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Session 2

Current Assessment:

Impacts of Global Financial Turbulence on Financial Systems in
China and Australia - 全球金融动荡对中国和澳大利亚金融体系的影响

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I am not well familiar with the Australian financial system so I think my Australian colleagues will be better qualified to comment on the impacts of the global financial turbulence on the Australian financial system. I will focus my comments on the impact of this global financial turbulence on China's financial system. But I hope that some of my reflections will to some extent also have something useful to offer to the Australian financial authorities.

During the discussion at the first session this morning, I focussed on analysing the factors contributing to instability, both global and in the Asia-Pacific region. I will now give an analysis of the main aspects of the effects on China's financial system of the financial crisis brought about by the American sub-prime lending crisis.

1. Direct Financial Losses

The losses experienced in China's financial sector because of the sub-prime lending crisis principally fall into three categories. The first are losses arising from the falls in the prices of sub-prime loan products; fortunately Chinese banks did not purchase large amounts of these products. Only a limited number were bought by banks such as the Bank of China, and they were made public from a very early stage and counter measures were adopted. As a result, after absorbing the corresponding losses sustained in the first half of 2008, they still netted a good profit.

The second are losses arising in connection with Fannie Mae and Freddie Mac. It is well-known that following the US Treasury Department's taking control of the two companies, foreign investors' bond investments in these two companies received protection; only the value of shares in the two companies saw large falls. Happily, Chinese financial institutions did not buy their shares, or if they did, I am confident that it was only a small number.

The third category of losses arose from some China financial institutions having investments

in American financial products under the QDII scheme, and although the quantities were not large, the majority of the investments performed badly.

2. Indirect Effects

A) The slowdown in American economic growth will make the global macro-environment unfavourable, and the Chinese economy will be affected, directly and indirectly. China financial institutions will now be very prudent about foreign investments, particularly regarding near term investments in America.

B) The American sub-prime lending crisis has shattered the belief that American financial markets are the world's safest. People will think anew about American investments, will make a fresh evaluation of the risks of the American financial markets, and will tend to invest in relatively low-risk financial products. This will have an impact on the overall level of China financial institutions' foreign investment profits.

C) The large depreciation of the US dollar against currencies such as the Euro will increase revaluation pressure on the Renminbi, and the interest rate difference between China and America has increased the difficulties for China's currency authorities applying currency policy instruments.

D) Following the sub-prime lending crisis, people began to examine and review other financial derivative products, such as CDSs, in fine detail. CDSs alone have a notional value of 62 trillion US dollars, while sub-prime loans are generally estimated to be on a scale of 1.2 trillion US dollars. The sub-prime lending crisis and other events will have an unavoidable impact on the development of China's financial derivative product market.

3. Regulatory Aspects

The sub-prime lending crisis has led people to give deep thought to the service rendered by America's financial regulatory authorities: why had there been no awareness of the looming crisis before it erupted? Had the warning mechanisms designed beforehand been of any use? These questions will spur China's financial regulatory sectors to implement more stringent effective regulation. Governance issues in some rating companies have also become more glaringly obvious: does formulating international criteria for rating companies merit discussion?

Following the Asian financial crisis, the Chinese government has devoted vigorous efforts to overhauling the financial sector, and resolved problems with the financial sector's non-performing assets; several major state-owned banks have absorbed foreign strategic investors, adopted shareholding system reforms, and successfully listed on the stock exchange. The Chinese government has also vigorously developed the financial market; promoted capital market development, and strengthened financial regulation. It is constantly improving and fine-tuning financial laws and regulations, and has greatly enhanced the risk resistance capacity of China's financial system. As a result, although America's sub-prime lending crisis and turbulence on the international financial markets have had negative impacts on China's economic and financial development, the risk resistance capacity of China's financial institutions is already much stronger than it was ten years ago, and they will continue to develop in this turbulent environment.