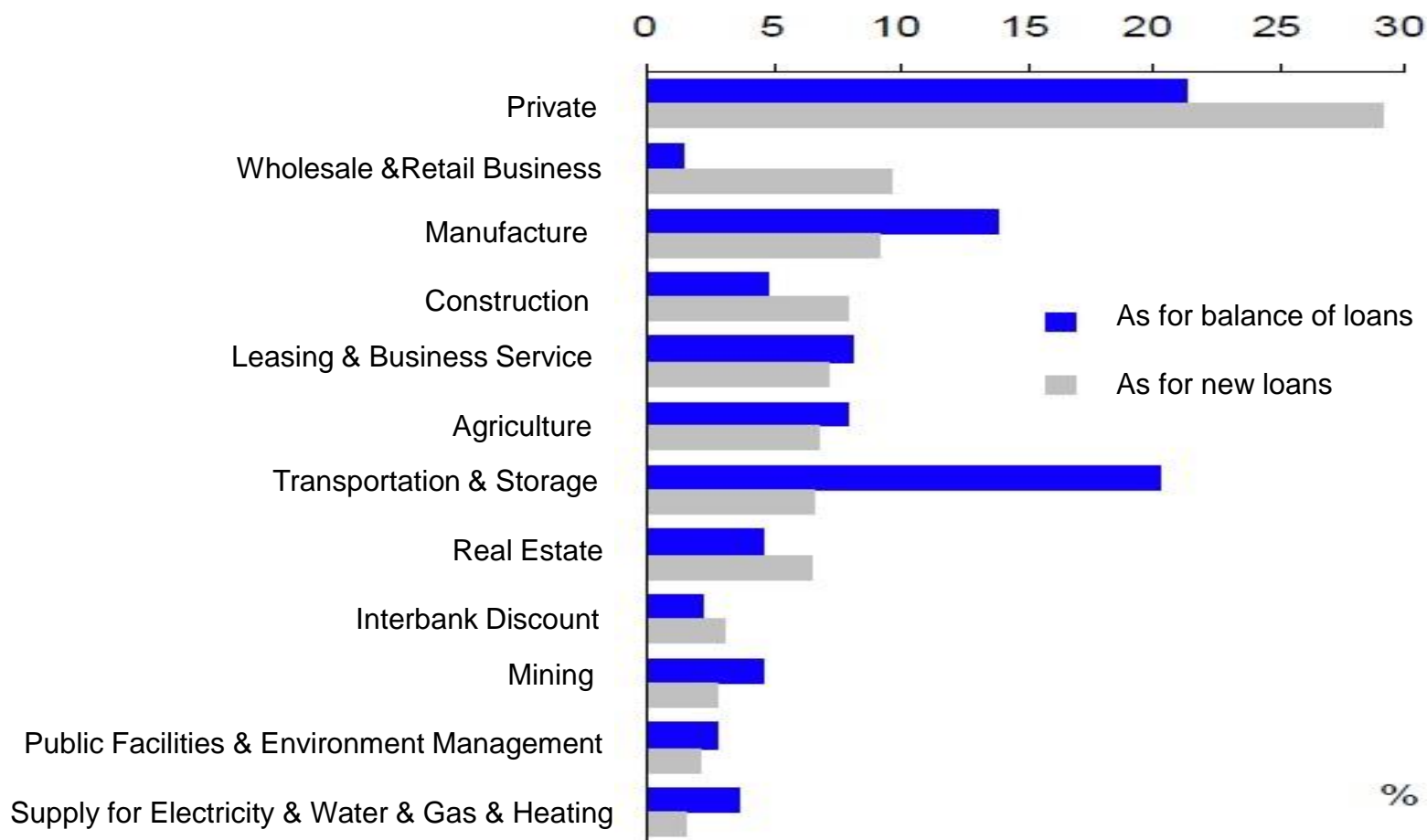
Source :China Banking Regulatory Commission

Growth Rates of Total Assets of Different Chinese Commercial Banks



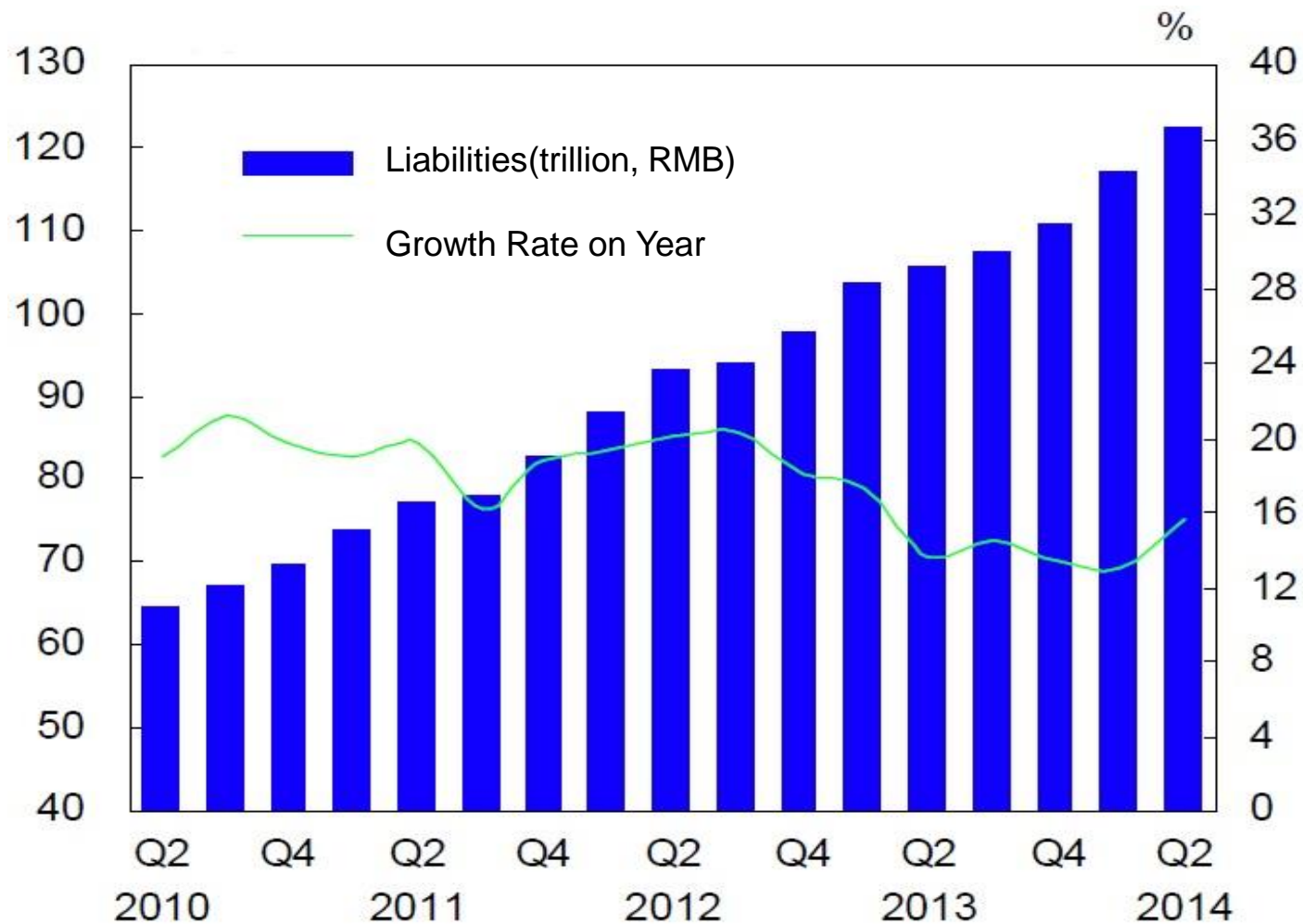
Source :China Banking Regulatory Commission

The Composite of Bank Lending(2014,Q2)



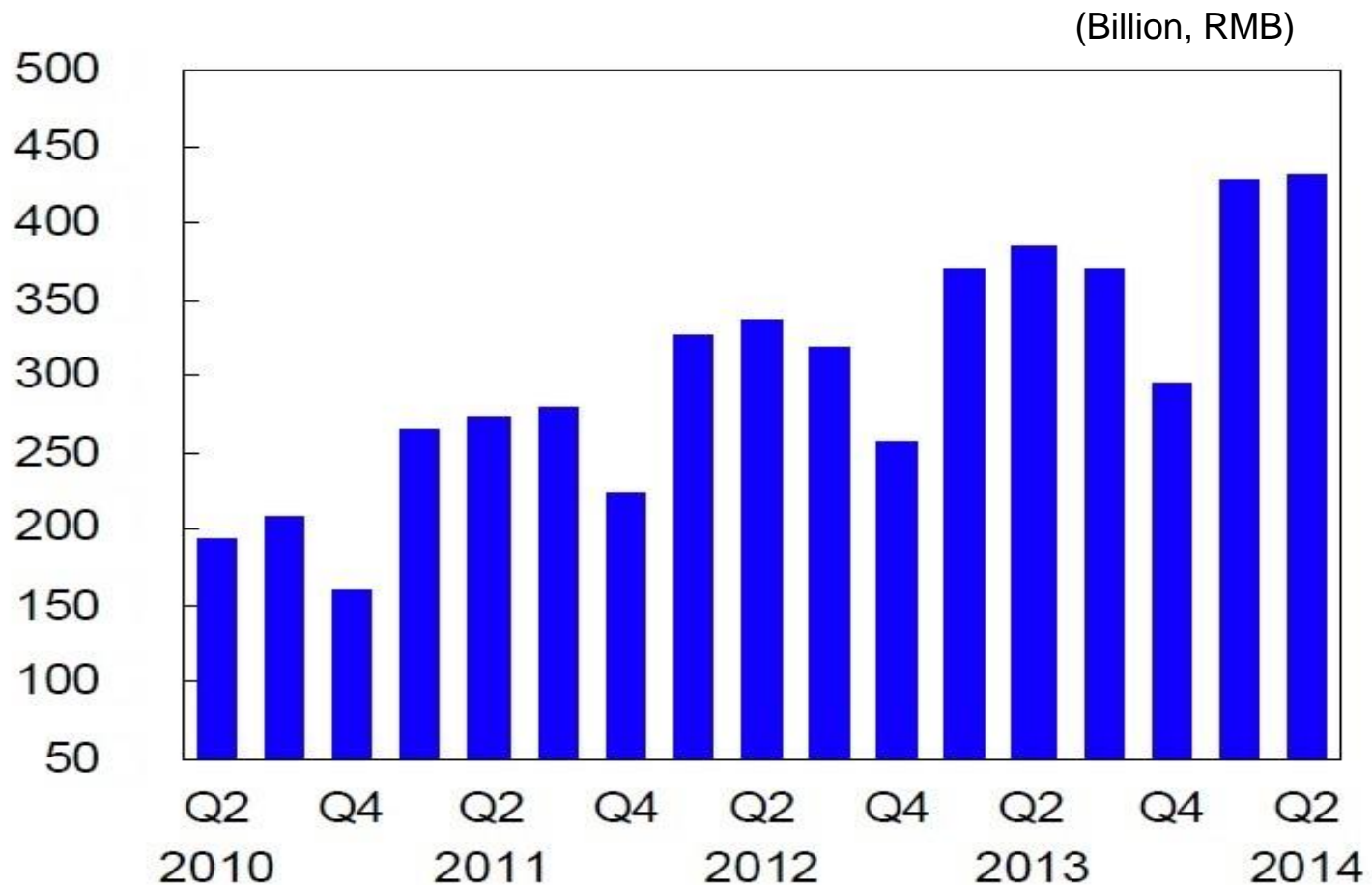
Source :China Banking Regulatory Commission

Growing Trend of Total Liabilities of Chinese Commercial Banking System



Source :China Banking Regulatory Commission

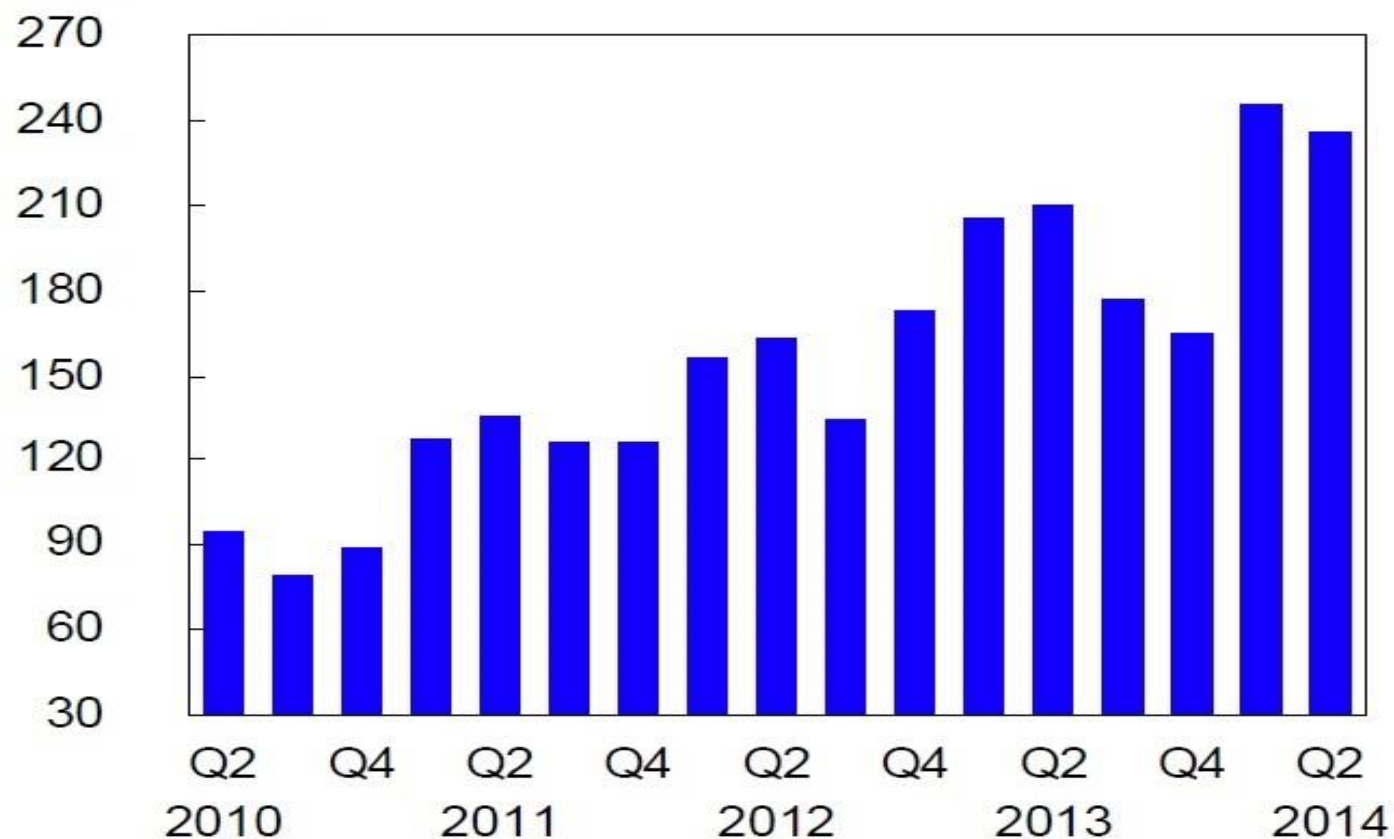
Total Net Profit of Chinese Commercial Banking System



Source :China Banking Regulatory Commission

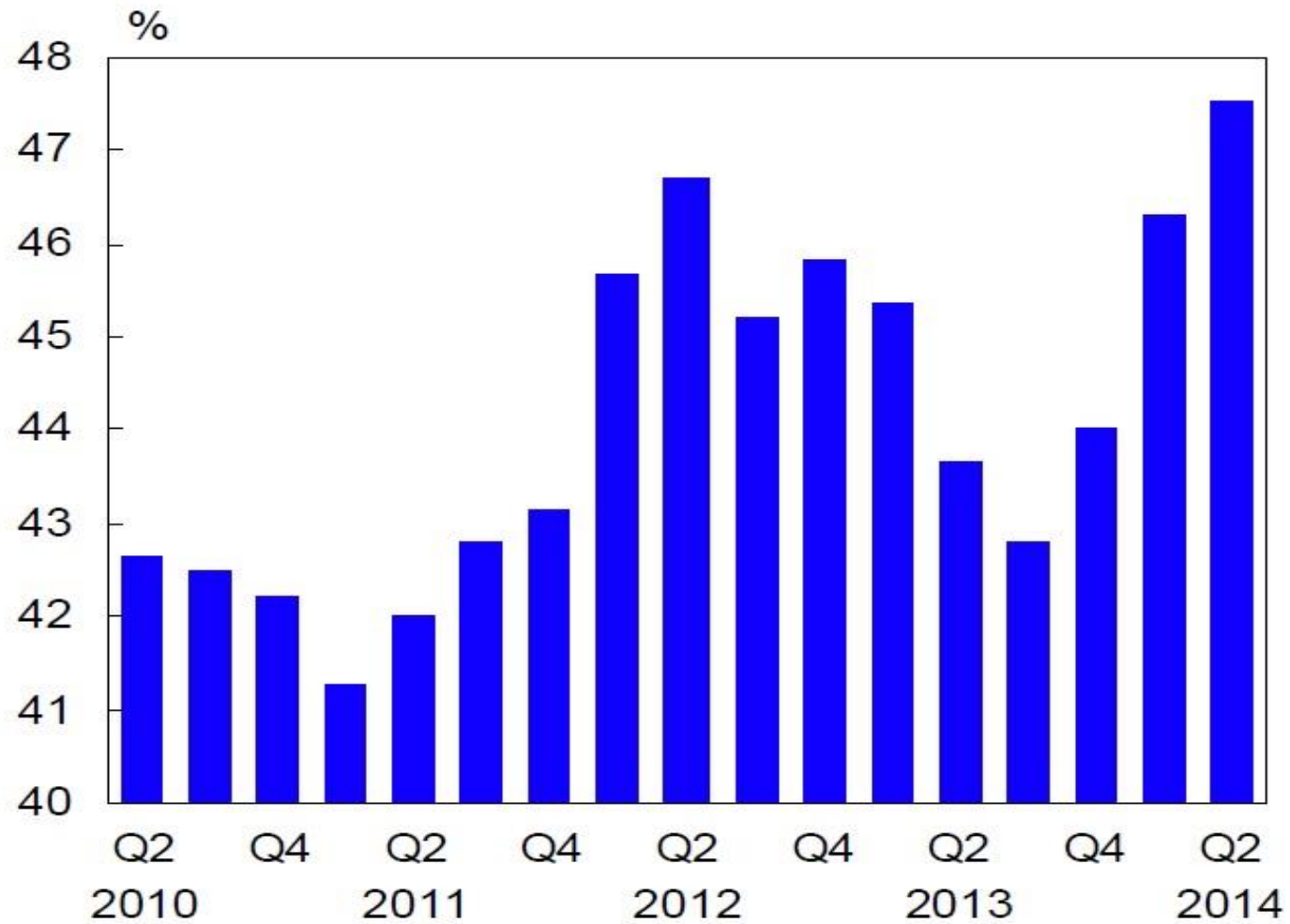
The Ratio of Non-interest Income to Total Income of Chinese Commercial Banks

(Billion, RMB)



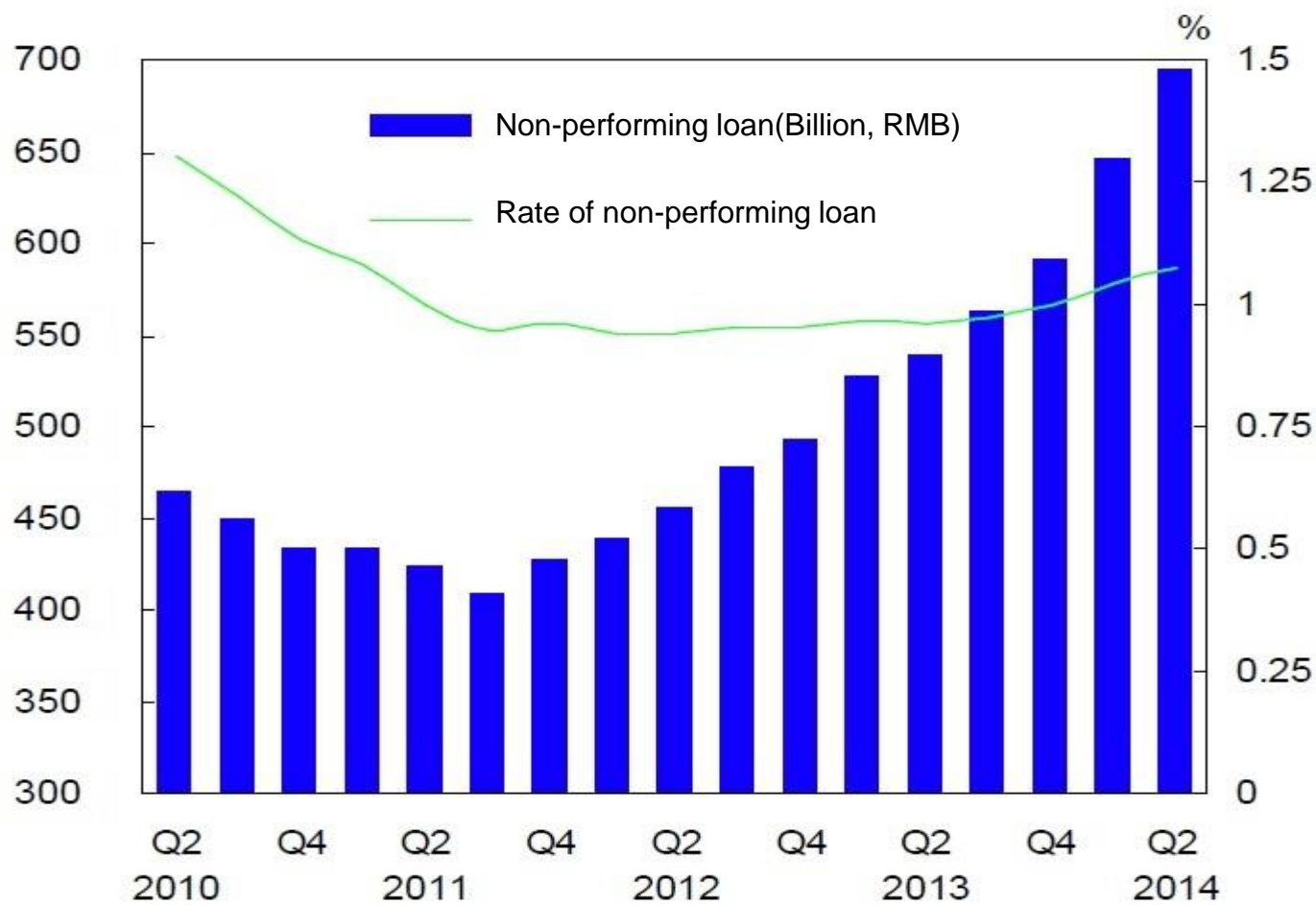
Source :China Banking Regulatory Commission

Liquidity Ratio of Chinese Commercial Banking System



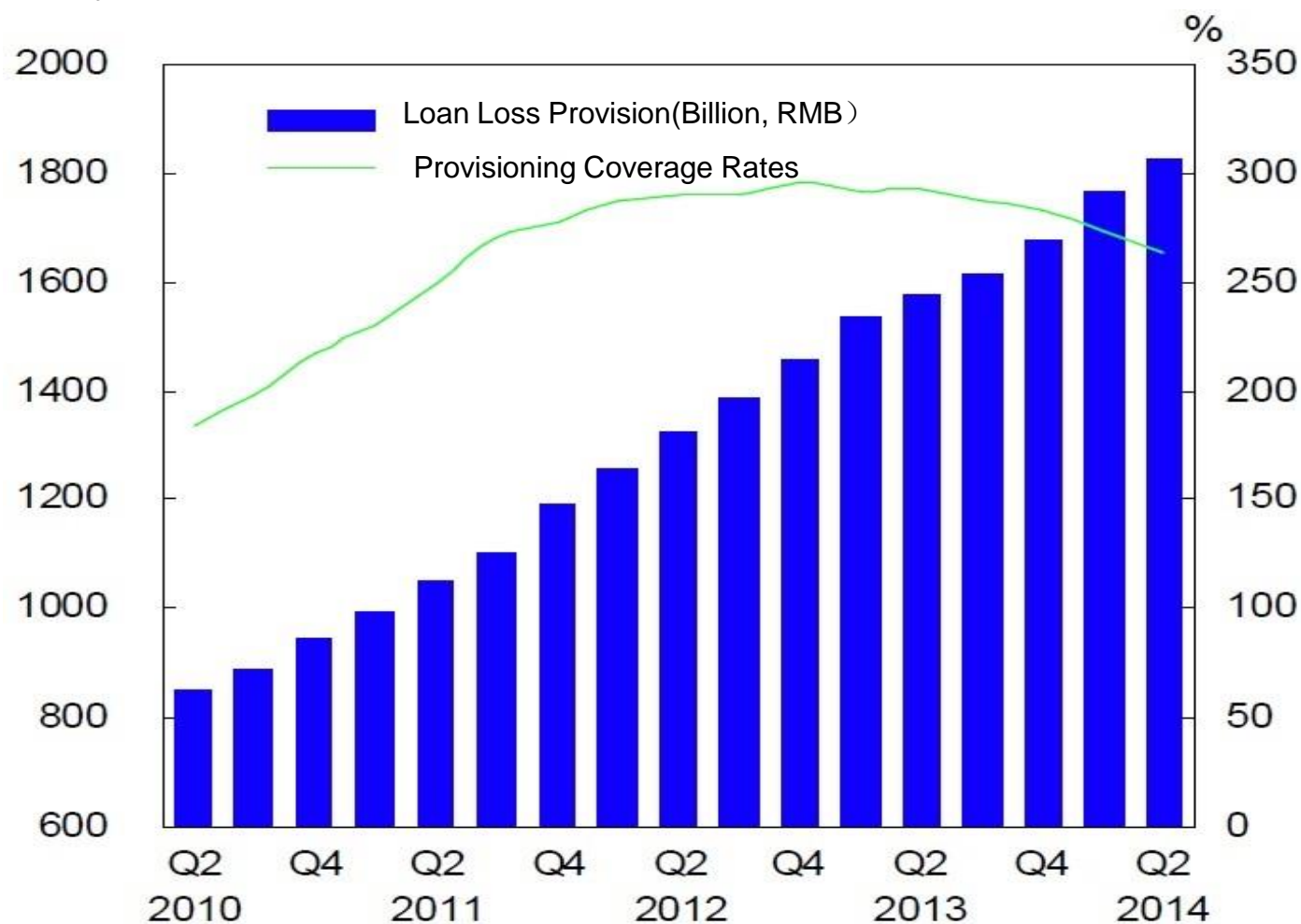
Source :China Banking Regulatory Commission

NPL ratio and NPL aggregate of Chinese Commercial Banking System



Source :China Banking Regulatory Commission

Loan Loss Provision of Chinese Commercial Banking System



Source :China Banking Regulatory Commission

Third, Financial reform and opening up is one of the top priorities on new government's economic agenda.

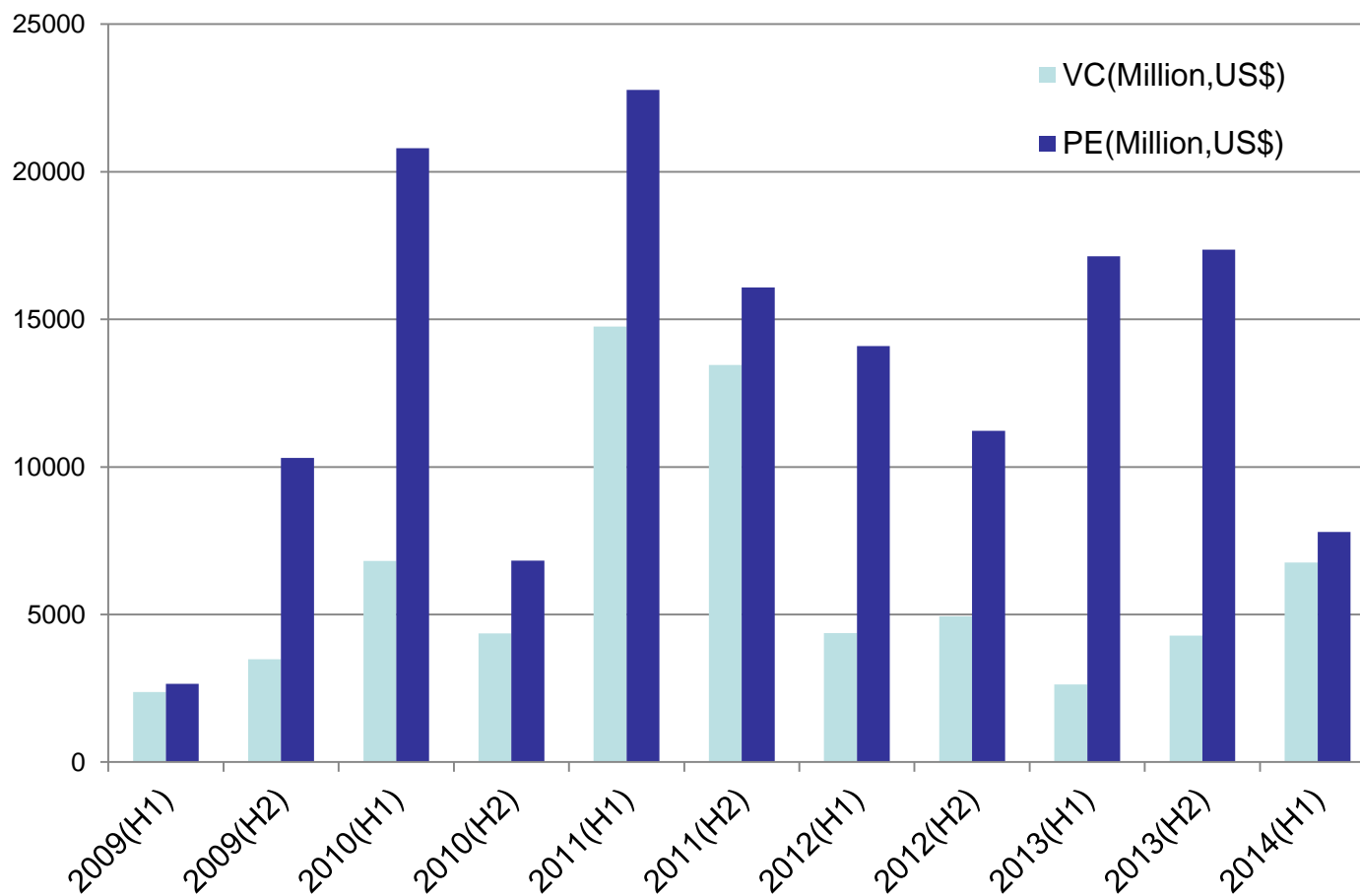
Major policy directions of Chinese financial reforming:

- I. Continue interest liberalization and exchange rate flexibility
- (1) establish deposit insurance facility very soon
- (2) enhance efficiency of interbank offering market
- (3) establish futures market for RMB
- (4) encourage more intensive competition in financial industry by reducing entry barrier for private capital into banking and other financial services.

II. Encourage direct financing such as PE. VC. Bonds Market. etc. to reduce reliance of social financing on commercial banking lending

- (1) PE.VC and alternative financing are booming in China.
- (2) Now incremental bank lending account for a little bit less than 50% of total incremental social financing (from more than 90% six years ago). Total outstanding bank lending still account for about 65% of total outstanding social financing.
- (3) Congress will approve new law about VC, PE and alternative financial tools very soon.

The statistics for new capital flowing into VC&PE markets



Source :Zero2IPO Group

III. Promote Capital Account Convertibility and encourage overseas investment by Chinese individuals and enterprises.

(1) Preconditions for capital account convertibility are actually mature.

(2) Shanghai (and other cities) Pilot Free Trade Area is very significant in this regard.

(3) Increasing international use of RMB requires capital account convertibility and two-way flows of RMB funds.

IV. Promote international use of RMB and multinational business of Chinese financial institutions.

- (1) Expand further RMB trade settlement.
- (2) Expand volumes of Currency Swap with other countries.
- (3) Promote offshore RMB markets in HongKong, London, Singapore, etc.

Thank you for your attention!