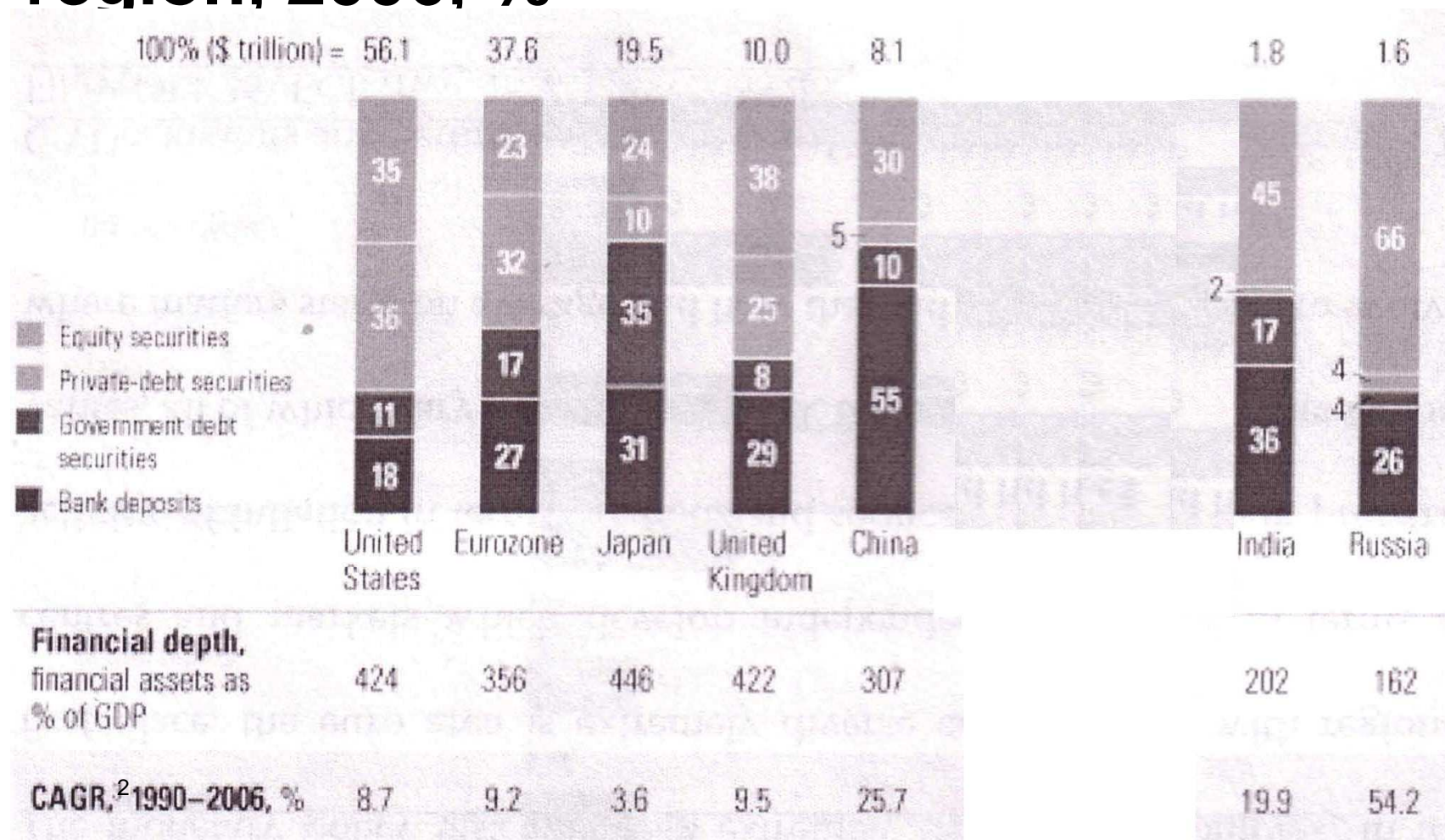


China and Financial Reform

Howard Davies
Director

October 2008
Beijing, Chevening Alumni
Lecture, British Embassy

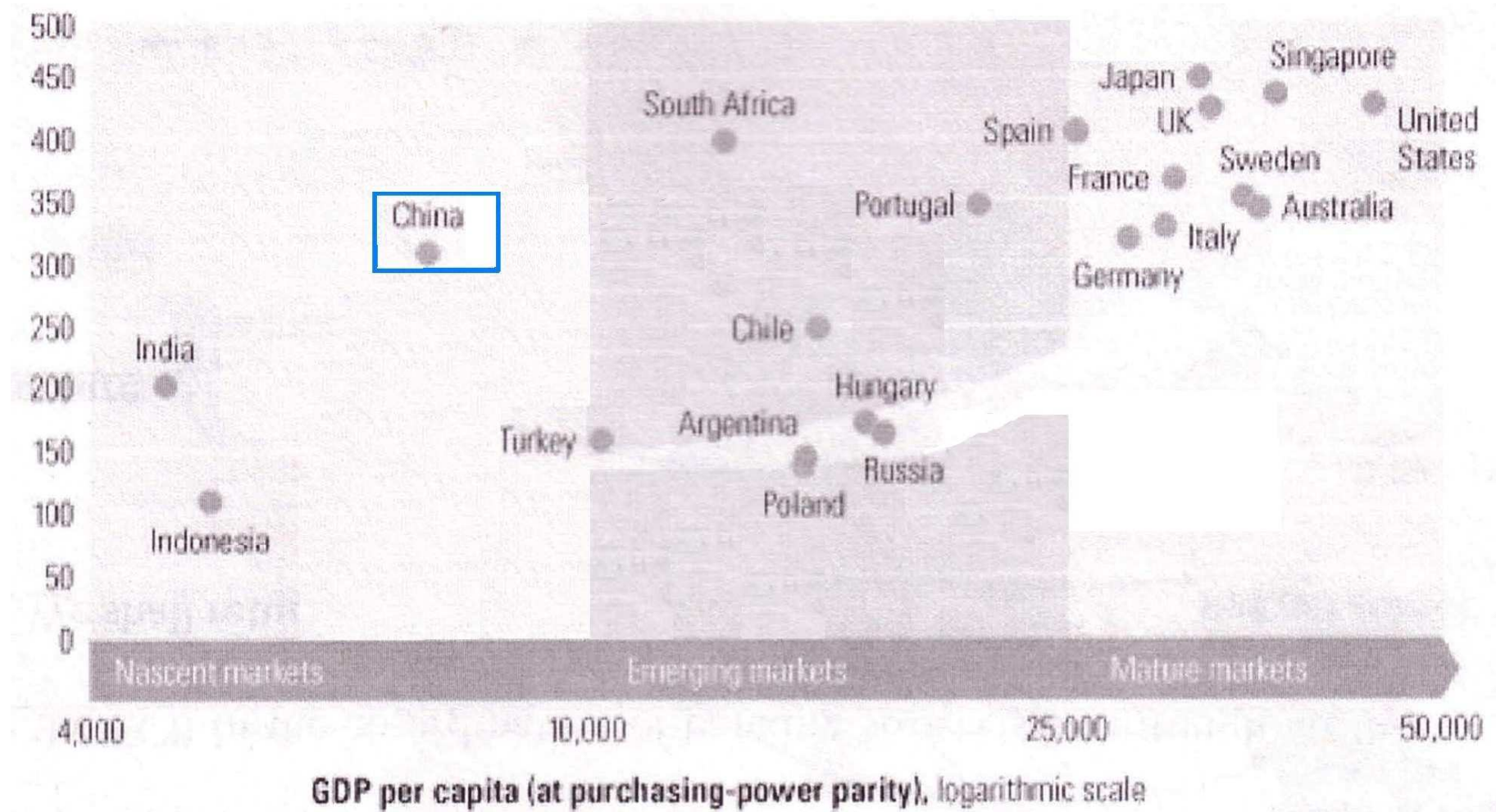
Distribution of financial assets by region, 2006, %



1 Figures may not sum to 100%, because of rounding

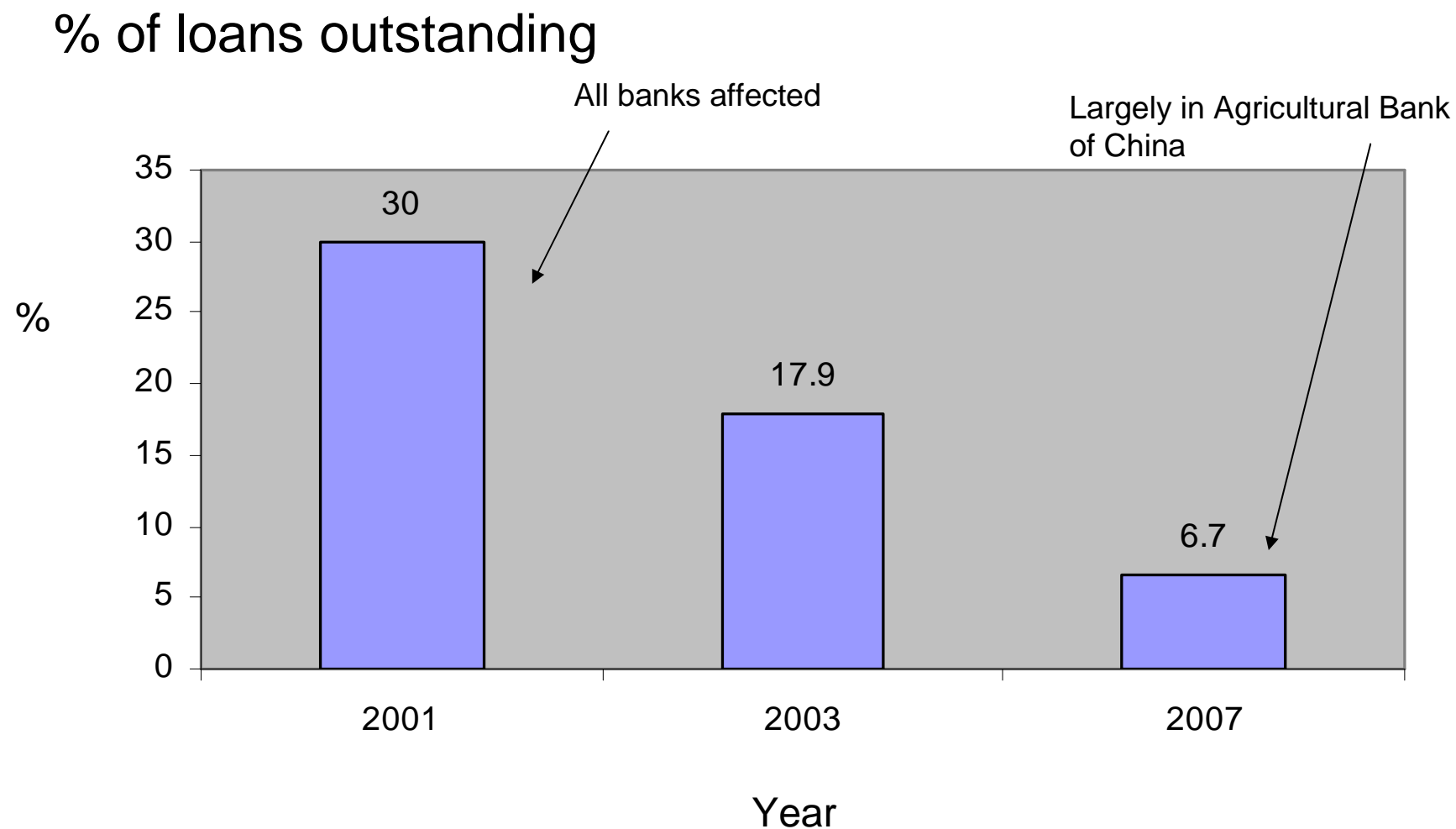
2 Compound annual growth rate constant 2006 exchange rates

Value of bank deposits, bonds, and equities as % of GDP



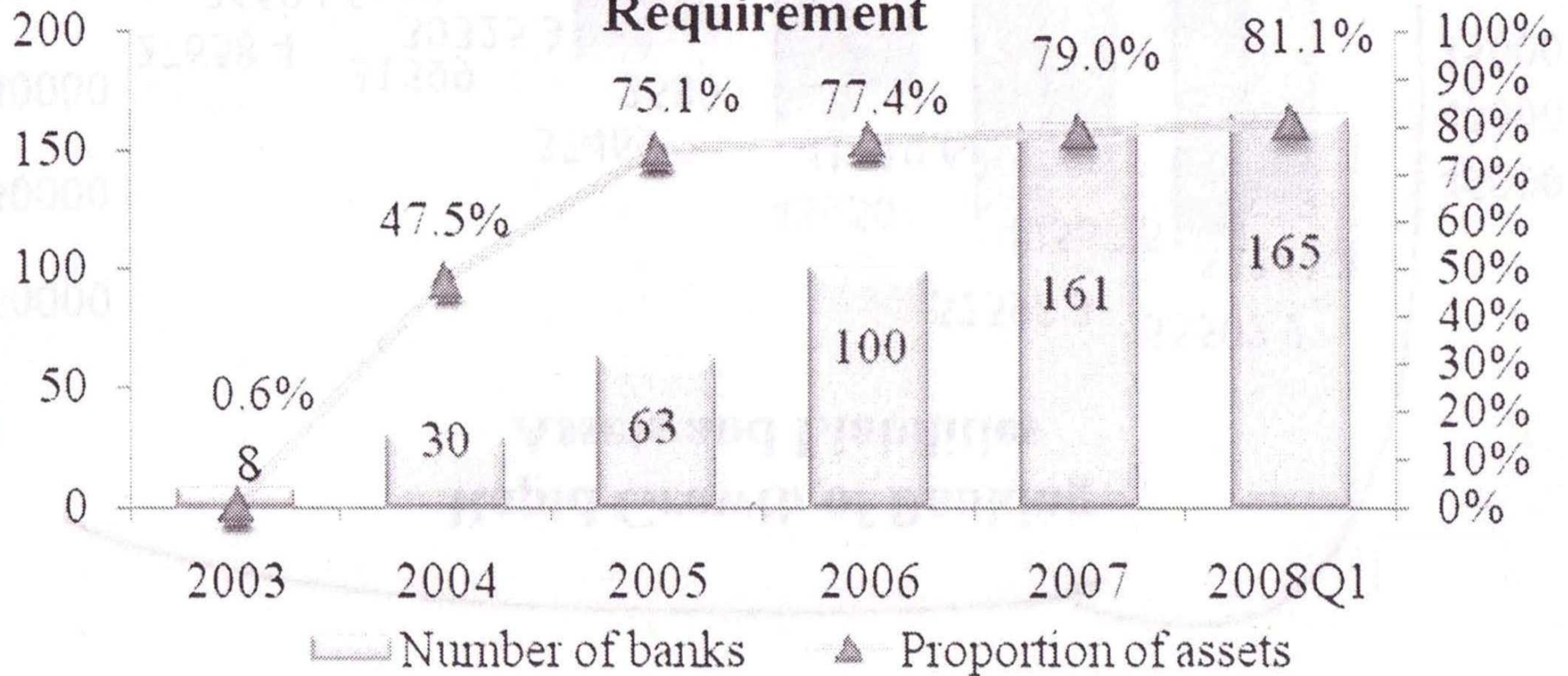
Source: McKinsey Global Institute global-financial stock database

Non-Performing Loans (CBRC Figures)

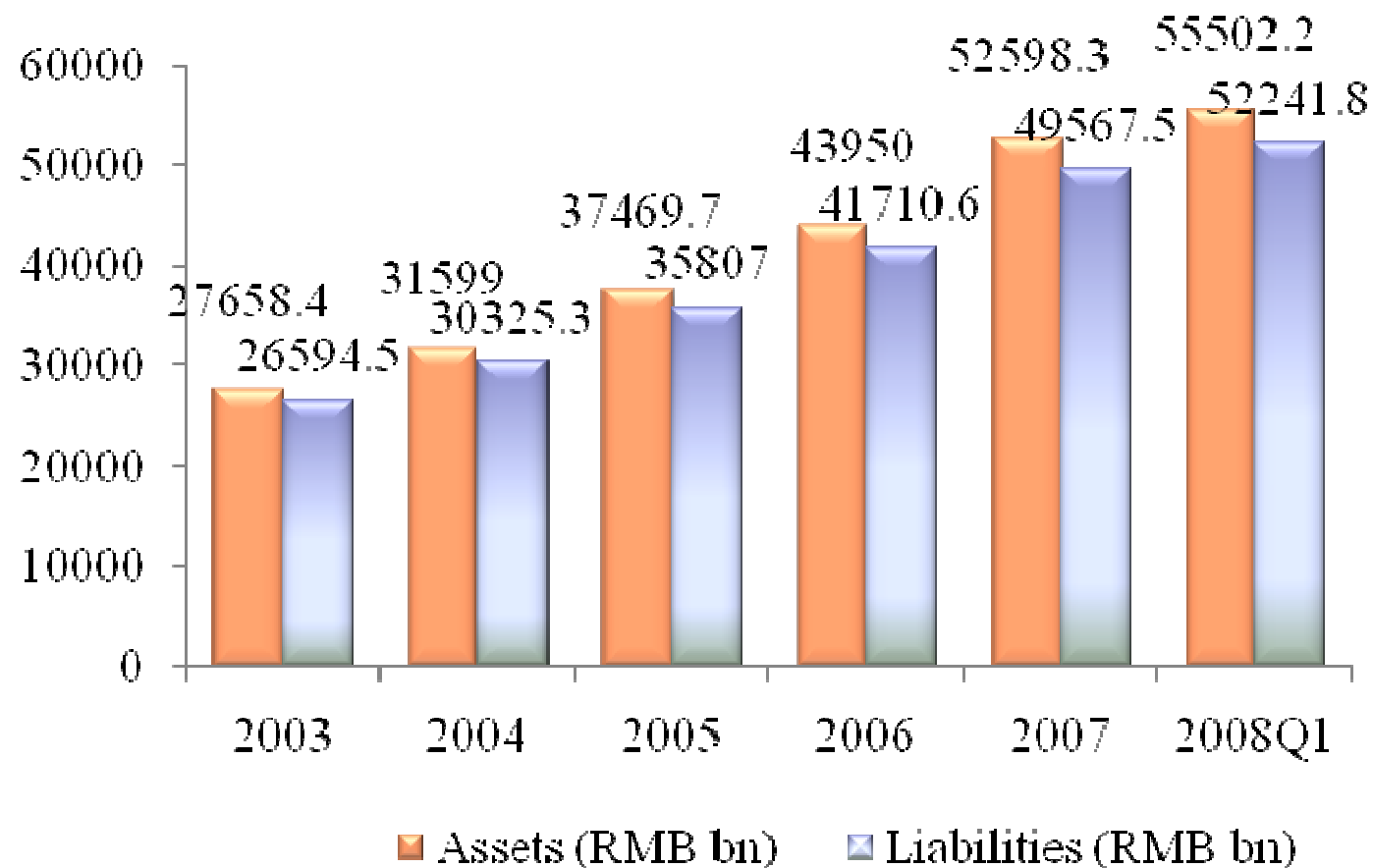


Share of banking assets in banks meeting capital adequacy standards

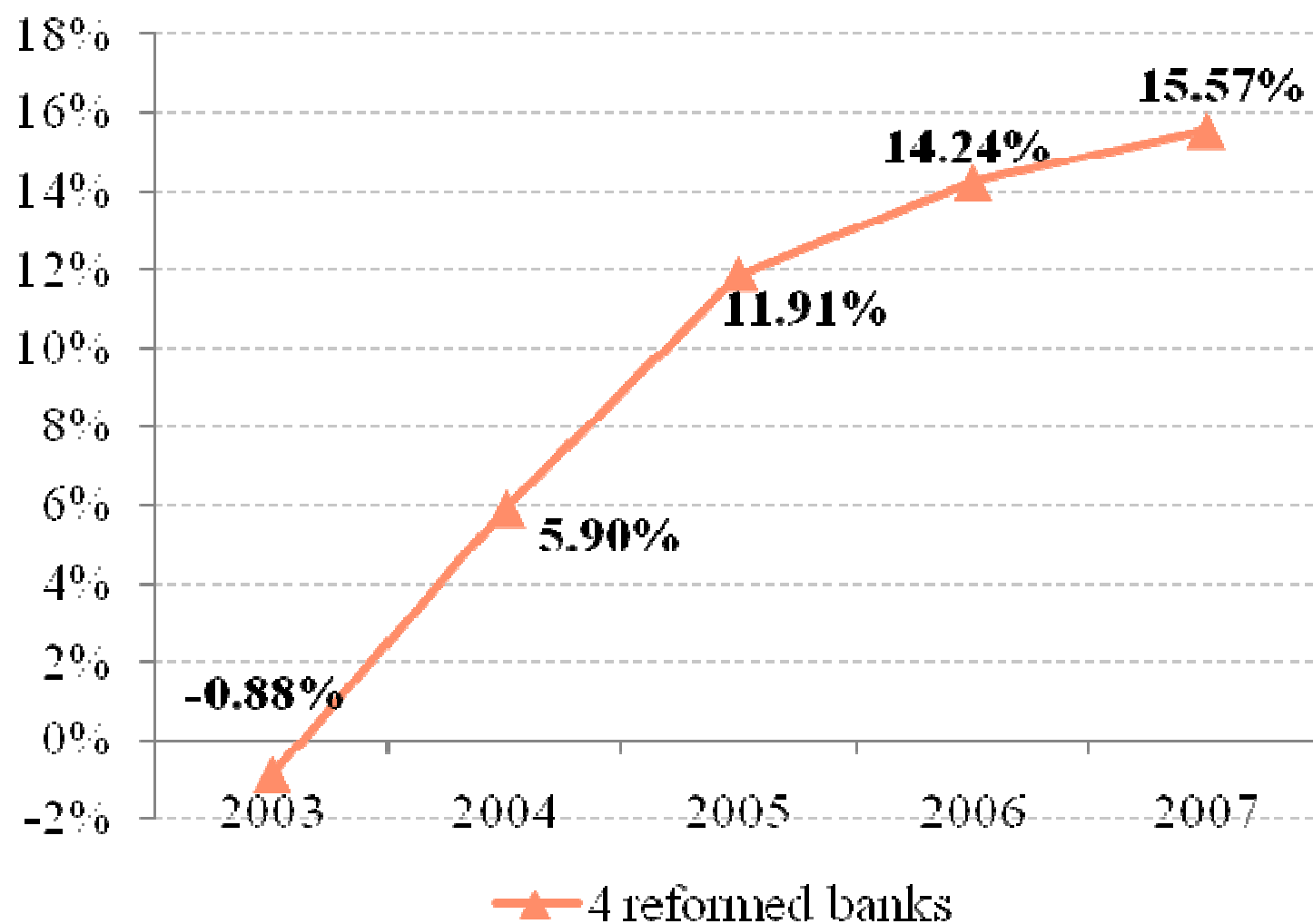
Numbers and Share of Banks Meeting the CAR Requirement



Rapid Growth of Banking Assets and Liabilities



ROE



Foreign Banks in China

Impressive expansion....

24 foreign bank subsidiaries (119 branches)

2 joint venture banks

71 foreign bank branches (117 offices)

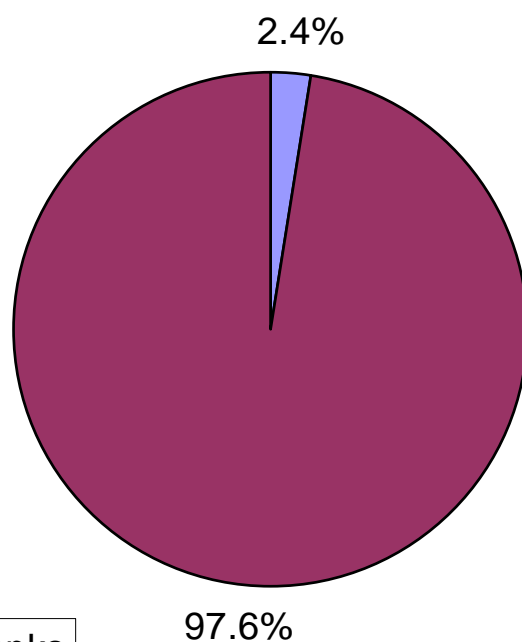
Total assets (end 2007)

\$171 billion (+ 45% yoy)

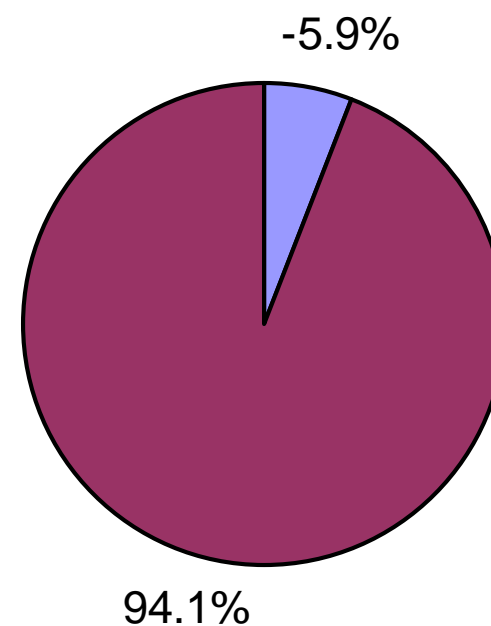
Loans \$95 billion (+ 62% yoy)

...But still modest market share

Assets



Capital

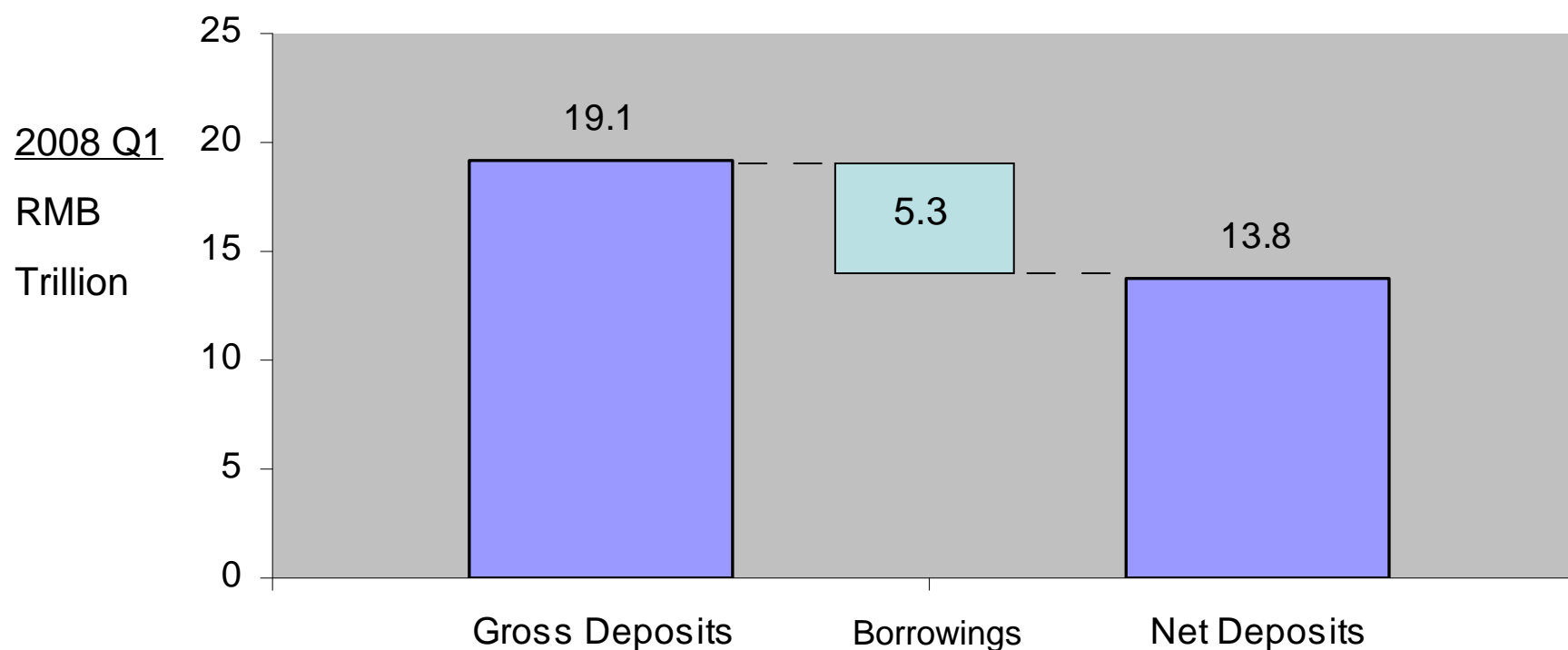


Financial ‘Repression’ in China (1)

- The PBOC sets maximum interest rates on bank deposits
- Those rates, already low, have not kept ahead of inflation
- By Q1 2008 the real return on one-year deposits was minus 3.86%

Financial 'Repression' in China (2)

- Households are large net depositors in banks



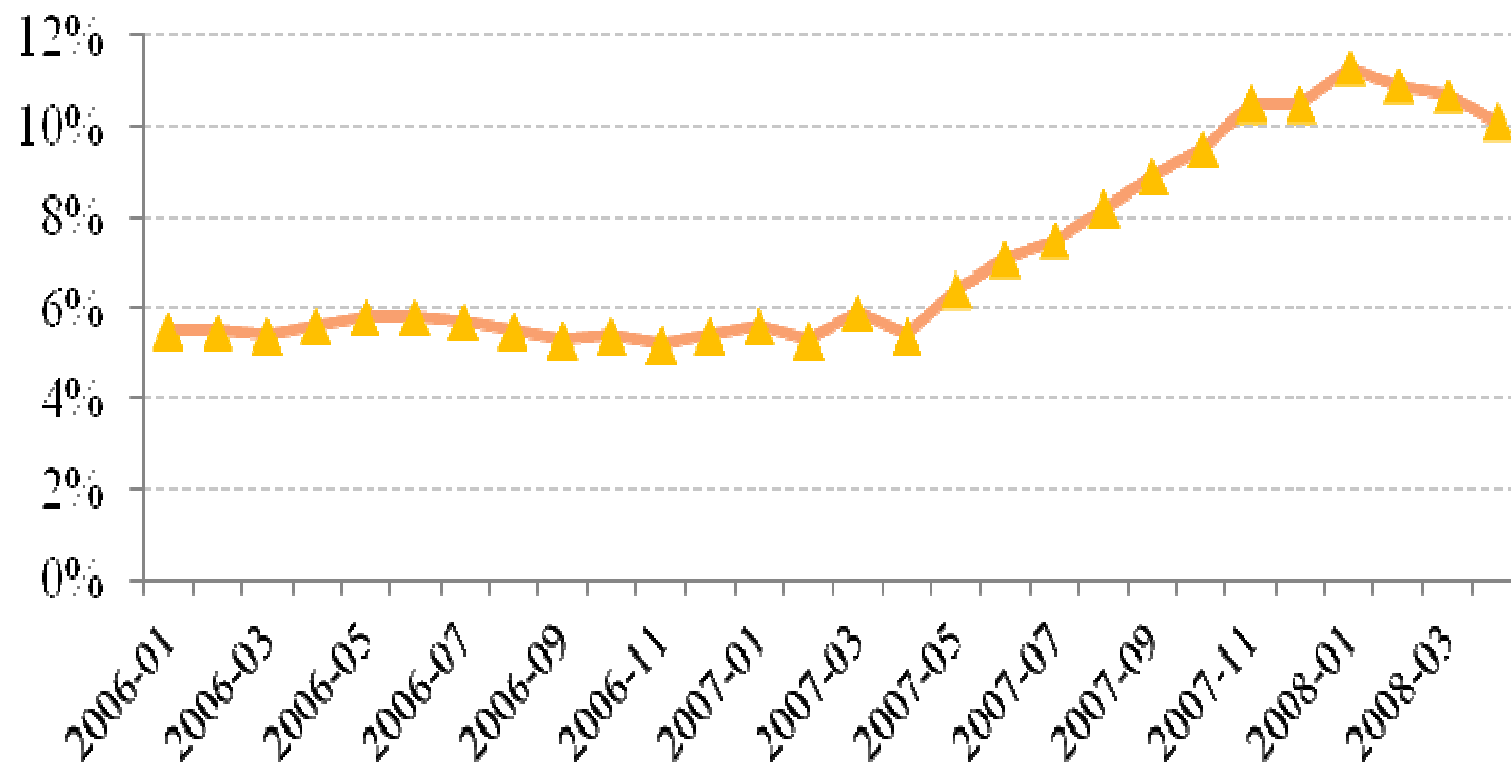
Financial 'Repression' in China (3)

- If households had received the 2002 interest rate, their income would have been RMB 255billion higher (4.1% of GPP)
- This 'tax' benefits corporate (net borrowers) banks, and government
- It is a major reason for low growth in consumer spending

**“China’s Economic Growth is unsteady,
unbalanced, uncoordinated and
unsuitable”**

Premier Wen Jiabao
National People’s Congress
March 2007

Monthly house price movement (Jan 2006-April 2008)



Performance of the Chinese Stock Market over the last year



9/10/08



HIGH 106.42 15/10/07, LOW 33.42 18/9/08, LAST 35.55 8/10/08 Source: DATASTREAM

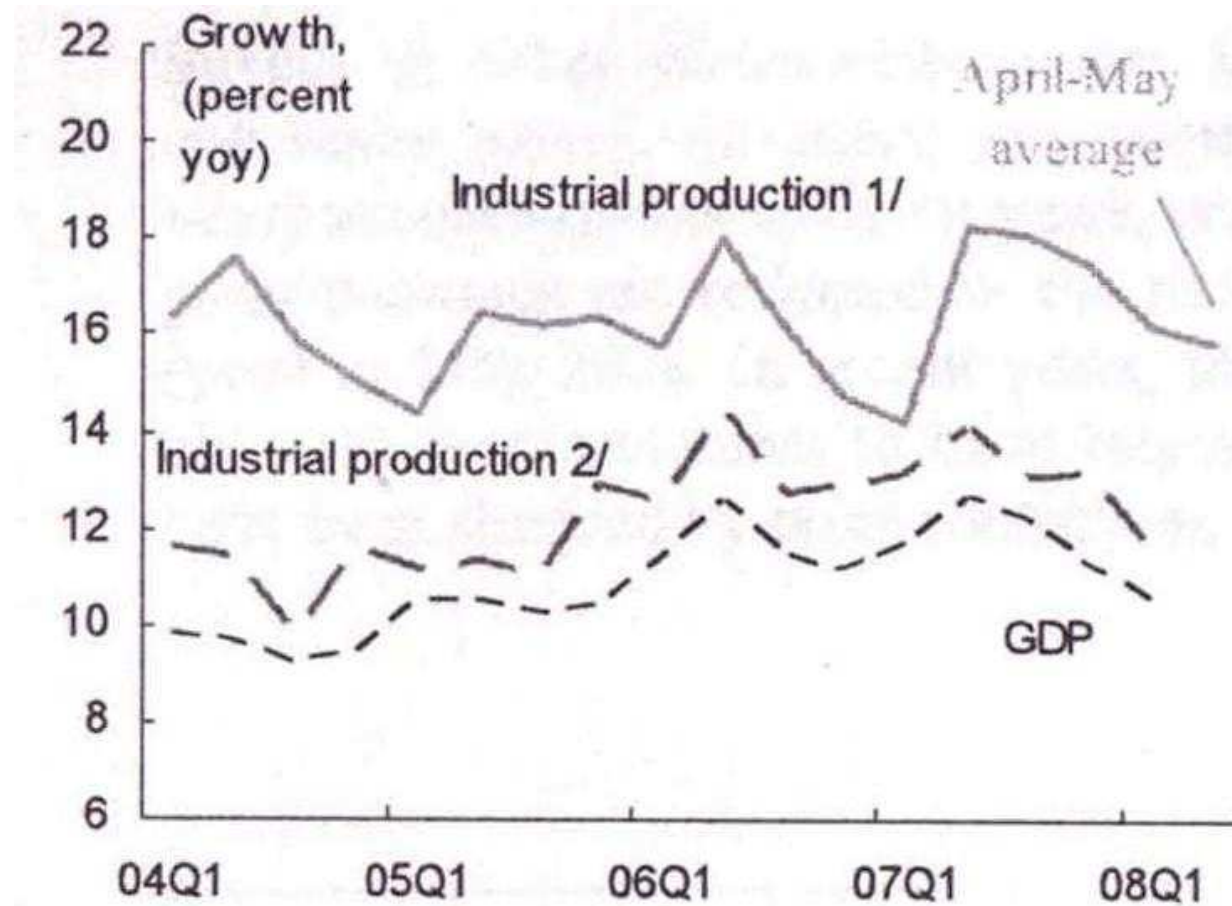
Foreign Insurers in China

45 joint ventures with Chinese partners

Growth rates 30-50% p.a. life insurance
 20-40% p.a. property and
 casualty

6% market share (2007)

Economic growth is moderating

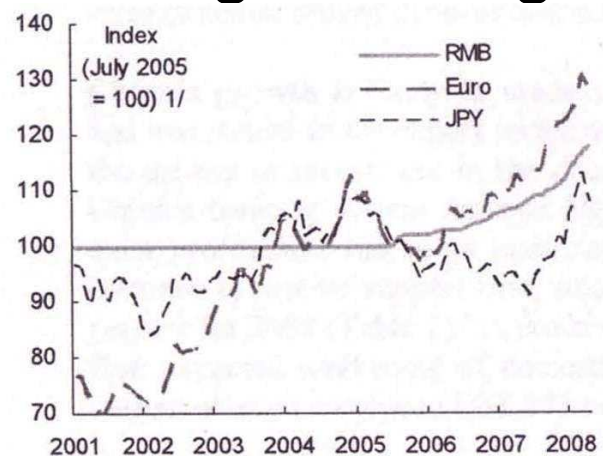


Source: NBS, staff estimates

1/ Monthly data, covering SOEs and large non-SOEs

2/ Quarterly data from national accounts

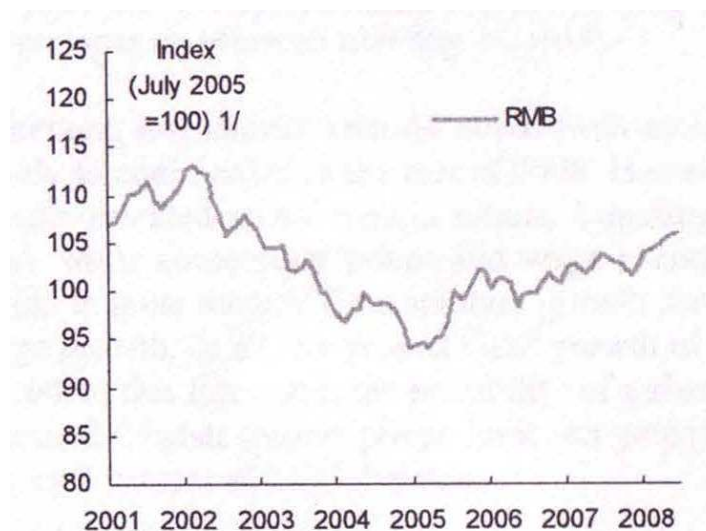
The RMB has strengthened against the US dollar



Source: CEIC, World Bank staff estimates.

1/ Increases of indices indicate appreciation against USD.

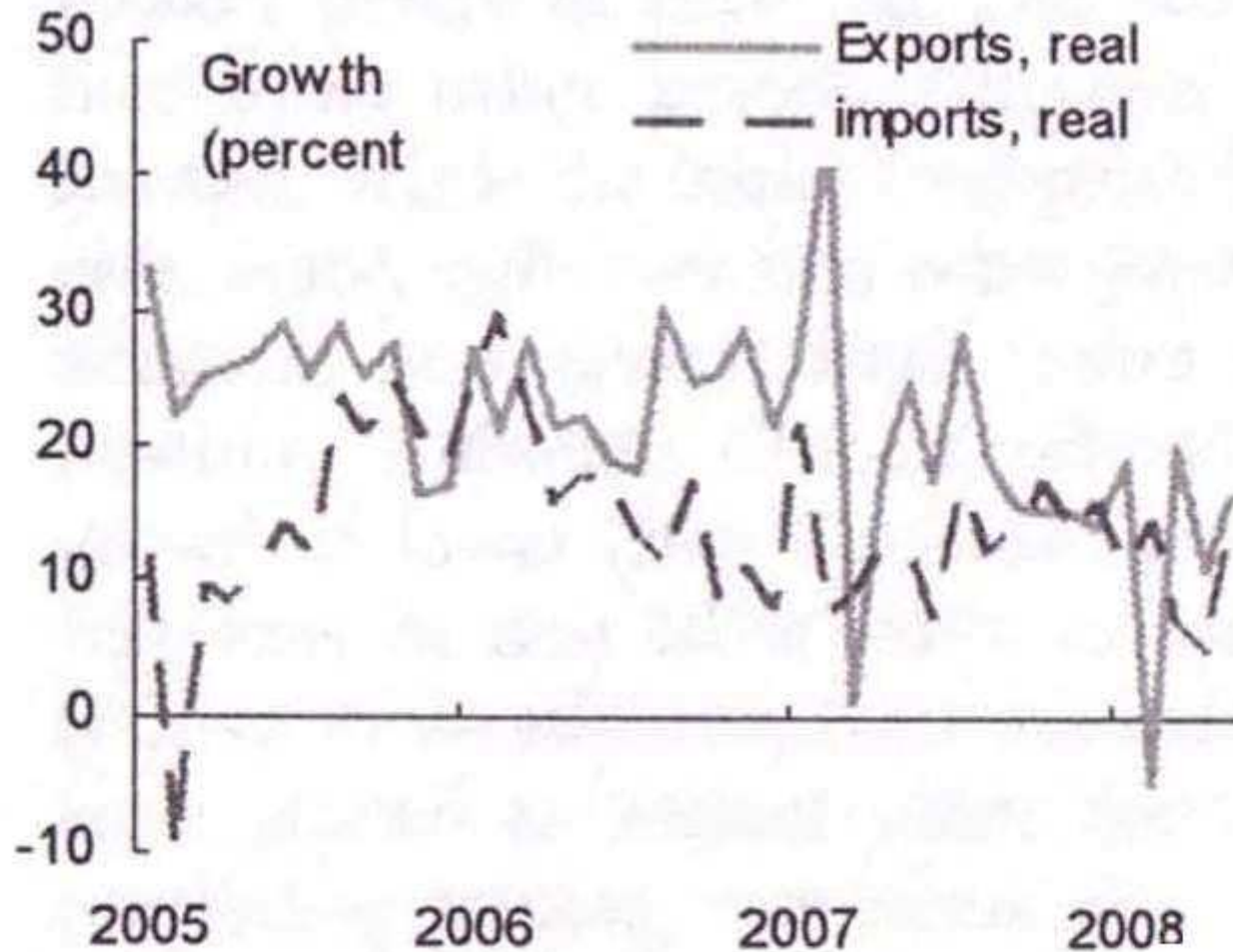
The nominal effective strengthening was smaller



Source: IMF, World Bank, staff estimates.

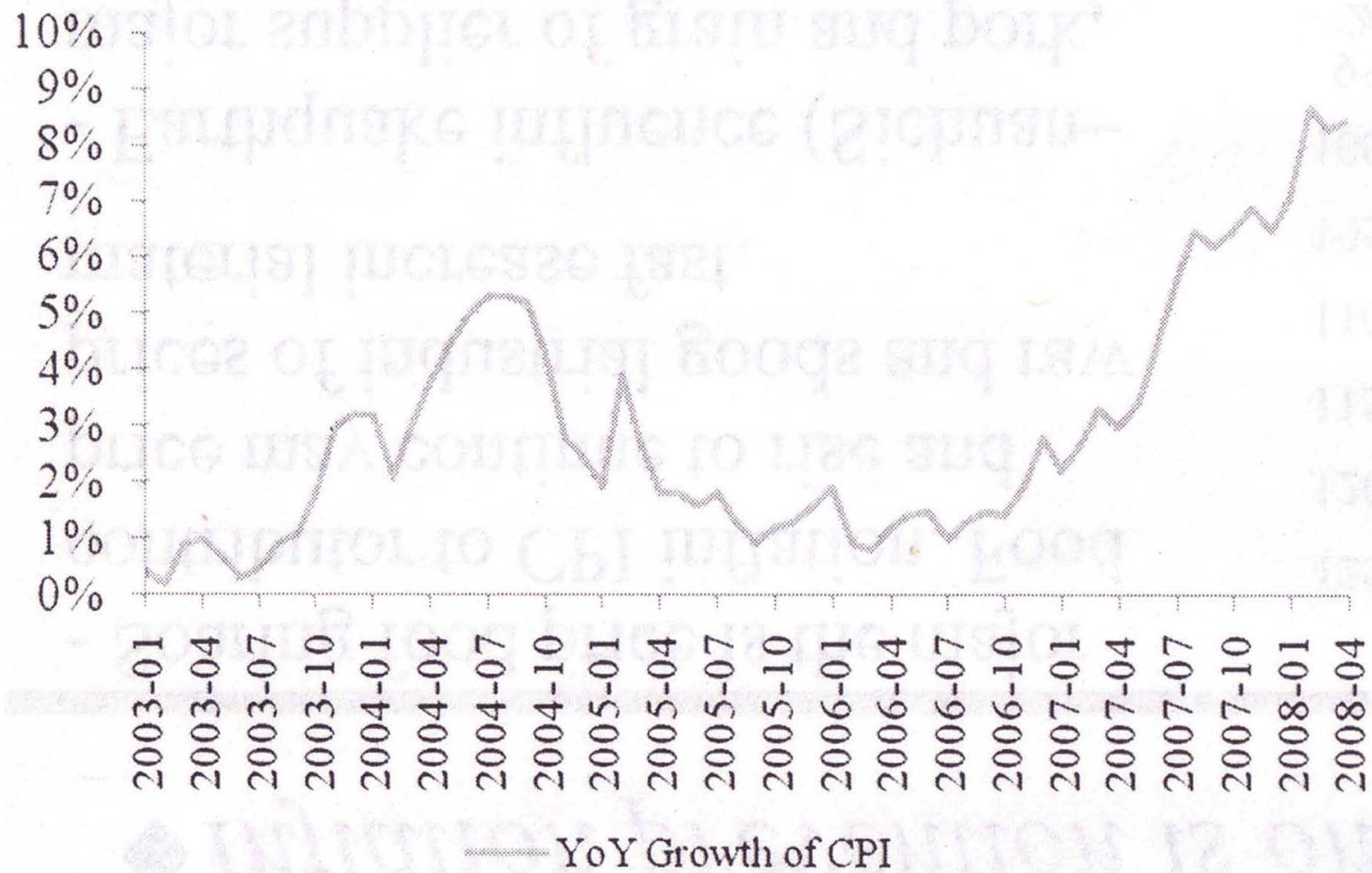
1/ Increases of index indicate appreciation.

External trade volumes have decelerated

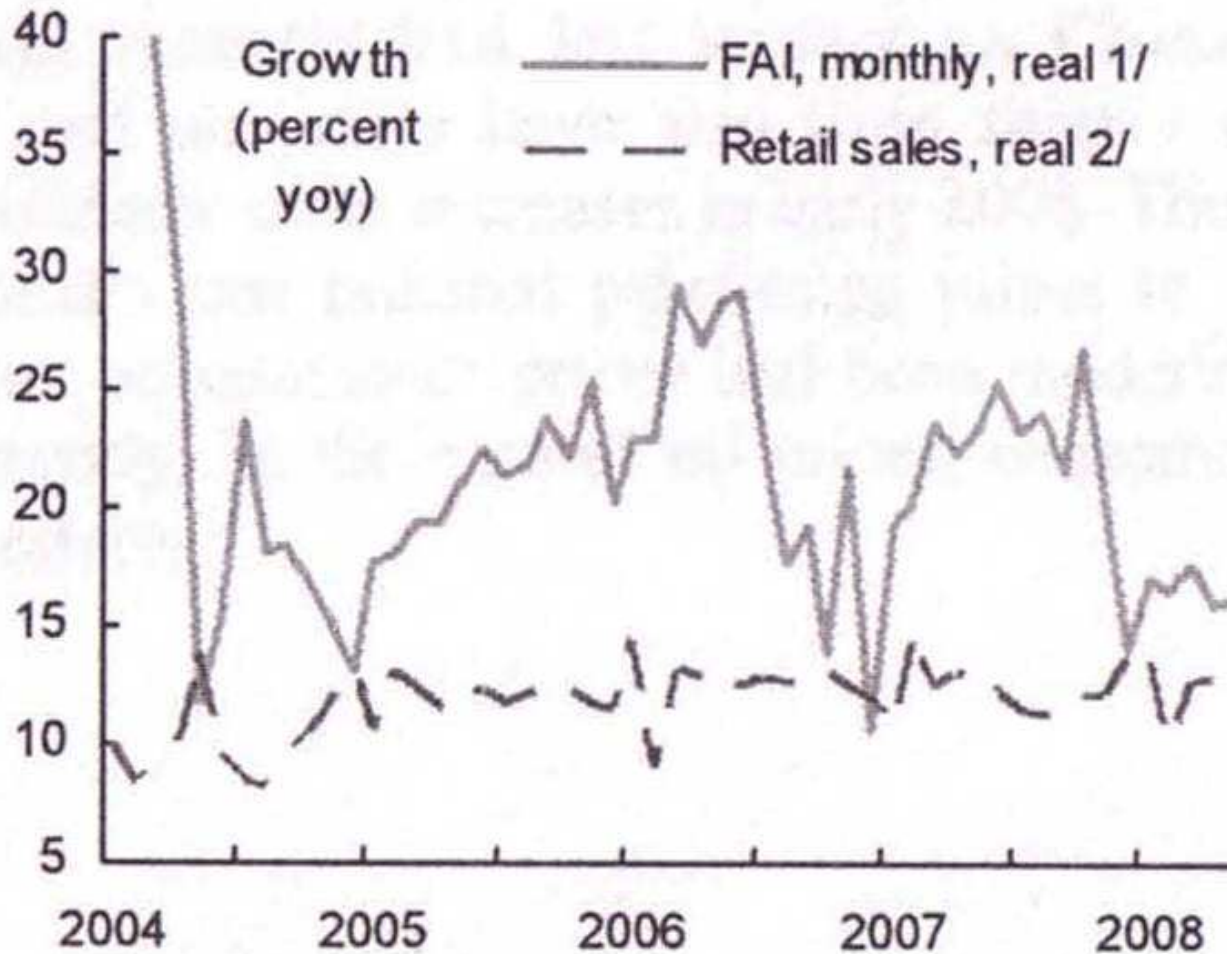


Source: CEIC, staff estimates

YoY Growth of CPI (China)



Investment is slowing down



Source: NBS, staff estimates

1/ Deflated with the PPI

2/ Deflated with the retail price index

China and the Credit Crunch

- Export slowdown highly likely
- Reduction in foreign capital imports
- Modest direct impact on Chinese banks,
but asset prices now weakening in China

But...

Major Questions about future direction of financial reform



- Should China continue to build Wall Street in Beijing?
- Should China continue to sell stakes in banks?
- Is it an opportunity for China to make a great leap forward overseas?

Leading Sovereign Wealth Funds

Country	Fund	Size (\$ Billion)	Year Created
United Arab Emirates	Abu Dhabi Investment Authority (ADIA)	500 - 875	1976
Singapore	Government of Singapore Investment Corporation (GIC)	100 - 330	1981
Norway	Government Pension Fund - Global (GPFG)	308	1990
China	China Investment Corporation, Ltd. (CIC)	200	2007
Kuwait	Future Generations Fund	174	1976
Russia	Stabilization Fund for the Russian Federation	122	2004
Singapore	Temasek Holdings	108	1974

Source: Edwin Truman, "Sovereign Wealth Funds: The Need for Greater Transparency and Accountability", Peterson Institute for International Economics, August 2007.

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15th October 2008
New Academic Building