

Financial Risk in China

Peterson Institute for International Economics

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2015 Chinese Stock Market Turbulence



The New York Times | <https://nyti.ms/1K01hkg>

Opinion | OP-ED CONTRIBUTOR

False Alarm on a Crisis in China

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By NICHOLAS R. LARDY AUG. 26, 2015

Washington — CHINA, many believe, is in a financial and economic meltdown causing anxiety and panic everywhere. China's stock market dive first dragged down other emerging markets and has now spread to the United States, slicing trillions of dollars off the value of stocks traded here and in other global markets. Since China is the world's second largest economy and has growing financial ties around the world, developments there clearly have enormous potential implications for both developed and emerging markets.

Exchange Rate Policy Revision in 2015

Aug 11th, 2015 PIIE China Economic Watch



CHINA ECONOMIC WATCH

China's Latest Currency Actions Are Market Driven

Nicholas R. Lardy (PIIE)
August 11, 2015 4:15 PM

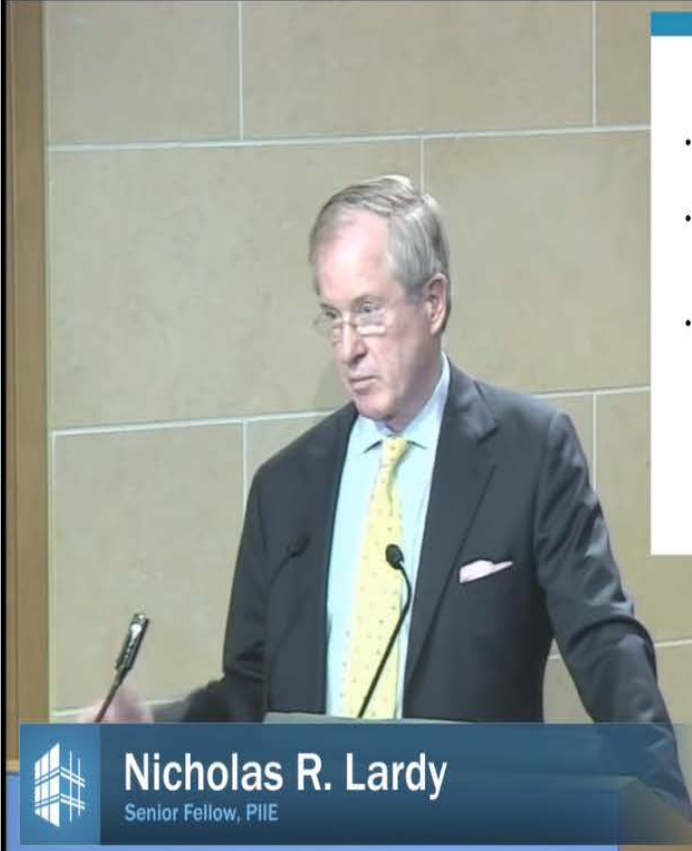
China's central bank took a potentially major step toward a more market-determined exchange rate on August 11, when it announced a revision in the process for fixing the central parity exchange rate, the starting point for daily trading of the renminbi (RMB) in the onshore market.

While the reform has set off alarm bells in some quarters, it is unlikely that this move will usher in another chapter of currency manipulation to support Chinese exports and thus its economic growth. China may well be concerned about an economic slowdown accompanied by a slump in exports, but its motivation for this move is almost certainly tied to another objective: China's aspiration to have the RMB join the four



The Decline in China's Foreign Exchange Reserves

April 11th, 2016 Spring Global Economics Prospects




←

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Takeaways

- Services and consumption are likely to remain the major drivers of China's economic growth.
- The assertion that authorities will engineer a large step devaluation of the currency to prevent a further economic slowdown is not well founded.
- The view that the decline in China's foreign exchange reserves is because panicked mainlanders are desperately seeking ways to get money out of the country is misinformed. Rather, the decline largely reflects the unwinding of the renminbi carry trade and Chinese companies paying off dollar debt, both of which are self-limiting. Thus the market is unlikely to force a large currency depreciation.

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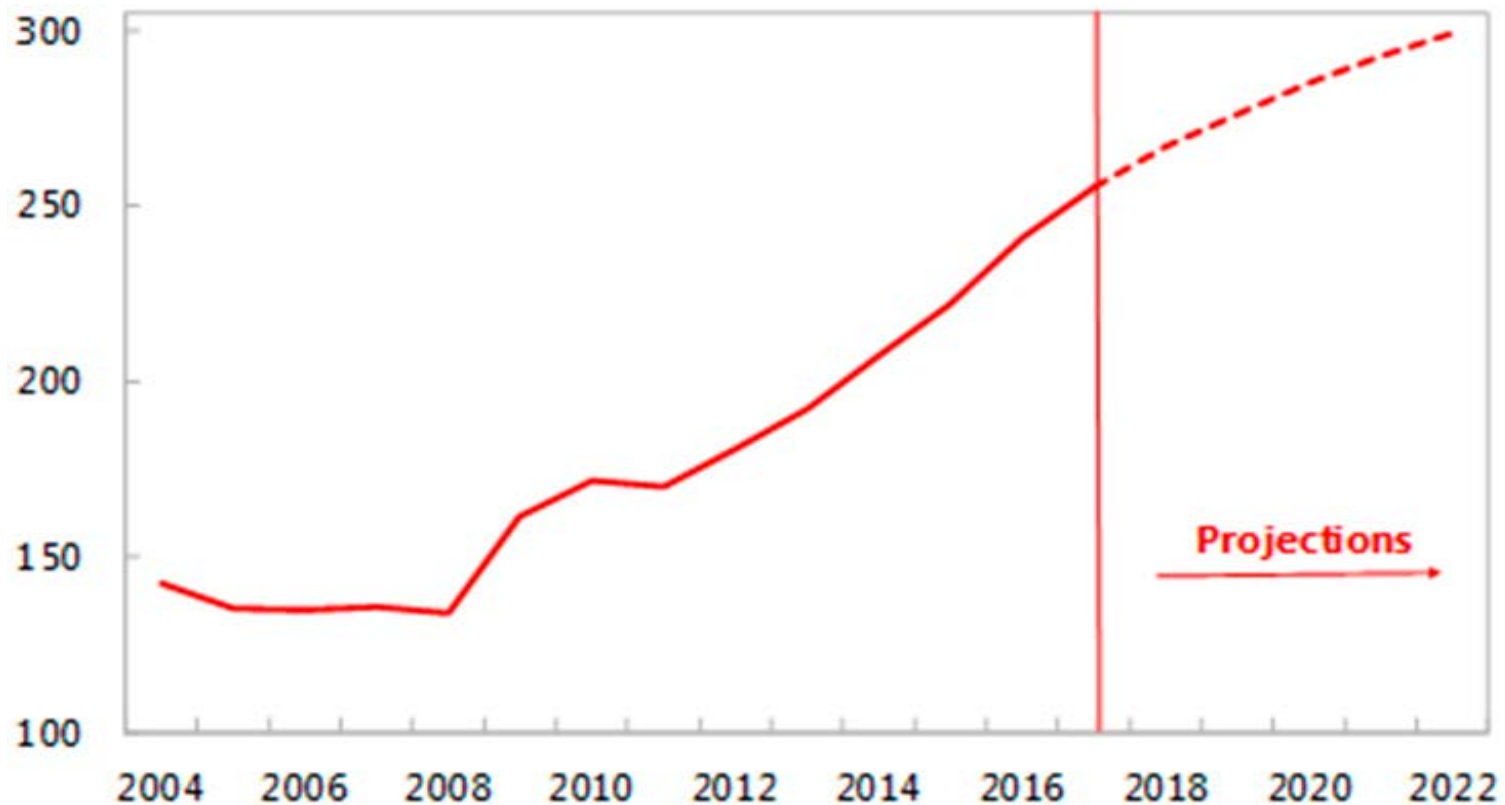
Nicholas R. Lardy
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Non-Financial Sector Debt, 2004 – 2022



Non-Financial Sector Debt: High and Rising

(In percent of GDP)



Sources: Haver Analytics; and IMF staff estimates.

Aug 22th, Financial Times



Chinese Economy

Focus on financial risk puts China on a more sustainable path

The leadership seems to accept slower growth as price of moderate credit expansion



Steps have been taken to raise short-term interest rates © Reuters

AUGUST 22, 2017 by Nicholas Lardy



Xi Jinping's Speeches on Financial Risks

Occasions	Time
Central Economic Work Conference	December 2016
The 15 th meeting of the Central Leading Group for Financial and Economic Affairs	February 2017
Meeting of the Political Bureau of the CPC Central Committee	April 2017
The 40 th group study of the Political Bureau of the CPC Central Committee	April 2017
National Financial Work Conference	July 2017
Meeting of the Political Bureau of the CPC Central Committee	July 2017

National Financial Work Conference: Xi's Remarks



- Guarding against systemic financial risks is the eternal theme of financial work and the government should take stronger initiative to monitor, warn against and deal with risks in a timely manner.
- China will accelerate developing laws and regulations governing the financial sector, improve macro prudential management and emphasize functional as well as behavioral regulation.
- the government will continue to deleverage the economy by firmly taking a prudent monetary policy and prioritizing reducing leverage in state-owned enterprises.
- China will control local government debt growth, crack down upon financial irregularities and improve supervision on Internet finance.

National Financial Work Conference: Setup of a New Committee

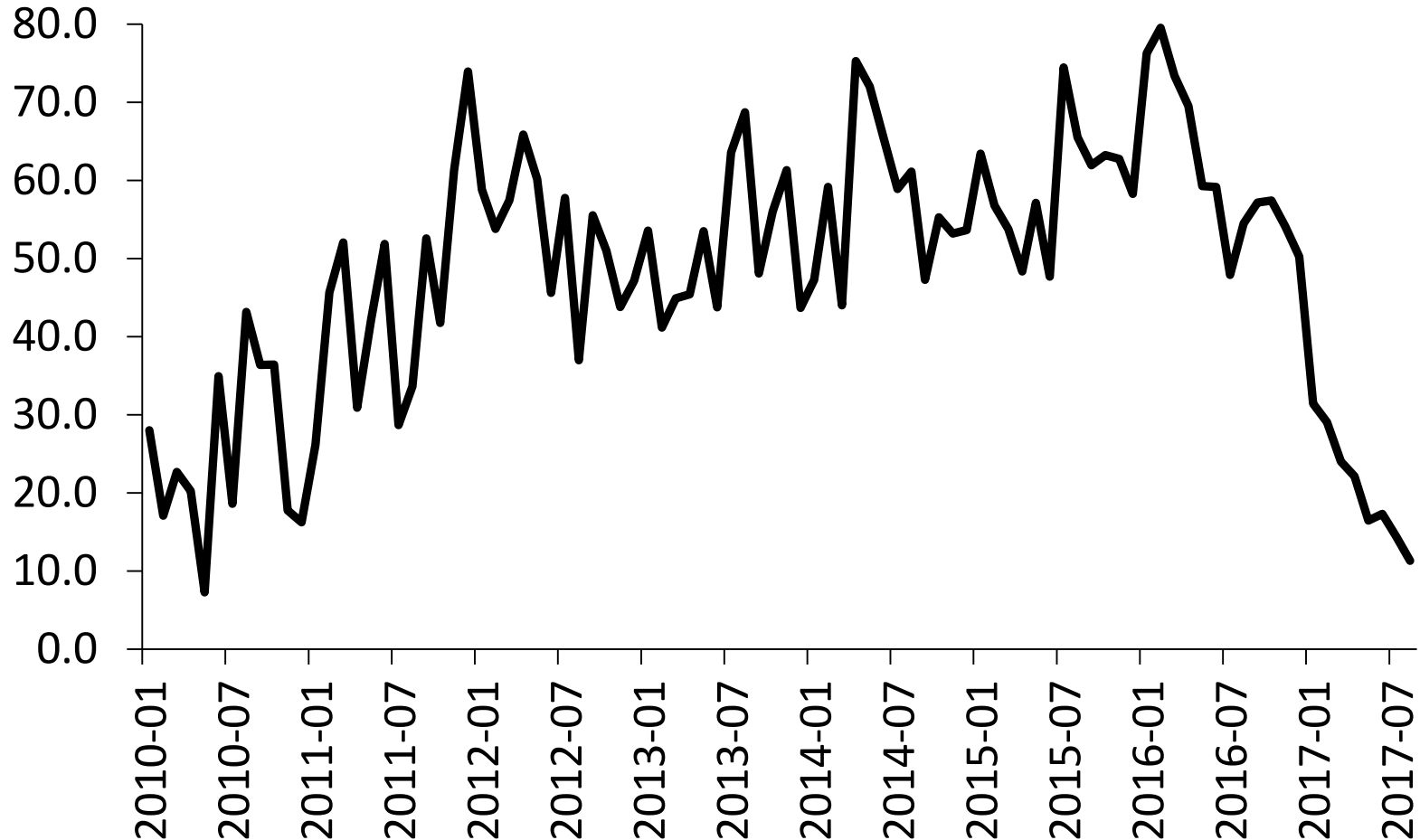


- The State Council Financial Stability and Development Committee
- Responsible for the coordination of the country's financial reform, development and regulation
- Target weak links in supervision and guard against systemic risks to ensure the sound development of China's financial system and help it better serve the real economy

Interbank Market Lending, 2010 Jan – 2017 Aug



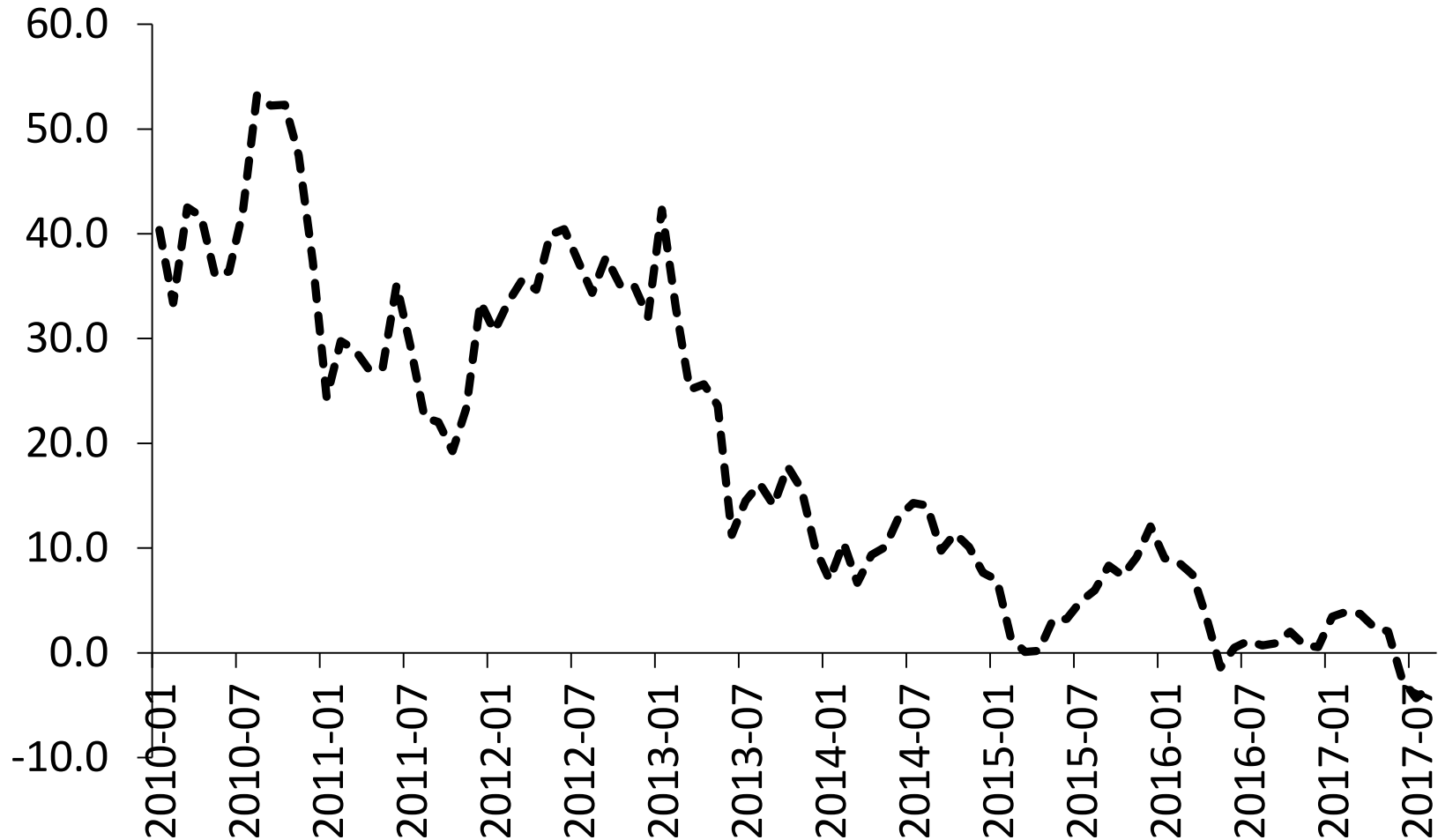
% (year over year)



Bank Claims on Non-bank Financial Institutions, 2010 Jan – 2017 Aug



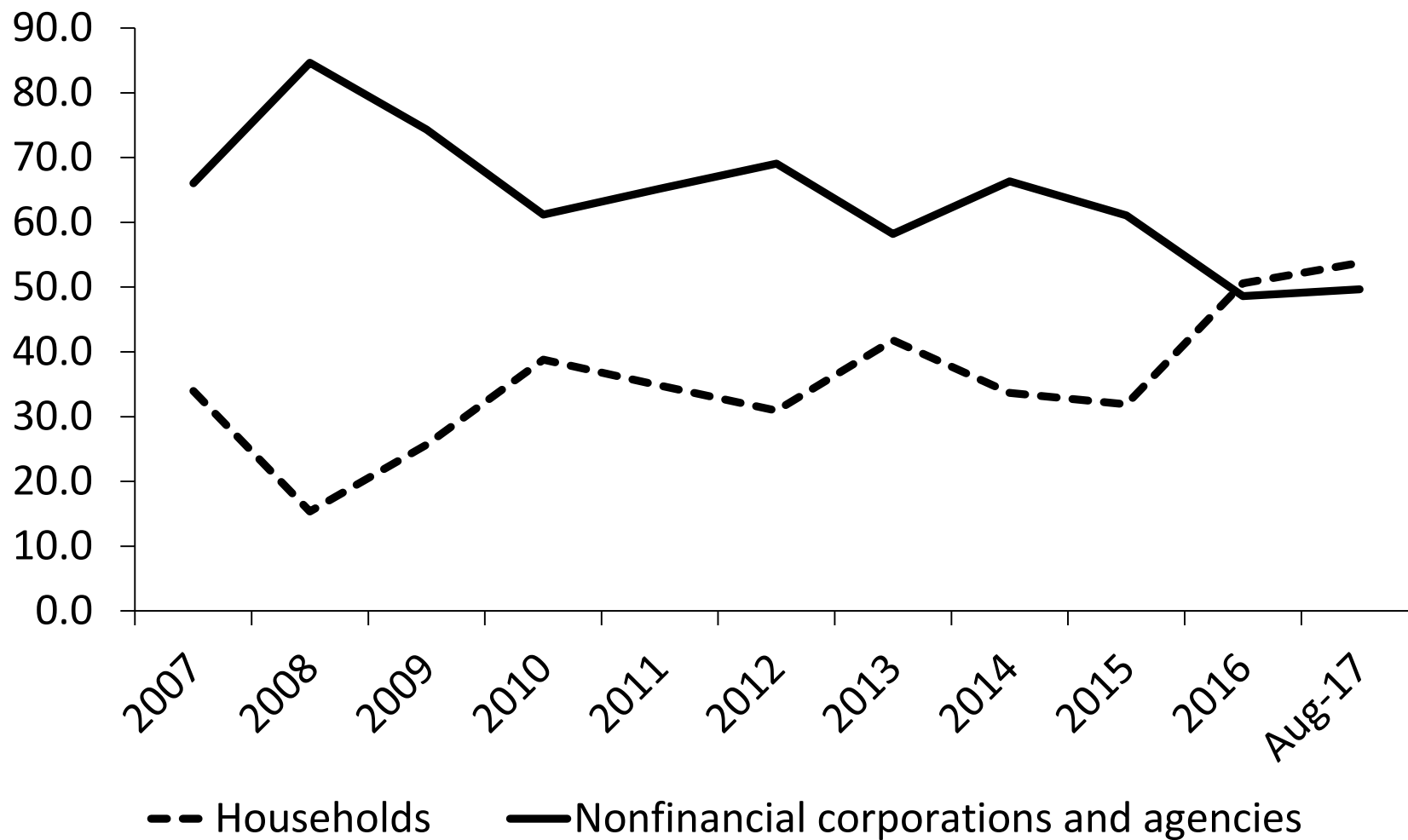
% (year over year)



Share of New RMB Loans by Sector, 2007 – 2017 Aug



% (year over year)



Anbang: Regulatory Crackdown



Billions of renminbi

180.0
160.0
140.0
120.0
100.0
80.0
60.0
40.0
20.0
0.0

%

90.0
80.0
70.0
60.0
50.0
40.0
30.0
20.0
10.0
0.0

2015 1H

2016 1H

2017 1H

■ investment products ■ share of total premium revenues (right axis)

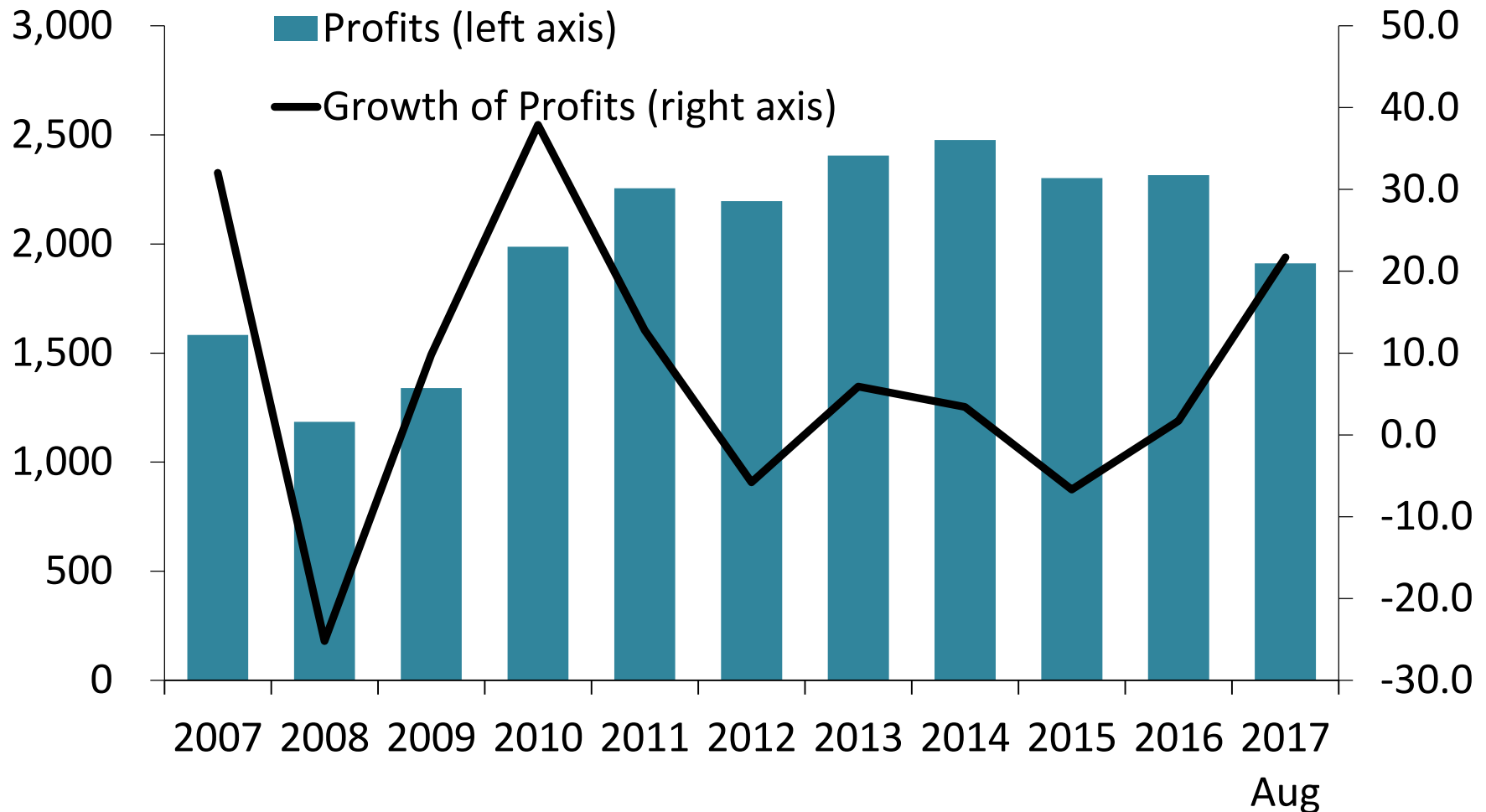
Sources: China Insurance Regulatory Commission

Profits of State-owned Enterprises, 2007 – 2017 Aug



Billions of renminbi

% change, year over year



Takeaways



- The rapid growth of corporate debt poses risks
- This risk has been acknowledged by China's top leader and regulators have responded vigorously
- Interbank lending, particularly to non-bank financial institutions, is shrinking
- Share of RMB lending to less leveraged households is rising, to more leveraged corporates is falling
- Major risks in the insurance sector are being addressed
- Profitability of SOEs, the most highly leveraged of corporate borrowers, is recovering
- Key question remains-if growth slows from here will ultra-rapid credit growth resume?