LUJIAZUI FORUM
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Reforming Global Financial Governance For Real Economic Growth

YU Zhengsheng:	Accelerating the Construction of Shanghai as an International Financial Center
ZHOU Xiaochuan:	Reforming Financial Governance and Promoting Development of the Real Economy
HAN Zheng:	Creating an Internationally Competitive Financial Environment
SHANG Fulin:	Steadily Implementing New Regulatory Standards and Promoting the Transformation of the Banking Industry
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Preface

The 2012 Lujiazui Forum, with the theme of Reforming Global Financial Governance For Real Economic Growth, has come to a successful close. During the event, we had nearly 1,000 distinguished guests and a record number of speakers. From June 28th to 30th, we held four plenary sessions, 10 panel discussions and eight "night chats by the Huangpu", during which top government officials, financial leaders, and renowned scholars and experts discussed important questions of global finance. Our guests explored the future of China's financial reform and provided valuable advice for the development of Shanghai as a global financial center. On behalf of the organizers of the forum, I would like to thank you all for generously sharing your wisdom and foresight.

The world economic setup is undergoing profound changes. Uncertainties regarding the course of economic recovery are on the rise. As the European and American sovereign debt crises worsen, the call for extensive reform in global finance is gaining strength. China, with its rapidly growing financial markets and increasing influence in global economic and financial affairs, faces a strategic development opportunity. But it is also confronted with the task of rebalancing its economic structure. This year's Lujiazui Forum has inspired heated discussion over how we can achieve this task through a multilateral approach. The topics covered in the forum were both numerous and diverse. They included: financial reform and the development of the real economy, internationalization of the yuan and the 'going out' of Chinese finance, exchange rate and interest rate marketization, the future of bond markets, the reform of local financing structure, the refinement of financial administrative systems, and the establishment of a financial system compatible with the development of small businesses.

How to transform Shanghai into a global financial center undoubtedly attracted the most attention, with many speakers offering constructive advice. Great achievements have been made, yet new challenges have arisen as the environment has changed. The next few years will be a crucial phase for the project, and we will follow the guidance of the central government and move ahead with the goal of constructing Shanghai into a global financial center. In the process, we will draw advice from all fields. We will uphold the dictum that finance serves the real economy while continuing marketization. We will emphasize internationalization and legalization, coordination and innovation.

As short as it was, our gathering will leave lasting memories. The Lujiazui Forum is a feast of ideas and a stage for new knowledge. To this end, the organizing committee of the Forum has invited Caixin Media to glean the cream of the crop of the speeches, and gather them in this publication. We look forward to meeting with you again in 2013.

FANG Xinghai
Director, Financial Service Office, Shanghai Municipal Government
Secretary, 2012 Lujiazui Forum

Opening Keynote Speech

Accelerating the Construction of Shanghai as an International Financial Center

YU Zhengsheng/ Member of the Political Bureau of the CPC Central Committee and Secretary of the CPC Shanghai Municipal Committee

Respected guests, friends, ladies, gentlemen, good morning!

I am very happy to meet our old and new friends here on the banks of the Huangpu River and discuss about economic development and progress.

The global economy is continuing to recover, and although prospects for growth are improving, the operations of the economy remain unstable, and uncertainties abound. We have yet to eliminate the deep-set causes of the global financial crisis, and new problems continue to emerge. In particular the impact of the worsening sovereign debt crisis European financial markets and the real economy is once again demonstrating to us the protracted nature and arduousness of the global economy's recovery. We must thus align ourselves with the spirit of cooperation and mutual benefit, actively respond to the crisis, strive to promote reforms to the global financial system, and lay down a solid foundation for both the recovery of the global economy and continued growth.

The National Financial Work Conference held at the beginning of the year showed us that the financial industry must better serve the growth of the real economy. President Hu Jintao emphasized at the G20 summit that we must resolutely deepen the reforms to the international financial system. It is for these reasons that the theme of this year's Lujiazui Forum is "Reforming Global Financial Governance for Real Economic Growth." We must once again examine the relationship between finance and the real economy, explore how to reform financial governance so as to better serve the needs of real economic growth, and allow both finance and the real economy to realize balanced, coordinated growth. These issues are doubtlessly of great significance.

After the eruption of the global financial crisis in 2008, the Chinese government responded decisively and implemented a series of effective measures to maintain stable, fast growth of the domestic economy, at the same time making an important contribution to the recovery of the global economy. Shanghai, as one of the Chinese cities with the greatest degree of openness to the outside world, felt the impact of the global financial crisis more directly and profoundly. The State Council issued Document 19, which detailed the construction of "the two centers" in Shanghai, thus mitigating the effects of the global financial crisis on Shanghai and giving great drive to the building of "the two centers".

In the past few years, with the great support of all central ministries and committees and all comrades from financial regulatory departments present today, and through tireless hard work, we in Shanghai have made heartening achievements in responding to the global financial crisis, accelerating the construction of an international financial center, and promoting transformation to the mode of development. In the past five years the city's GDP has grown an average of 10.3 percent annually. Financial transactions in the city totaled 418 trillion yuan in 2011, and the financial industry realized an EVA of over 224 billion yuan, 11 percent of the city's GDP.

Global finance's center of gravity is now shifting to the Asia Pacific region. This has been a notable development on international financial markets in the past few years. How can we take advantage of this new opportunity? How can we accelerate the construction of Shanghai into an international financial center? How can we increase the influence of China in the global financial system? These are the most important questions we need to answer today.

At the end of last year, the National Development and Reform Commission issued the "Plan to Construct Shanghai into an International Financial Center." The Plan clearly highlights the necessity to take advantage of our current historical opportunity to accelerate the internationalization of the yuan, to continuously strengthen the international significance and influence of the Shanghai financial market, and to strive to establish the position of Shanghai as a global center of the innovation, price-setting, trades, and clearing of yuan-denominated transactions by 2015. In the coming period as we construct Shanghai into an international financial center, we will actively comply with planning requirements, integrate tightly with the development of the global financial system, provide strong support to the yuan's "going out" process, improve Shanghai's development amid the course of globalization, and use our scientific development to promote even healthier advancement toward globalization.

The relationship between financial governance and the real economy is an old problem. The international community must come together to explore new answers.

We will need to study and draw experience from countries and regions around the world in our quest to spur innovation, to transform our mode of development, and to build Shanghai into an international financial center.

Opening Speech

Reforming Financial Governance and Promoting Development of the Real Economy

ZHOU Xiaochuan/ Governor of the People's Bank of China and
Rotating Co-Chairman of Lujiazui Forum

Good morning to all respected leaders and guests.

June is already a summer month in Shanghai, and it is in this season that we have come to the 2012 Lujiazui forum.

Both the importance and the influence of the financial industry in the modern economy are growing rapidly, with the help of capital and the Internet. However, as the financial industry has grown rapidly, it has begun to grow disassociated from the real economy and has become one of the greatest contributing factors to the current international financial crisis.

Those in academic and business circles around the world have been deeply reassessing the reasons behind the crisis and are profoundly pondering the true nature of the financial industry. In order to better promote growth of the real economy, we must reform the governance structures of financial institutions. In consideration of this background, we made the theme of this forum "Reform of Financial Governance and Development of the Real Economy". We hope that all guests will speak freely and air their views, in order to promote reforms to financial governance, and to foster a financial industry that makes more contributions to supporting the growth of the real economy.

I would like to summarize a few viewpoints for you without laying out a detailed plan. First, we must continue to implement stable monetary policies and make timely, appropriate pre-adjustments and micro-adjustments. Second, we must urge the financial industry to better serve the development of the real economy. Third, we must work hard to promote reform and innovation in the financial industry and coordinated development of the economy and finance. Fourth, we must work hard to promote the reform and opening-up of the financial industry, and resolutely implement reforms to interest rates, exchange rates, and internationalization of the yuan. Fifth, we must diligently support and contribute to the construction of Shanghai as an international financial center, and especially support the development of capital markets. Sixth, we must prevent systemic risk, and respond to the global economic and sovereign debt crises.

The rest of the forum will be dedicated to discussing such topics as the deepening of financial reforms and the development of the real economy; moving toward reforms of the new era; global financial markets and regulatory structures; the internationalization of the yuan and the Chinese financial industry's entering the global arena; and the construction of Shanghai into an international financial center during the "12th Five-Year Plan" period. We look forward to hearing the enlightened speeches of all honored guests. We believe that this forum, on the strength of a concerted effort by all attendees, can effectuate profound stimulation and effective aid in promoting the development of the Chinese financial industry and the construction of Shanghai into an international financial center.

Banquet Speech

Creating an Internationally Competitive Financial Environment

HAN Zheng/ Mayor of Shanghai and
Rotating Co-Chairman of Lujiazui Forum

Distinguished guests, ladies and gentlemen, good evening!

This morning, the opening ceremony of the 2012 Lujiazui Forum was officially convened. And all the distinguished guests focused their presentation on the thing reforming the global financial governance for the real economic growth. And you have shared with us many constructive and forward-looking insights and proposals. Here, I'd like to pay my greatest appreciations to all the guests for sharing your insights on the global financial reform and promotion of the real economic growth. And I'd also like to offer my gratitude to all of you for your consistence support and care about Shanghai's development.

The financial reform is a very important driving force for the economic transformation and restructuring of China. Shanghai needs to proceed with its financial innovation and to provide better services as a global financial center to China as a whole. And this is a very important mission charted out by the central government of China.

On the leadership of the central government of China, and with the support and care from all the circles of the society, the Shanghai ministry government will be fully committed to the development of the financial market system and to turn the city into a rich field of financial reform and innovation, we'll do our best to create a very competitive environment for the financial industry. Looking ahead, we'll proceed to do our international financial innovation and to make our due contribution to the sound development of real economy of China.

I hope that all of you here will continue to show your kind support and care to Shanghai's development as an international financial center. And together, we can make more contribution to the financial reform of China and to the prosperity of stability of the global economy and financial industry.

Plenary Session I

Steadily Implementing New Regulatory Standards and Promoting the Transformation of the Banking Industry

SHANG Fulin/ Chairman of the China Banking Regulatory Commission

These past few years, under the leadership of the Party Central Committee and the State Council, we have made great accomplishments in the Reform and Opening and development of the Chinese banking industry. We have made positive contributions to spur growth of the real economy and counteract the negative effects of the international financial crisis. We now have a rare historical opportunity to reform, develop, and restructure the Chinese banking industry, but we are also faced by challenges. I would like to take this chance to discuss two ideas that will further push forward the restructuring of the banking industry and better serve the real economy.

First, in restructuring the banking industry, we must persistently fulfill the essential requirements of serving the real economy.

The banking industry and the real economy depend on each other. The real economy is the foundation for the survival and growth of the banking industry. The current global financial crisis illustrates that the financial industry's departure from the real economy has not only caused ineffective resource allocation, but has also weakened the financial system itself. The banking industry is a major fundraising source for the Chinese real economy. The starting point and the foothold of our restructuring ought to be: how to better satisfy the needs of the real economy. The banking industry should actively make use of such functions as credit intermediaries, risk management, and information processing, and it should promote healthy growth of the real economy.

We also realize that there are still many deep-seated contradictions and problems within the development and reform of the banking sector. Its capacity to service the real economy must be further strengthened, and its development mode urgently requires to be transformed. In the next phase, the banking industry should accelerate transformation of the mode of development, work hard to increase the universality, diversity, and effectiveness of financial services by transitioning its development mode.

The first requirement is to improve the banking system's layout and broaden access to financial services. We must accelerate the construction of a modern banking system with strong functions, reasonable distribution, orderly competition, and effective service on the foundation of the current organizational structure of the banking industry. Practical experience from within China and abroad illustrates that small community financial institutions also possess robust, sustainable vitality; even though they operate on a small scale, they are of great significance. We should work hard to develop small banks into community financial institutions that "are anchored in local development, are anchored in grassroots operations, are anchored in the real economy, and are anchored in small and micro enterprises" and should strive to provide substantial service to local economies.

The second requirement is to optimize the allocation of credit, to substantially satisfy the demands of the real economy. Banks should use credit resources to substantially satisfy the demands of the real economy, considering the cyclical characteristics of the economy's operation and continuously optimize the credit structure. We must strengthen financial service to such weak domains as small and medium enterprises and to the "three rural issues." We must increase targeted support to Central and Western China and underdeveloped regions.

The third requirement is to accelerate the transformation of the commercial model of financial services and increase their diversity. Banks should see the client as their core, maintain a clear and reasonable market position, and actively foster a core client base and profit growth points that are appropriate for the realities of their development. We should adapt to the demands of interest rate marketization reforms, and further increase the ability to provide such services as deposits and loans. We should actively develop intermediary businesses, expand non-interest income channels, and gradually change the existing profit model which is too reliant on profit from interest spreads. We must follow the principles of intensification to flatten institutions and vertically integrate management, build organizational structures with clear business lines, reasonably delineated responsibilities, and effective management.

The fourth requirement is to strengthen risk management and increase the stability of the banking system. Banks must see risk prevention as their lifeline, properly differentiate current risk from potential risk, and increase the forecast capability of risk management. As we continuously deepen financial marketization reforms, the complexity and interconnectedness of financial products and services are becoming increasingly large, risk patterns faced by the banking industry are constantly changing, and it is becoming increasingly difficult to distinguish and manage risk. Banks must step up supervision of new business risks, look far into the future to predict complicated situations, correctly manage and control risk, and pay close attention to the various trends and directional changes of risk. Banks must identify risk early, expose risk early, and dispose of risk early. Banks must actively build a stable risk appetite framework, build a rounded risk management system, improve risk management procedures and workflows, strengthen information networks and risk data management, foster a healthy risk management culture, and ceaselessly increase the effectiveness of risk management.

Second, new capital standards will effectively promote restructuring of the banking industry.

In accordance with the State Council's deployment, the CBRC has established new capital and liquidity regulatory standards that are far-sighted, reflective of the national condition, in line with international standards, and in step with the realities of the Chinese banking industry. The implementation of these new standards will not only aid to stabilize the Chinese banking industry and prevent systemic risk, but will also help to promote restructuring of the banking sector.

The new capital standards were written in accordance with the Basel III agreement. First, they established multi-layered capital adequacy ratio requirements in order to fully cover risk to individual banks in addition to systemic risk. Second, they defined the qualification standards for every kind of capital instrument, strengthen requirements on the loss absorption capacity of capital instruments, and reasonably establish the risk weight of all kinds of assets. Third, the standards expanded the scope of risk coverage of capital, and call for all banks to have provision for market risk and operational risk. Fourth, while maintaining cautious management, they increased flexibility of capital supervision, which means that banking regulatory institutions can take responsive regulatory measures on the basis of capital adequacy ratios.

The new regulatory standards for liquidity risk formally introduced a liquidity risk regulatory indicator, which, in accordance with the global standard, includes the liquidity coverage ratio and the net steady finance ratio. The regulations also improved the regulatory demands of liquidity risk, and established a a more systemic liquidity risk analysis and evaluation framework. We hope that the new regulatory standards will allow us to achieve the following goals:

First, promote restructuring of the banking industry. In the long term, it will be difficult for banks to sustain their current development model of high capital consumption. The new regulatory standards will aim at strengthening capital constraints, and will promote banks to shift their growth model -- one of constantly expanding -- toward a model of constantly improving quality and efficiency.

Second, further optimize the banking industry's credit structure. The implementation of the new capital regulatory standards will use capital requirements to guide banks' credit allocation, and will promote bank asset quality, and will improve credit structure. The new standards scientifically adjust the risk weight of micro enterprise loans, personal loans, and credit cards, will lead to banks' increasing lending in relevant domains, and will more effectively support economic restructuring.

Third, increase the level of the banking industry's risk management and strengthen their capacity to withstand outside forces. The new standards call for strengthening capital loss absorption capacity and expanding capital risk coverage. The new liquidity standards require banks to closely follow liquidity changes, to strengthen analysis and supervision of cash flows, to build an adequate, high-quality liquid assets reserve, to increase pressure testing and the effectiveness of contingency plans, and to better respond to external liquidity issues.

The implementation of the new standards is the most important step of the reforms to Chinese financial regulation. Their effective implementation will ensure the effectiveness of stepped-up regulation. We will make concerted efforts together with every relevant department to implement the new standards.

The first job is to seriously establish and implement a capital compliance plan. Banking and financial institutions must establish and implement transitional compliance plans during this period in accordance with the requirements of the new regulatory standards, and begin concrete work in the areas of management policies, procedures, instruments, data, and information systems. They must also strengthen risk management and internal control and compliance structures that link up with the implementation of the new standards.

The second job is to pay close attention to developing supporting structures. The CBRC will pay close attention to such supporting structures as reforming regulatory procedures, developing of regulatory information systems and designing regulatory reports. Our focus will be guiding, fostering, and on-site supervising the implementation of these new regulatory standards within banks, following and monitoring the progress and impact of the standards, analyzing their outcomes, and ceaselessly improving regulatory policies and instruments. The CBRC will further advance the construction of internal regulation capabilities and increase the effectiveness of regulation through the implementation of the new standards.

The third job is to diversify capital replenishment sources. To mitigate capital replenishment pressure in banks brought on by credit growth, banks must increase their own profit retention rates and increase their in-house capacity to replenish capital. The CBRC published suggestions for how to encourage and induce more private capital into the banking industry, actively create a healthy environment, support private and other capital's entry into the banking system, and promote diversity of banking capital sources and ownership structures.

The fourth job is to strengthen coordination and cooperation with relevant policies. The effective implementation of the new regulatory standards is impossible without the energetic support of relevant departments. The CBRC will strengthen communication and cooperation with the NDRC, the Ministry of Finance, the People's Bank of China, and other relevant departments to realize coordination with other regulatory policies, industrial policies, financial policies and monetary policies, and to promote sustainable development of the real economy.

Development and restructuring are the most pressing tasks facing China's banking industry. Since we are faced by an urgent and arduou restructuring task, we must make tireless efforts to explore sustainable development methods suitable for various different banks.

The CBRC will steadily implement the new regulatory standards, promote the development and restructuring of the banking industry, and work hard to build an even more stable banking system, in order to promote the real economy and strengthen efforts to build Shanghai as a global financial center.

Plenary Session I

Financial System Reforms are Vital to China's Economic Development

GUO Shuqing/ Chairman of the China Securities Regulatory Commission

The rapid growth of the Chinese economy over these last 30 years has caused fundamental changes to global economic structures. But our achievement has come at a price. We have run up against hard limits in many areas, including factor investment costs and resource allocation efficiency. Thus it is both normal and reasonable that our domestic economy has slowed since the beginning of the year. We cannot forego transformation to our mode of development; in fact, that is the core of the 12th Five-Year Plan. Throughout this process, deeply reforming the financial system will be a historic task on the success of which hinges the fate of everything.

Severe Imbalances to Savings and the Investment Structure

According to National Bureau of Statistics, the Chinese GDP in 2011 was 47 trillion yuan, of which 22.5 trillion came from end consumers, 22.9 trillion from capital formation and 1.2 trillion from net exports. This shows that the Chinese savings rate is as high as 52 percent. Some economists abroad think that our accounting methods are different from those in general use, but even if we calculate based on a 45 percent savings rate, total savings in China in a single year exceed 21.5 trillion yuan, equivalent to US$3.4 trillion. That is the highest savings rate in the world, so we Chinese can no longer talk about our capital shortages.

Our savings are primarily placed in industrial investments, which account for 40 percent of total Chinese fixed asset investments. But as early as 2009, there were over-capacity problems in 21 of the 24 major industries. Almost no manufacturing industries with mature technology suffered from insufficient capacity. So-called high technology industries, such as crystalline silicon, solar powered batteries and wind power, which have benefitted from large-scale investments in recent years, are currently facing or will soon face heavy losses.

Second, we have been sinking huge investments into the construction of infrastructure. The energy, transportation and communications industries alone account for about 12 percent of total Chinese fixed asset investments. This used to be the "bottleneck" for development, but now the excess of construction has appeared in some local regions.

Third, urban construction accounts for a high proportion of our investments, with real estate alone accounting for about 25 percent, yet all over the country we continue to tear down and reconstruct buildings over and over.

Fourth, rural investments make up a small proportion of total investments, only 3 trillion plus yuan annually, but the waste is not at all lower than urban consumption. For structures built by peasants themselves, the problem of repeated razing and rebuilding is more severe.

Lastly, we should turn an eye to other service industries, which account for less than 20 percent of total fixed asset investments. Among the service industries, wholesale and retail account for 2.4 percent; scientific research for 0.5 percent; education for 1.3 percent; health and public welfare for 0.8 percent; citizen services for 0.4 percent, and culture and entertainment for 1 percent.

Human capital formation is possibly more important than physical capital formation. In 2008 the average education expenditures totaled 5.4 percent of GDP in high-income nations and 4.5 percent in middle-income nations. The global average in 2008 was four percent, yet this year it is possible that China may for the first time reach the four percent mandated by our law. Global average expenditures on healthcare and sanitation are 9.7 percent of GDP, 5.4 percent in middle-income nations and 11.2 percent in high-income nations. In China it is 4.3 percent.

The savings structure in China is also different from the rest of the world. The Chinese population is much older than the American population, with 13.7 percent of our population 60 or older. But we have accumulated very little money in our old-age pension funds, only about 3 trillion yuan altogether, less than 7 percent of GDP, or 2300 yuan per capita. According to OECD statistics, the social security fund in the US amounts to 73 percent of GDP, or US$35,000 per capita. The ratio is 87 percent in the UK, 61 percent in Canada, and 67 percent in Chile.

The divergent nature of the structures of savings, investments, and consumption in China can very handily explain the structural imbalances in our economy. Among the three industry sectors in the Chinese domestic economy, there has been insufficient growth among tertiary industries, including finance. In 2011 tertiary industries accounted for only 43 percent of total GDP. That is a significant divergence from the near 73 percent of developed nations and near 53 percent of middle-income nations. It is even lower than in many developing nations. The world average in 2008 was 69 percent.

There are deep societal, cultural, and economic backgrounds behind our structural imbalance problems. A major reason for imbalance is that factor markets have been unable to effectively allocate our resources. To resolve this problem, we will need to continue deepening our reforms and to eliminate long-term systemic obstacles in factor markets, such as labor, land, and capital markets. And we will need to greatly increase the efficiency of resource allocation.

Urgent Improvement of the Financial Service Industry Needed

There is a paradox inherent to the financial industry that we all know: When there are too many companies, financing is difficult, but when there is too much capital, investing is difficult.

This paradox is closely related to the theme of this year's forum. The crux to solving it is reform to the financial system and construction of the capital market. However, there are many other structural problems within our country's financial market.

A) There are structural imbalances within the financial industry. The most prominent of those imbalances is over-reliance on indirect financing and under-reliance on direct fund-raising. Since the beginning of this year, loans and notes accounted for 80 percent of all Chinese financing. Less than 20 percent of financing was accomplished by issuing stocks and bonds.

Bank loans accounted for 54 percent of social financing at the end of 2011, and company stocks and bonds accounted for only 26 percent. This ratio is not only lower than the direct-financing-predominant nations the U.S. (73 percent) and the UK (62 percent); it is also lower than indirect-financing-predominant nations Germany (39 percent) and Japan (44 percent). Bank deposits account for 64 percent of personal financial investments; with stocks, bonds, funds, etc. amounting to less than 14 percent of that total. In the U.S., stocks, funds, and pensions invested in capital markets altogether account for nearly 70 percent of personal financial assets.

B) There are structural imbalances within capital markets. The first imbalance is the severely lagging growth of bond markets. At the end of 2011, stock market values were nearly 4.5 times total company debt, and in most mature markets, company debt was much greater than the market value of its stock.

The second is our insufficient

layering of equity financing markets. In the U.S. they have the NYSE, NASDAQ, OTC markets, the grey market and several other layers to choose from. Their system is roughly in the shape of a pyramid. In markets in our country, we have the Main Board, the SME board, the ChiNext Board in Shenzhen Stock Exchange, and the Agency Share Transfer System, which roughly form an upside-down pyramid.

The third is insufficient growth of futures and derivatives. Futures, options, swaps and other derivative products on mature markets are well developed in terms of variety, with large transaction amounts and a high level of connection to the growth of the economy. But our derivatives markets have not grown enough.

The fourth is an irrational investor structure. Professional investment institutions hold 15.6 percent of the A-share Market, but in developed markets that ratio is closer to 70 percent. Even more irrational is the transaction structure. Individual investors on the A-share market hold 26 percent of total market value but are responsible for 85 percent of transactions.

C) There are structural imbalances affecting the real economy within the financial service industry. In the financial system, which is led by commercial banks, large enterprises and enterprises connected to government have a clear advantage in access to financial resources. Small, mid, and micro enterprises and innovative enterprises receive very limited service. In 2011, there were over 10 million SMEs in China, which contributed 50 percent to total tax revenue, accounted for 60 percent of our domestic GDP, were responsible for 70 percent of innovation, and provided 80 percent of urban employment. In the Zhongguancun Science and Technology Park alone, there were over 1000 companies that met the conditions to list on the ChiNext Board, but their access to capital markets is still very limited.

Direct Financing Can Promote Industrial Restructuring

The most pressing problem facing the Chinese economy at present is the difficulty in obtaining financing for small and micro enterprises. We need to root up all latent capacity in the banking industry and actively promote the expansion of private loans. But small and micro enterprises often require principal or debt financing over a slightly longer term, and this kind of service can only be provided through direct financing.

In order to develop the industries of scientific and technological innovation and cultural creativity, and to upgrade industry in general, we must make better use of the capital market. We should make better use of the mergers market as we integrate many of our industries. In developed nations, the annual transaction amount of mergers is often 5 percent or more of GDP, sometimes even over 10 percent. In emerging market nations the amount is 3 percent or more. But in our country it is only about 1 percent.

True emerging industries are often born amid small and micro enterprises. Uncertainties and such enterprises' light assets tend to limit their access to bank capital. The capital market has provided a system in which financiers and investors mutually shoulder risk and share profits. This can become the basic platform for promoting the growth of innovative enterprises.

In order to develop the capital market, we will need to strengthen protection of the peoples' livelihood. I estimate that by 2020, 12 percent of our population will be seniors 65 and older, but our social security and pension system are still severely insufficient. It is difficult to invest social security capital, enterprise annuities, and other long-term capital on the capital market due to narrow investment channels and an outdated system. We must scientifically and rationally allow such capital to be invested by developing professional investment institutions. The average Chinese citizen has 23,000 yuan deposited in banks. A great proportion of that money is being saved for retirement, which in itself is a good thing. The only problem is that it is hard to guarantee that these deposits will maintain or increase value. Without access to capital markets, that will be impossible.

The growth of the capital market is beneficial to dispersing risk within the financial system. It may also decrease the frequency of systemic risk and mitigate its harmful effects.Economies that predominantly make use of direct financing display stronger elasticity and faster recovery. That is mostly because of widespread participation in the capital market and the fact that citizens can better dissipate the negative effects of the crisis by spreading out the risk.

Developing the Capital Market Requires Hard Work

There is no reason that the Chinese capital market cannot become one of the foremost in the world. However, we can't achieve this goal sitting down. In the short term, we face the following formidable tasks:

Resolutely deepen reforms to both the listing and delisting systems. Increase power to regulate and punish illegal behavior during the course of an IPO. Strengthen awareness of responsibility and laws within institutions. Quickly implement reforms to the delisting procedure on the Main Board and SME Board and strengthen regulation throughout the implementation.

Accelerate the development of a multi-layer, multi-product capital market system. Work hard to develop the bond market. Actively promote an OTC market with unified regulations. Develop standardized regional equity markets. Steadily the develop futures and derivatives market and integrate them into the multi-layer capital market system. Increase innovation of new products. Seriously create pilot programs for SME high-yield bonds. Introduce petroleum futures and treasury bond futures. Expand financial management channels for citizens.

Urgently improve governance of listed companies. Heed closely whether companies' governance is sound throughout the listing process. Pay closer attention to regulating the operations of the boards of directors and boards of supervisors of listed companies. Ensure that governance regulations are effective. The only way to ensure a solid foundation of the stock market is to guarantee the quality of listed companies.

Serve and foster institutional investors even more resolutely and meticulously. Expand the wealth management industry, and open to the outside world to a greater degree. Introduce a broad spectrum of professional institutional investors. Provide a fair, effective platform for enterprise annuities, social security funds, public housing reserve funds, and old-age pension funds to enter the capital market. As long as our insurance industry is sixth in the world and our mutual fund industry is not among the top ten in the world, it will be very difficult for us to have a strong, mature capital market.

Ceaselessly increase the market's efficiency. Always place the most emphasis on protecting the interests of investors. Build a mature, rational market culture. Strengthen the construction of intermediary institutions and the construction of a justice system for the capital market.

Resolutely prevent the occurrence of regional systemic risk. Accelerate the cleaning up and reorganizing of non-standard trading venues. The financial crisis has shown us that we need not only to strengthen microeconomic regulation of the market, but that we must also strengthen cautious macroeconomic regulation, especially in the prevention of systemic risk. Before the subprime debt crisis, the amount of housing loans in the U.S. was as high as 90 percent of total GDP, much higher than the 30 to 40 percent average in other nations. This was perhaps the most easily observed early warning, yet it did not arouse sufficient attention from regulators.

Shanghai as an International Financial Center

Shanghai is a city that has never lacked financial genes. Beginning with the establishment of the Shanghai Stock Exchange in 1990, Shanghai has today evolved into the most important financial center in China for trading stocks, bonds, commercial futures, financial futures, foreign exchange, gold, and currency. On June 1 of this year, direct exchange between the yuan and the yen began in Shanghai and Tokyo. This has tremendous significance for the internationalization of the yuan and the construction of Shanghai into an international financial center. In the big picture, a great deal of empirical research indicates that the reality of increasing exchangeability of the yuan for capital feeds is progressing much faster than the theory. We are looking forward to the day that Shanghai becomes a true international financial center.

Shanghai possesses tremendous natural strengths. It is an extremely open and international city, and is home to a great amount of foreign businesses and joint ventures. The labor market and infrastructure of Shanghai are approaching the levels of advanced cities around the world. The economy of the surrounding Yangtze River Delta Region is well developed, which means vigorous demand for financial services from nearby businesses and society. Even more important, Shanghai's financial environment is very good, and its level of integrity is high. Integrity is of utmost importance to the development of a financial market. In the 200 years since Shanghai's founding, the city has accumulated an excellent commercial culture and tradition, which may be the city's most important strength.

The construction of Shanghai into an international financial center is inseparable from the development of the capital market. The CSRC will, as always, do its utmost to support and service the construction of Shanghai into an international financial center.

We also look forward to the day when Shanghai will be able to make use of its international and domestic advantages in resources and human resources to attract institutional investors; develop a modern wealth management industry; foster outstanding financial analysts; and nurture both investors who believe in us for the long term and companies that operate on the value investing concept, etc. As we deepen financial reforms, Shanghai will play an even larger, even more innovative role.

Plenary Session I

Increasing the Ability of the Insurance Industry to Serve the Economy and Society

XIANG Junbo/ Chairman of the China Insurance Regulatory Commission

The Lujiazui Financial Forum has displayed great vitality in its development up to now. I believe there are two reasons it has captured increasingly great attention from financial and economic circles around the world. The first reason is that the forum bears witness to Shanghai's development as an international financial center and international shipping center. The second reason is that the forum bears witness to China's development as major economic and financial powerhouse in the world. On behalf of the insurance industry, I would like to offer congratulations to Shanghai for its great accomplishments in economic and social development, and wish the Lujiazui Financial Forum a complete success.

First, we must focus on the effects upon financial reforms of the profound changes that have taken place in the Chinese economy and Chinese society. Over the past 30 years, the Chinese economy has realized great achievements, which would have been impossible without support from the financial industry. However, we must also focus on the challenges that the profound changes within the Chinese economy and society have imposed on the financial industry.

The first change is the labor market, which is around the Lewisian turning point. In the past entrepreneurs needed to do no more than combine cheap labor with bank loans to make profits in the domestic market and even in foreign markets. But this kind of profit opportunity is becoming much rarer for both entrepreneurs and banks.

The second change is that China can no longer rely on "catching-up" with the rest of the world to develop its technology. In the "catch-up technological advancement model", the government sets the course of technological advances and even provides concentrated financial support. But when economic entities rely primarily on innovation, nobody can set the course of technological advances ahead of time, and concentrated financial support can end up causing enormous losses.

The third change is the level of industrialization and infrastructure construction in China, which now is relatively high. However, banks focused primarily on projects, which were all launched by the government. Once returns on investment from industry and infrastructure projects fall off, the vitality of this model will also fall off.

The fourth change is China's rapidly aging population. In the past the Chinese financial system's major function was mostly cross-regional and cross-industry resource allocation. As the population ages, there will be more problems with cross-regional and cross-industrial resource allocation. Once the population is older, savings rates across the nation may drop off gradually, posing a new challenge to the financial system.

The fifth change is the distribution of wealth, of which laborers are beginning to receive more. In the past, large enterprises were the major clients and profit sources of the financial industry. But as the population structure has changed and the income distribution system has been reformed, laborers are claiming an even greater share of China's wealth distribution. In the future it will be of increasingly great importance for the financial industry to provide diversified wealth management services to individual citizens.

The above changes demonstrate that we have entered a special phase in the development of China's economy. In this phase, there will be many profound changes to the interaction between the real economy and finance, and these changes demonstrate clear demand to deepen financial reforms. To respond to financial reform, we must achieve at least three goals.

The first is to make the financial industry conform to the transitioning development model of the economy; provide better service for technological innovation; build multi-pillar, multi-layer, multi-faceted financial institutions by promoting marketization of financial factor prices; develop more financial institutions with reasonable structures and high sensitivity to profit and risk; and satisfy the financial needs of innovators.

The second is to make the financial industry respond to the aging of the population; better serve the social insurance and social security system; integrate the financial system reforms with the perfection of the social security system; make the financial system match up better with such functions as long-term savings and investments and intertemporal risk management; induce investment of long-term savings capital to increase productivity.

We have entered a special development phase. There will be many profound changes to the interaction between the real economy and finance

The third is to make the financial industry respond to the demands of creating a people-based society and better serve social wealth management; effectuate deep reforms to allocate more financial profits to individual citizens, protect citizen's long-term purchasing power, promote the healthy development of the wealth management industry, and allow citizens access to more of the fruits of economic growth.

Second, we must focus on the unique advantages of the industry and increase the level of service that the insurance industry provides to the economy and society. In its development up to now, the insurance industry has become an important component of modern society, especially in developed nations, where insurance has seeped into every aspect of society and life.

The unique advantages of the insurance industry are the reason for its proliferation. In consideration of China's national condition, I think there are four relative advantages of the insurance industry.

The first is its benefit to improving the structure of the financial system and its ability to increase the financial system's efficiency while simultaneously reducing its risks. Currently, there is a common mismatch between the benefit period and the maturity of loans, as we mainly rely on banks taking short-term deposits and lending to projects, from which they only benefit in the long run.

If the insurance industry is able to grow substantially, and more long-term capital is used to support long-term projects, we will be able to alleviate to a great degree the problems of mismatched assets and liabilities in the Chinese financial system.

The second is its benefit to strengthening the social risk management system and its provision of a more stable environment for the development of society and the economy. If China wants to become a relatively developed country, it must gradually divide the government's responsibilities over market-driven risk diversification mechanisms and social management institutions. Ever since the development of commercial insurance, the government is more than equal to the task of social management.

The third is its benefit to stimulating long-term savings and improving the social security system. As a result of its population structure, China will face more cost pressure in its social security system than many developed nations.

Therefore, the development of tax-deferred old-age insurance system and perfection of the multi-pillar pension system are of extreme significance to China.

The fourth is its benefit to promoting technological innovation and upgrading of the industrial structure. Technological innovation implies the greatest uncertainty, especially for small and medium enterprises.

The insurance industry can have a positive effect on dispersing the risks of technological innovation and serving the national strategy of independent innovation.

The next step for the CIRC is to plan our insurance work under the guidance of the State Council and based on the overall demand of preserving and promoting social stability and increasing the efficiency of economic and social operations.

Our first job is to focus on integrated urban-rural development and increase the ability of the insurance industry to safeguard the "three rural issues"; build an integrated rural insurance system; strengthen innovation and promote "three rural issues" insurance service; and explore the establishment of a disaster insurance system that is appropriate for the national condition of China.

Our nation is beleaguered by frequent windstorms, blizzards, and earthquakes. There are practical demands for research and exploration into disaster relief.

Our second job is to focus on strengthening the construction of society and the people's livelihood and increase the ability of the insurance industry to build a social security system; actively participate in the establishment of a multi-level medical insurance system; promote a tax-deferred insurance system for individuals; and diligently promote the corporate annuity program.

Our third job is to focus on servicing the relatively rapid growth of economic stability and increase the ability of the insurance industry to support economic construction; deepen market reforms in which insurance funds make use of specialization; invest more insurance capital into infrastructure construction projects -- assuming controllable risk, reasonable profits and legality of the projects -- via such methods as bonds and equity.

There is a mismatch as we mainly rely on banks taking short-term deposits and lending to projects, from which they only benefit in the long run

Our fourth job is to focus on servicing the harmony and stability of society and to increase the ability of the insurance industry to participate in social management; strengthen the construction of fundamental institutional and infrastructure construction for liability insurance system; continue to expand the experimental scope of pilot insurance programs in areas ranging from environmental protection to medicine, education, and tourism.

Our fifth job is to contribute to accelerating the transformation of the economic development model. In order to do this, we need to increase the ability of the insurance ability to innovate; strive to provide insurance service to high-tech companies and assist in the design, Research & Development, manufacturing and social responsibility of their products via our innovative insurance products; focus on service; strict supervision; prevent risk; promote development; strive to create a modern financial regulatory system that links up with the realities of the Chinese insurance market and with the international insurance market; establish an effective, standardized, open, transparent modern insurance market, and use it to promote the good, fast development of the insurance industry.

The CIRC will continue to support the fast development, the innovative development, and the standardized development of the insurance industry in Shanghai, and we will make even greater contributions to service the construction of the two centers in Shanghai.

Plenary Session II

Reforming the Global Financial Market and Regulatory Structure For a New Era

Moderator: HUANG Ming/ Professor of Finance, China Europe International Business School; Professor of Finance, Cornell University

John LAKER
Chairman, Australian Prudential Regulation Authority

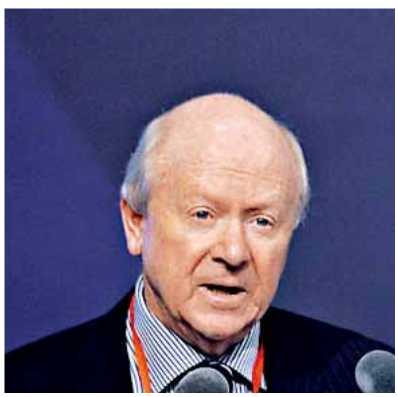
KIM Jong Hwa
Deputy Governor, Bank of Korea

Ravi MENON
Managing Director, Monetary Authority of Singapore

LI Yang
Vice President, Chinese Academy of Social Science

Frederic OUDEA
Chairman and Chief Executive Officer, Societe Generale

Steve ALMOND
Chairman, Deloitte Touche Tohmatsu Limited



John LAKER
Chairman, Australian Prudential Regulation Authority

The global financial crisis is now five years old. No one yet has been able to drive a stake into the heart of this demon. In its early phases the crisis was a U.S. banking crisis with its origins in the U.S. subprime mortgage market, but it quickly engulfed banking systems in a number of other North Atlantic economies. This is proof yet again that banking institutions subject to inadequate regulation and supervision are prone to cyclical excesses and episodes of cyclical failure. These early phases also saw a break down in the bonds of trust between investors and global banks and between banks themselves. This distrust has persisted.

In more recent phases the fragility of some banking systems has interacted with weak public finances creating dangerous feedback loops. In the Euro area particularly, significant bank exposures to sovereign credit risks and the reality that some governments can no longer support either their banks or their economies, have sapped general confidence further and heightened risk aversion in global financial markets. North Atlantic companies are still at the epicenter of the crisis but in its reach and its consequences the crisis remains a global one. Current Euro tensions, insipid European growth, and doubts about the durability of the U.S. recovery all have global repercussions.

Firstly, global growth prospects, which had been firming earlier in

2012, are again uncertain. This must be a worry for all countries in this region including Australia. Secondly, renewed fears of dislocation in global funding markets have resurfaced. Such an outcome is a particular risk for larger Australian banks. A new era is resurging in the face of these obstacles.

KIM Jong Hwa
Deputy Governor, Bank of Korea

The world economy faces uncertainties brought about by the Eurozone sovereign debt crisis amid the lingering effects of the global financial crisis.

What is the most important lesson from the recent global financial crisis? First, while the global financial market is pro-cyclical, the policy framework of major economies falls short of providing an appropriate solution for this problem. In this respect, the crisis could be a failure of market and at the same time it could be a failure of policy. Secondly , while financial globalization has made the world economy more interconnected than ever before, it also means that a localized crisis may spread like wildfire.

There are three things I would like to talk about.

Firstly, emerging economies' statuses in the world economy should be reflected in the reform of global financial architecture from the perspective of global equilibrium. Furthermore, emerging economies should make policy efforts to mitigate capital flow volatility.

Secondly, the global financial architecture should try to overcome the contradiction between liquidity and credibility for a reserve currency. An international reserve currency country needs to provide international liquidity, but the accumulation of deficit eventually leads to the loss of credibility. Considering the fact that scales of emerging economies have greatly increased along with their trade volumes, the international monetary system is likely to be transformed into a multi-reserve currency system that might include the currencies of emerging economies.

Thirdly, the global financial architecture should be sure to include a strong and sustainable coordination mechanism because prolonged global imbalances may become a potential source of a crisis.

The cross-border assets, liabilities of banks are higher than ever before. For example, the failure of a domestic bank can have ripple effects globally

Ravi MENON
Managing Director, Monetary Authority of Singapore

The global financial crisis has spurred global financial regulatory reform on a scale that is unprecedented. I would like to offer four propositions as key elements of a proper governance regime. First, finance is increasingly global. Take financial markets; they are globally interconnected and interdependent. Shocks are quickly transmitted across jurisdictions in the context of much freer capital flows. The other channel is through financial institutions. The cross-border assets, liabilities of banks are higher than ever before. For example, the failure of a domestic bank can have ripple effects globally.

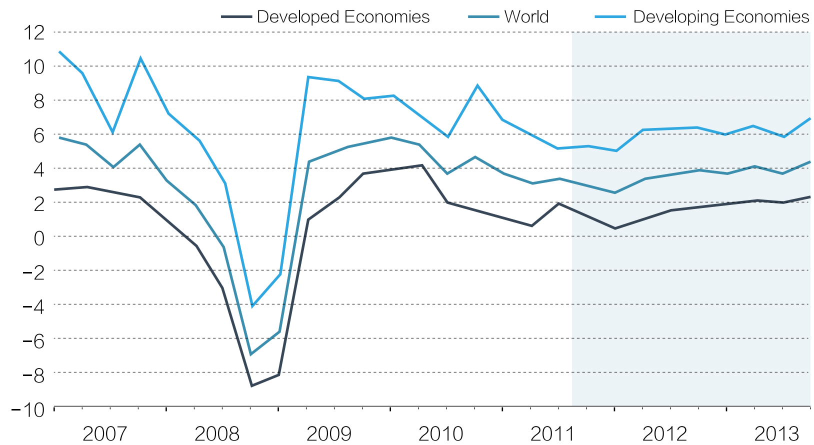
Second, financial regulatory policies must be harmonized to an increasing extent. Regulation is about rules governing behavior of financial institutions. Regulation continues to be organized along national lines. In the absence of a global regulator, we need much better harmonization of regulatory standards across jurisdictions and across sectors. It's important that countries consider the extraterritorial implications of their proposed domestic regulations.

Third, the supervision of global financial institutions must be coordinated better. Regulation alone is not enough. Effective oversight of finance is also about supervision, ensuring regulations are complied with and risks are managed well in financial institutions.

Fourth, global financial governance is still an evolving regime. Will global finance at some time in the future require global regulation or at least global rule setting? Should international finance be governed by a more rules-based system? Only time can tell. At this point it is hard to imagine such a system. In the meantime more effective frameworks should be built.

Global GDP growth

(percentage change year-on-year)



Source: IMF "World Economic Outlook - January 2012"

LI Yang

Vice President, Chinese Academy of Social Science

A crisis changes traditional ways of thinking. There are usually two types of responses to a crisis. One type is to return to conventional approach, the other type is to forge a new path. The first approach is easy to carry out, the latter approach is more difficult. We are currently behind a crisis. The current crisis has destroyed our regulations forcing us to start over. As a result, merely discussing cooperation on a policy level is not enough.

In this way, this crisis is especially important and profound. First of all, it is a crisis in each country's development model. This is obvious among every kind of country. During development, the economic system relied too heavily on exports and the rate of saving is unbalanced. Each country's real economy faces extremely serious imbalance issues. As a result, the solution to the current crisis first has to deal with the real economy. The financial system has created unprecedented changes. One of the biggest changes it has caused is its effect on the development of the real economy.

In the current international financial system, during its reform, each party had different interests – there was extreme competition. As a result, right now what we first need to do is create a cooperative attitude, then move forward with practical development.

In my opinion, the reform of the international economic system and the international financial is most important. Because of globalization, each country has its own right to develop and establish its place in the world. As a result, each country's interest can't be in the interest of the entire world. We should be tolerant towards these countries. It's worth exploring this general principle of an attitude of tolerance.

First, we need a more diversified foreign exchange reserve. Secondly, the only consensus regarding the current crisis is the need for more prudent macro-level economic policy. Third, we should fight against every form of protectionism, as the world economy becomes more globalized, it's important to promote global development; protectionism is not beneficial in this regard. Fourth, is the protection of technological and intellectual property rights which has already been commonly recognized as an essential part of promoting economic development. Fifth, globalization has resulted in the integration of many areas. Being able to look at issues at many different levels is an invaluable perspective. Finally, every reform or new policy should be carefully considered in light of the circumstances within each country, in light of what phase of development each country is in, and whether it is able to improve each country's economic development and isn't simply following some abstract principle.

Frederic OUDEA
Chairman and Chief Executive Officer, Societe Generale

First of all let me say that banks are convinced of the need of new financial governance framework and we are very open and happy to dialogue with the different regulatory bodies to shape the rules and design of this new financial framework which will make the whole system more resilient. Sometimes we challenge the overly simplistic view that we are the problem. We think that we are part of the solution. We are also effectively in a new era with probably a long term adaptation of our business model which probably means lower profitability of our activities and we accept that.

Let me also highlight that regarding this crisis, I think we need to remain humble. I think we face a pretty specific crisis. We could see this crisis as just a classic unraveling, a sequence of non-performing assets causing a contraction of liquidity. But I think we would miss out on the specifics of this crisis.

First, this crisis is really global in nature because of the interconnectivity between markets, between banking sectors. Second, this crisis has highlighted the weaknesses of the governance of the Eurozone. This specific crisis makes regulatory changes even more challenging for the European bank sector. Third, the very significant regulatory push for a new framework has translated for banks into a lot of uncertainty, which again makes our capacity to adapt and to design a strategy.

Overall, the design of the new system will be difficult and implementation by banks will be challenging.

Although policy and regulation are defined within national boundaries, massive market interactions just ignore boundaries

Steve ALMOND
Chairman, Deloitte Touche Tohmatsu

There are three key reasons why we faced unprecedented challenges and why we need to take a coordinated approach to reforms globally.

First, events are interrelated more closely and more quickly than ever before. So an election in Greece causes dramatic swings in markets in New York and in Hong Kong. A surge in shale gas production in the U.S. reduces the price of diesel fuel on the other side of the world. A tsunami in Tokyo disrupted supply chains everywhere.

Secondly, whether it's fiscal policy, monetary policy, regulatory policy, or indeed just that relationship between state and systemically important players like the big banks are jealously protected differ greatly at a national level.

Finally, although policies and regulations are defined within national boundaries, massive market interactions just ignore boundaries, cutting across boundaries in what sometimes described as the race to the bottom as institutions look for places with the most lenient regulations.

Plenary Session III

RMB Internationalization and the Globalization of China's Financial Sector

Moderator: SUN Lijian/ Vice Dean, School of Economics, Fudan University, Director, Financial Research Center, Fudan University

HU Xiaolian
Deputy Governor, The People's Bank of China

WANG Hongzhang
Chairman and Executive Director, China Construction Bank

LI Peiyu
Chairman, China Reinsurance (Group) Corporation

Mark BOLEAT
Chairman of Policy and Resources Committee City of London

Lawrence LEIBOWITZ
Chief Operating Officer, NYSE Euronext

Magnus BOCKER
Chief Executive Officer, Singapore Exchange

Nicholas LARDY
Anthony M. Solomon
Senior Fellow, Peterson Institute for International Economics

HU Xiaolian
Deputy Governor, The People's Bank of China

We started cross-border yuan businesses in 2009 by allowing only 300-odd enterprises in four cities to use yuan for trade settlement. It has been three years and we have made huge progress in this field. Now all import-export enterprises spreading across the nation can use yuan to buy and sell their products and services across borders. The latest preliminary statistics show that the amount of yuan cross-border trade settlement have increase between 70 and 80 percent from January through May compared with the same period of last year. Also, yuan settlement is gaining importance in the service trade category. Customs data show that up to 7 percent of imports and exports of China are now settled in yuan, whereas in service the ratio stands higher at about 15 percent. These prove that we made huge progress in the past three years.

Chinese currency is gaining international influence. It has been increasingly used in not only cross-border trades but also investments to other countries. Foreign governments as well as companies across the globe are showing more interest in yuan-denominated assets.

The achievement is resulted from a combination of measures, including encouraging cross-border yuan trade settlement, opening up domestic yuan-denominated bonds market to offshore investors, and launching the RQFII program to expand the use of yuan in global finance.

The underlying momentum for

developing cross-border yuan services has been the demand of domestic enterprises to hedge against exchange fluctuation risks and to reduce transaction costs. Their demand is the first driving force behind the yuan services. We started by providing the same services for yuan as for other foreign currencies, and then moved on to make its transactions more convenient than others'. Keeping reforms and maintaining an open attitude is the most important driving force behind the development of cross-border yuan services. There has been much discussion on this topic. It mainly covers three areas, namely, interest rate and exchange rate reforms, convertibility of capital account and further expansion and diversification of the financial market.

There are debates about the proper order of reforms. Which one should be the prerequisite of another? Which one needs to wait until others are completed? Economists have yet to reach consensus on such questions. We believe that reforms have to be a mutually reinforcing progress. Which area can see the fastest progress depends on not only personal will but also the external environment and conditions.

Last but not least, I would like to talk about the risks associated with cross-border yuan businesses. How significant a risk would cross-border yuan businesses pose to our society and financial order? This is the question that concerns us most.

To put a long story short, every endeavor carries risks. Our risk assessment needs to be conducted whiling keep the ultimate goal and core interest in mind.

A number of things can help us ward off risks. First, we need to maintain a steady and balanced economic growth. Second, we need to emphasize that all reforms, including the development of cross-border yuan businesses, are to serve the real economy. Thirdly, we must pay attention to systemic risks rather than focusing on the perils of a single project. Lastly, we need to follow market rules to manage and reduce risks.

WANG Hongzhang
Chairman and Executive Director, China Construction Bank

China Construction Bank has done a relatively good job in promoting yuan's internationalization. It has also encountered difficulties in the process and has shortcomings. Commercial banks such as CCB can take advantage of yuan's internationalization from four aspects.

Firstly, their offshore branches can profit from an expected increase in yuan deposits as demand for the currency grows in foreign markets. Secondly, banks' intermediary services would rapidly increase as cross-border yuan trade settlement grows along with expansion in other markets such as currency exchange platforms. Thirdly, they can devise more yuan-denominated investment instruments for foreign clients to choose. The offshore market for yuan investments has been expanding, providing Chinese banks a large opportunity to participate in the market as investors or service agents. Lastly, they can cater to foreign clients' need to develop new yuan-based products to help them hedge against exchange fluctuation risks, among other things.

Chinese banks are also likely to encounter difficulties, caused by a variety of factors such as a divergence in the legal system and regulatory environment between China and foreign countries as well as cultural differences.

CCB has done a lot of work to promote the yuan's internationalization. It has stepped up support for Chinese companies to "go abroad". To date, domestic CCB branches have provided more than 6,000 clients with cross-border yuan services involving more than 500 billion yuan. Over 130 billion yuan was processed in the first quarter alone, higher than the industrial average and three times more than CCB's own record in the same period of last year. Our offshore branches have opened more than 2,500 accounts and provided services involving more than 100 billion yuan. Yuan settlement has been expanded from only trade to non-trade areas such as direct foreign investment, acquisitions and offshore financial derivatives.

Banks also have opportunities in offshore yuan markets and in creating a mechanism for overseas yuan to flow back to China. Hong Kong's yuan bond issuance has exceeded 100 billion. Chinese banks, including the CCB, have played an indispensable role in building Hong Kong into an offshore yuan business center. They will also play an important role in facilitating yuan's flow back to China.

CCB is the world's second or third largest bank in terms of marketization. Its tier-one capital adequacy ratio is the eighth highest in the world. Our overseas assets and employment are growing by an average annual rate of 31 percent and 20 percent, respectively. The amount of yuan deposits in these overseas branches have increased by 16 times compared with five years ago. Our board of directors has just passed CCB's overseas development plan for the next five years, which determines that we need to lay out a basic service network in all major countries by 2015. We'll also speed up developing more services suitable to local needs.

LI Peiyu
Chairman, China Reinsurance (Group) Corporation

Reinsurance plays a special and important role in the insurance industry. It has a close relationship with global trade in both developed and developing countries. China Re Group is by far the only domestic reinsurance company in China. We were among the first to recognize the business opportunity in cross-border yuan trade settlement. When insurance companies in an offshore market provide insurances to local enterprises, they need to have the contracts reinsured. This involves dealing with cross-border yuan trade settlement, which is relatively new to reinsurance companies in China.

To explore this new type of business, China Re Group founded a work team dedicated to researching the clients' needs and developing products and services accordingly. We also actively communicated with both domestic and foreign regulatory authorities when conducting cross-border yuan reinsurance business.

It's been more than two years. By the end of the first quarter, we have signed yuan reinsurance contracts with 16 Chinese and foreign insurance companies in Hong Kong, Macao and Singapore, which provide yuan insurance services to nearly 100,000 families. This satisfied the need of overseas residents for yuan insurance and enriched the content of China's reinsurance industry. In 2010, China Re Group's yuan reinsurance service was awarded the second price in a financial innovation competition held by Shenzhen government.

We are obliged and honored to help promote yuan's internalization by strengthening our services and expanding to overseas market. We will continue to enhance our yuan reinsurance in Hong Kong, Macao and Singapore, while looking to expand the service to more regions. We will start cross-border yuan settlement for our businesses in Shanghai by August this year.

We have become more confident with yuan's internationalization partly because China has become the world's second largest economy. But I think we need to pay more attention to our "soft power", such as our participation and influence in global finance. We still have a large room for improvement in this aspect. Also challenging is the requirement for us to align domestic rules with internationally accepted regulation. Last year, when we communicated with regulators regarding our investment in Lloyd's of London, I found that our policies did not address the issues in some areas. Neither did Chinese banks provide all services we needed. This is indeed a process of constant exploration and gradual improvement. Enhancing soft power may be more challenging.

Mark BOLEAT
Chairman of Policy and Resources Committee City of London

The increasing use of the RMB

is a trend which will have a significant impact on international trade. The subject is important not just to China but to the world economy. China's share of world trade has grown exponentially over the past decade. The IMF notes that China has emerged like the U.S. as a major systemically important trading hub. By 2010 China had become the world's second largest trading nation after the United States overtaking Germany and Japan.

However the share of this trade denominated in dollars remains very high. HSBC estimated that in 2010 over 70 percent of China's annual trade flows were settled in U.S. dollars. It's therefore natural to see the Chinese government exploring options to move away from this dollar dominance and increase use of the RMB. The introduction of RMB denominated trade settlement has created a clear framework for increasing the usage of the RMB outside China. Starting with trade and leading into investment.

The biggest development of course has been the emergence of Hong Kong as a hub for the offshore RMB market.

Hong Kong's development as a center for RMB trade and investment has been phenomenal. And the development of the dim sum bond market shows that there is an international demand for the Chinese currency beyond trade into the investment sphere.

The natural next stage in this evolution is increasing the use of the RMB outside Asia. This is where London's role becomes important. Developing RMB products and services in London provides an opportunity to extend the use of the RMB into the western hemisphere. London is the world's leading center for foreign exchange.

Lawrence LEIBOWITZ
Chief Operating Officer, NYSE Euronext

The internationalization of the RMB is essential for Shanghai to fulfill its vision as an international financial center. It is a catalyst for the growth of China's financial market and economy as a whole and enables Shanghai's financial market to become more open, more international, for China to become less dependent on international financial flows, and to take a more influential role in world economic affairs. Prerequisites for becoming an international currency include demonstrating capital convertibility as well as liquid currency in capital markets. The gradual steps of the past few years, including entering into bilateral swap arrangements and establishing RMB trading zones as well as allowing RMB denominated bond issuance in Hong Kong. These have all been steps in the right direction giving hope that enlightened and balanced loosening of restrictions may help control any negative effects.

Continued open linkage and cooperation with such centers as Hong Kong, London, Singapore, and New York will enable Shanghai to utilize such leading financial centers for support as the process proceeds further but also to allow Shanghai to become an integrated part of the world capital markets fabric. RMB capital account convertibility is very complex which will require many steps such as increasing the flexibility of the RMB exchange rate. Liberalizing interest rates on bank deposits and loans and reforming the domestic bond markets to increase size, liquidity, and depth in addition to diversifying investors and generally making the market more institutional. The process of internationalizing the RMB cannot be viewed in a vacuum.

Magnus BOCKER
Chief Executive Officer, Singapore Exchange

In recent years the RMB has accelerated its internationalization. The RMB has exploded into the offshore markets through cross-border settlement schemes and through financing and investment programs. Yet to be truly global, the RMB must reach out to the world in a different way. The RMB must establish itself not only in mature markets like the U.S. or– in Europe but also in emerging markets here in Asia. China must align itself with other markets to create a better understanding but also more importantly to gain trust among its peers.

The existence of large and vibrant financial markets both onshore and offshore is essential for the RMB's development and success. There is an immense pent up demand for the yuan particularly here in Asia. I therefore observe a need for more offshore markets and RMB hubs.

The question is how we can support this successful journey. I believe Singapore represents one of many financial centers that will be well placed to support this journey. From the perspective of Singapore, Singapore is the fourth largest foreign exchange hub in the world. Singapore is a natural and important platform to promote RMB trade. In fact, Singapore's reputation as a major trade center and gateway to the ASEAN countries attracts many investors also keen to trade in the yuan.

Nicholas LARDY

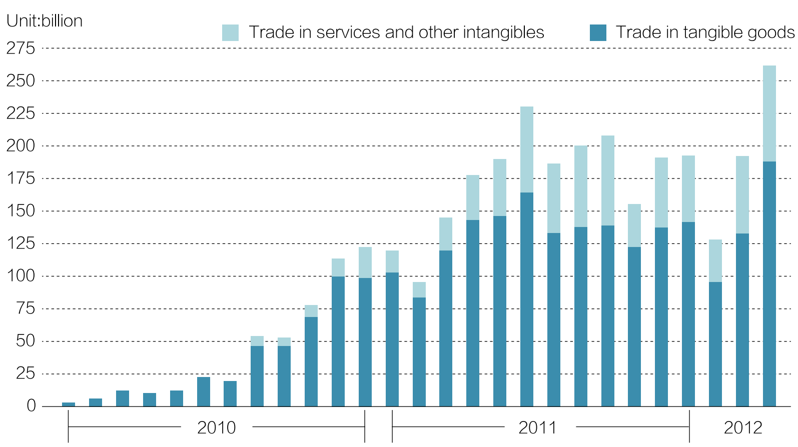
Senior Fellow, Peterson Institute for International Economics

Many speakers have mentioned specifically the further domestic financial and economic sector reforms that are a key prerequisite for further RMB internationalization. When I say further RMB internationalization I'm thinking primarily of the further opening up of the capital account and the emergence of the RMB as an important reserve currency. I think that it is possible to do a lot of cross-border trade settlement when there are still very substantial distortions in the domestic financial market. But I think it is much more difficult to further liberalize on capital account transactions and would be extremely difficult for the RMB to emerge as a significant international reserve currency if some of these domestic financial distortions are not addressed.

The one I would like to talk about which hasn't really been mentioned explicitly is in my view the Chinese financial system is one that has a great deal of financial repression. This can be measured in a number of ways but certainly one of them is low interest rates. If we look at the period since the year 2004 we can see the average real deposit rate has been in negative territory.

I think sustained negative deposit rates are a major economic distortion that has led, among other things in China, to lower household income, a higher household savings rate, a lower share of consumption in GDP, and probably also excessive investment in the housing sector. I really want to focus on negative interest rates as an obstacle to capital account liberalization and ultimately the use of RMB denominated reserve assets by central banks. If interest rate formation is not driven by market forces and the capital account is opened up prematurely, there would be large amounts of capital flowing into or out of China in a short time.

Total RMB cross–border trade settlement



Source: People' s Bank of China(PBoC) – "China' s Monetary Policy: 2012 first quarter report"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Plenary Session IV

Toward an International Financial Center: Shanghai in the 12th Five-year Plan (2011-2015)

Moderator: LI Jiange/ Chairman, China International Capital Corporation

ZHANG Yun
President, Agriculture Bank of China

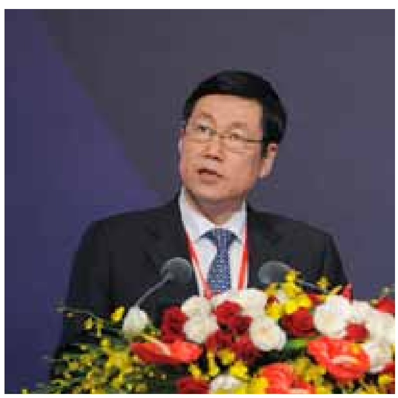
Youssef CASSIS
Professor of Economic History European University Institute

TU Guangshao
Vice Mayor of Shanghai

Andrew STONER
Deputy Premier, Minister for Trade and Investment
Minister for Regional Infrastructure and Service, State of New South Wales, Australia

ZHU Xiaoming
President, China Europe International Business School

Reto FRANCIONI
Chief Executive Officer, Deutsche Borse AG



ZHANG Yun
President, Agriculture Bank of China

As the most important participants in China's financial industry, the banking sector has an important role to play in building Shanghai into a global financial center. This great ambition cannot be separated from the active participation of the banking sector. The banking industry needs a more market-oriented, international financial environment for development and the rule of law.

First, there is a huge opportunity for development: the construction of Shanghai as an international financial center would help the banking sector enhance service capabilities, which in turn contribute to the overall internationalization of China's financial industry. The second is the aggregation effect of Shanghai's financial sector to attract the inflow of global institutions, customers, capital and talent. Third, by promoting financial reforms, Shanghai has become an experimental zone for financial reform.

Shanghai has made great strides as an international center of finance. But compared with the three international financial centers -- New York, London, and Hong Kong-- there is still a long way to go before it reaches that level. We will focus on five main points: first, Shanghai needs to act in the service of the real economy. This is the primary function of a major finance center. Second, we will expand on efforts to promote the financial market, to build a multi-functional, multi-layered financial market system. Shanghai will have to adhere to innovation, dig deeper into the market demand in order to strengthen its influence as a financial center. Third is to strengthen all-around cooperation among financial institutions. Building an international financial center will create a gathering place for foreign financial institutions which need to learn from each other and strengthen cooperation. Fourth, Chinese banks need to pay more attention to foreign market, as progresses are being made in areas including capital account convertibility, the interest rate market, and the internationalization of the yuan. Fifth, we need to stick to innovation while keeping risks in control.

Youssef CASSIS
Professor of Economic History European University Institute

I'm very glad the organizers thought to include a historical perspective of the rise of Shanghai as an international financial center. I will give a longer term perspective looking at what lessons Shanghai could learn from the previous experience of leading financial centers. There are four main broad lessons.

The first concerns what happened in the change of international financial leadership. In the last 300 years only three cities have been the leading international financial center: Amsterdam in the 18th century, London in the 19th century, and New York since the mid-20th century. I would like to point out that these three cities were the financial capitals of the country with the dominant economy of the day. However, there is a time lag between the emergence of a major economy and the rise of its financial center.

The second lesson can be drawn from the emergence of major international financial centers. Here history shows us that as a country becomes a major economic power, its financial capital usually becomes a major international financial center. It is happening now to Shanghai in this decade. The question is how this phenomenon will occur and what form of financial center is Shanghai likely to be.

The third lesson can be drawn from the types of international centers. There are two types. There are those where international financial activities play a dominant part. You also have international financial centers where domestic financial activities play the dominant part.

Finally, we can also think a little bit about the requirements to become a major international financial center. Here are a few: political stability, stability of financial institutions, wide, dynamic, and cheap financial markets, and a wide range of financial services.

TU Guangshao
Vice Mayor of Shanghai

The most important foundation of building an international financial center is to have an environment conducive to financial development. In recent years, the Shanghai municipal government has placed a strong emphasis on Shanghai's financial environment to optimize financial development, and have made progress in doing so.

First, the legal environment for financial development is under steady development along the course set by the municipal government's guiding principles and rules.

Second, Shanghai has devoted much effort to improving the information system recording individuals' and enterprises' credit records.

Third, there has also been progress in constructing the payment and clearance system along with other financial infrastructure.

Fourth, improvements have been made in developing professional service providers such as investment consultancy and legal advisory firms.

Fifth, we have established a mechanism where the government and companies work together to attract talents with financial expertise.

Sixth, we have improved the city's public services and strengthened favorable policies to attract financial resources to Shanghai.

Finally, we have also worked to enhance local people's financial literacy by educating them to better understand and navigate the world of finance.

Andrew STONER
Deputy Premier, Minister for Trade and Investment Minister for Regional Infrastructure and Service, State of New South Wales, Australia

New South Wales greatly values its relationship with China. This forum is relevant to the memorandum of understanding between the financial services office of the Shanghai Municipal Government and the New South Wales Department of Trade and Investment signed in 2010. The memorandum focuses on the establishment of a financial services partnership between Shanghai and Sydney and recognizes that our cities have similar objectives in the area of financial services. Sydney and Shanghai can work closely together to develop both our individual roles and our partnership in financial services in our region.

I would like to share with you Sydney's experience of developing into a regional financial center which began with Australia's deregulation of financial services starting in the 1970s. In 1984, there were only two foreign banks operating in Australia, now there are 40 and almost all of them operate in Sydney.

In my state of New South Wales, there are now almost 200,000 people employed in financial services. That's more than 80,000 than there was in 1984. Financial services have overtaken manufacturing to become the largest contributor to our national economy.

Every year the New South Wales financial sector generates some 60 billion dollars. When you look at our growth rates and consider the existing size of Shanghai's financial services sector, it is exciting to think just how prosperous this city will become.

ZHU Xiaoming
President, China Europe International Business School

Traditional wisdom believes that there are two types of fund raising, direct and indirect financing. Now they have been both challenged by a new rising channel, Internet-aided financing. This new type of fund raising is made possible by digital technologies, such as large volume data processing, cloud computing and third party payment system. They can indeed largely reduce transaction costs.

A number of financial sub-sectors have adopted large volume data processing. Insurance companies, for example, use the technology to calculate premiums that should be charged on an insurance product and to guard against fraudulent claims. Securities firms also use the technologies to analyze stocks and client behaviors. When a bank wants to expand presence, it consults information technology specialists to choose locations for its branches and decide upon various things such as the number of employees needed to staff the branches.

With technological development, finding a solution to a financial problem increasingly requires not only professional experiences but also data analyses.

I suggest Shanghai prioritize developing digital technologies, including building third party payment systems and strengthening large volume data mining capabilities. There is a large room for development in this respect. In near future, financing modes based on digital and Internet technologies will no doubt revolutionize the way direct and indirect financing methods now operate.

Reto FRANCIONI
Chief Executive Officer, Deutsche Borse AG

Every time I travel into this wonderfully dynamic city, I am amazed to see what the entrepreneurial spirit which is at work here has achieved in a very short time.

Looking back at the past years since the breakout of the global financial crisis, Chinese regulators and the Chinese economy have been enormously successful.

In fact, China has supported the world economy when it was in danger of plunging into a global depression. Exchange organizations form the core of a successful financial center. If one takes exchanges as indicators for the international significance of a financial center, Shanghai is now extremely well positioned. It is home to a number of important trading platforms including the Shanghai Stock Exchange, the Shanghai Futures Exchange, the China Financial Futures Exchange, and the Shanghai Gold Exchange.

In addition, the Chinese interbank market is located in Shanghai. The establishment of the Shanghai Clearing House about three years ago was another important innovation. All these institutions have made remarkable progress in the last few years.

We are very glad at Deutsche Borse that we could make at least a small contribution to this development through the cooperation with our partners and friends here in Shanghai, for instance by providing our technology to the development of Shanghai's Stock Exchanges new generation trading system.

In this, as well as in other partnerships, we are able to build upon characteristics China and Germany have in common. Firstly, both of our economies have a strong industrial sector, and we both believe that financial sector should serve the real economy, not the other way round. Secondly, for us the capital market orientation of companies is important just as it is for you in China, and especially here in Shanghai. In addition, we both believe that business development should ultimately promote the improvement of social welfare. Thirdly, our cultures both emphasize the contributions individuals can make for the benefit of a larger community.

Overview of Shanghai Banking and Financial Institutions (2011)

Type of institution	Operating Branches			Financial Institutions with Legal Person Status
	Number of branches	Employees	Total Capital (billion RMB)	
Large commercial banks	1510	41893	2990.5	0
State development banks & policy lenders	14	504	278.1	0
Joint-stock commercial banks	571	21469	2851.6	2
Urban commercial banks	248	9976	744.9	1
Urban credit cooperatives	–	–	–	–
Rural cooperatives	345	5358	315.3	1
Financial corporations	14	964	177.9	14
Trust company	7	746	18.1	7
Postal savings institutions	456	2731	111.3	0
Foreign banks	201	17654	1002	20
New rural financial institutions	8	–	8.3	8
Other institutions	7	277	98.1	7
Totals	3417	101572	8596	60

Note: Operating branches do not include headquarters. Rural cooperatives include rural credit unions, rural cooperative banks and rural commercial banks. New rural financial institutions include village banks, loan companies and rural mutual loan societies. "Other institutions" includes finance leasing companies, automobile finance companies, money brokers, consumer finance companies, etc.

Source: People's Bank of China (PBoC) – Shanghai headquarters

Panel Discussion I

European Sovereign-debt Crisis, the Euro and Europe's Economic Prospects

Moderator: Jamil ANDERLINI/ Beijing Bureau Chief, Financial Times

Frank ZHANG
Deputy Director General, Banking Supervision Department III China Banking Regulatory Commission

The Eurozone debt crisis occurred because periphery countries lost their competitiveness after they joined the Euro zone. The problem was hidden because they received a large amount of cheap capital, which created a credit bubble and concealed weaknesses in the system.

The current problem is a long term issue without a simple solution. The biggest issue short term is the banking system. The Eurozone has taken many measures that have been unsuccessful for three reasons. First, these measures all treat the symptoms but not the root of the problem. Second, many countries in the Eurozone are unwilling to admit the gravity of the situation. Third, the interests of countries in the Eurozone are not aligned. As a result, the decision-making power is scattered.

The Euro zone has to further integrate, and there are three aspects to the integration. The first one is the integration of the banking system. If we want a solution in the short term, we have to rescue the banking sector. This means creating a single supervisory body and creating a deposit insurance structure for the Eurozone. We have to buy off bad debt and recapitalize the banks. The second one is for the Euro members to form a fiscal union, by, for example, submitting their budget plans to the scrutiny and approval of the European Commission. The third aspect is a coordination of political and economic policies.

For the Euro zone to survive we need to achieve integration in the first aspect, hopefully in the second one. The third one is unlikely. A rescue plan will most likely involve reaching the integration of banking system and a certain degree of fiscal union. After all, the cost is too much for the Euro zone to collapse.

Rafael Gil-TIENDA
Chairman, Asia Pacific Member, Senior Advisory Board, Oliver Wyman

I'd like to make three points. Clearly, the Eurozone as a whole is financially, reasonable ok, compared with the situation in the US or UK. If you take total debt as a percentage of GDP, we're at 87%. If you take deficit as a percentage of GDP we're a little bit over 4%. In the UK those figures are 83% debt to GDP, but a defect of 8%. In the US the debt is practically equal to the GDP, and the deficit is close to 10%. So we're talking about a question of governance. And clearly the current situation, of the Euro and Eurozone is not right. And a number of steps are being taken in the short term. The critical thing is that aid from the center will go directly into capitalizing the banks, rather than becoming debt of the country. And it will not be senior. So that will tend to reduce the premium these countries pay over and above the bond.

The Eurozone is creating, not withstanding, these governance problems. A lot of the value that the common currency and open economy is supposed to create-- according to a study, the value creation of the common currency is over 300 billion Euros, which is what you would expect to have in the US, or in a smaller country like the UK. But


Frank ZHANG


Rafael Gil-TIENDA


Jean BOISSINOT

by and large, over 200 billion of that comes from the German economy. So there's a political issue with communicating that. The third point is my main concern-- the productivity in southern Europe. My issue with Spain is that the productivity has to be driven by hunger at one end and education at the other. There are some impediments that are politically very hard to fashion out. I hope Greece remains in the Euro, because it will be good for them in terms of improving their productivity.

Jean BOISSINOT
Senior Advisor to the Under Secretary, French Treasury
Secretary General, Corefris

All of the financial stress in Greece and some European countries is just one dimension of the global financial crisis. What's happening in Europe might not just be an economic crisis, but an institutional crisis. And it follows that although there is a clear need to respond to the financial situation, any long-lasting solution will include some large institutional changes. The Euro, as a monetary union, built upon the closer integration of European economies, has been a great success. Following the initial steps toward integration including the adoption of the common currency, Europe is now a very significant part of the global economy, at about 9.5 trillion Euros GDP and more than 300 million inhabitants. First, after two two decades of slower growth, the Euro area managed to match the US' performance, and exceeded that of Japan. It has become a stable economic area for the world economy.

Even through the global crisis, the biggest European economies did compare favorably with other advanced economies, except the UK where GDP has not recovered to pre-crisis levels. In the Euro area the GDP has mostly recovered. In Germany and France, the recovery is in line with the US. Additionally, in the Euro area private debt remained the lowest of all advanced economies. The crisis in Greece and other countries share the same root as other parts of the world: globalization made financing more available across borders, weak financial regulation failed to provide proper incentives and encouraged risk-taking, and the effects were amplified by an environment of excess liquidity and lax fiscal policies.

Laurent COURAUDON
Country Head, Chairman of the Board of Directors, BNP Paribas (China) Ltd.

This crisis is not the crisis of the Euro as a currency. The lowest point of the Euro in all of history was 0.82 [to the dollar] in 2000. Today, during this crisis, there is a fluctuation between 1.35 and 1.25. At its lowest point, it is not a weak currency. And if you ask an exporter, they would be so pleased to have a weaker currency. So no, this is not the crisis. After thirteen years of existence, the Euro is like a successful teenager. 25% of all the world's reserves are denominated in the Euro. The reason for the Euro is not ideological, it is commercial. When you have each country of the Eurozone making more than 60% of their foreign exchanges in the Eurozone, you can see why nobody wants the end of the Eurozone. If you want to imagine Europe without the Euro during the crisis, just look the terrible currency crisis at Iceland.

Laurent COURAUDON

Jean-Yves COLIN

Andre LOESEKRUG-PIETRI

The Eurozone is addressing its problem: the divergence of the competitiveness of the countries within the Eurozone. There is a start of a new convergence and competitiveness in countries like Spain, Portugal and Greece. In the newspapers you see austerity, you see discipline, but the results are starting to be there.

Jean-Yves COLIN
Senior Executive Advisor, Amundi Asset Management

We do not think Greece will exit the Eurozone. We always thought there were possible solutions in Europe, like a better banking system, more growth. We all know that it's a matter of negotiation and compromise in Europe, between the 'main' countries and the small countries. It's always been the case in Europe and will be for decades to come. We never predicted the collapse of the EU and the Euro. We understand that there might be some risk factors affecting investors (especially Chinese investors).

But you do not have to limit your reflection on Europe to public debt. Europe is a network of firms, which might be the champions in their activities, which are profitable. There will be a lot of discussion about Greek banks, Spanish banks but if you take the two main Spanish banks, they are very profitable and in good shape. If you take industrial companies, we can talk about German carmakers, the French luxury industry. These are both in a good situation, and we think at the level of markets there is room for a rebound. In the current environment, you can only do business as usual, which is what we are doing in China. For retail markets, we have a very long-term approach. We are deeply rooted in the long-term, in a long-term framework.

Andre LOESEKRUG-PIETRI
CEO & Managing Partner, A CAPITAL

People are surprised to hear that the Euro was introduced at a lower rate than it's at today, because they have this perception that the whole continent is bankrupt. You have in Europe a lot of what China is looking for-- renewable energy, transportation, managing natural resources, etc. Most of the champions in this area are not necessarily in Japan or the US, they're in Europe. So the complimentarily between the two blocs is important. When you believe in China, you should believe in Europe too.

When you have a political class whose voting age is, on average, ten years from retirement, obviously the decisions they're making are much more short-term than in a country where the future is in front of you. And I think this is a fundamental problem that you cannot change. You need to have politicians with vision and long-term perspective, and you don't have them today.

In the last two or three years Germany has emerged as the biggest lender, but they haven't guaranteed that they will always be there. If there's no guarantee that they can preserve 2 percent of Europe's GDP (Greece is only 2 percent and decreasing), then you have a confidence problem, and perception is reality. To make a comparison with Facebook, they have dubious fundamentals and a great roadshow. Europe has great fundamentals and a terrible roadshow.

Panel Discussion II

Energy and Other Commodity Futures Markets

Moderator: BAI Liang/ Senior Journalist and Director of Financial News Center in Beijing, China Business News

YANG Maijun
President & CEO, Shanghai Futures Exchange

Bulk commodities are taking on ever more prominent financial attributes and becoming a major influence on the real economy and financial markets alike, in this time of expanding economic globalization and asset securitization.

In light of recent situations, as the US is still in the middle of a slow recovery, while Europe's prognosis hardly clear, we no longer see a rising trend in bulk commodities as in the previous period. The prices have fallen slightly, but fluctuations are quite intense. The construction and development of bulk commodities market is important for the growth of our real economy. Pricing, resource allocation, risk aversion - these are all the functions of the market, which are becoming increasingly important on China's road towards becoming a full global economy.

Many people are also very concerned with the oil futures market. The government is aware of such concerns, and has already started to roll out relevant work. At the National Financial Work Conference, Premier Wen Jiabao clearly outlined the task: We must steadily introduce oil futures and other bulk commodity futures. The Securities Regulatory Commission has also made 'accelerating the construction of oil futures market' one of the priorities of this year. This reflects our understanding of oil as an important bulk commodity.

Oil is the blood of the economy. It remains the resource that influences the global economy most. China's economy is also heavily dependent on the global oil market. In this light, we must also hasten the construction of our oil futures market.

In terms of the setup of a global oil market, the US is becoming increasingly independent in its energy supply. The pricing trend in North America and that reflected in the Brent market are also different. There's now a significant gap between the two prices. The Brent market mainly represents European prices. But neither of these prices has factored in the oil demand and supply of Asian-Pacific countries and especially China. This is why we are in dire need for our own oils futures market. I think it's a very important job to be done.

PENG Junheng
Deputy Director General, Futures Supervision

Department I at China Securities Regulatory Commission

Development and Innovation in the futures market - this is the most discussed topic in our field in the past two years, and where we've also seen the most actions. We've done much relevant work, and I'd like to discuss some of our fundamental principles.

One important principle is that we must rely on the real economy while developing the futures market. Futures market comprises financial derivatives. It would be a river cut off from its source if it breaks away from the real economy. Fortunately, due to its outstanding macroeconomic background, China has become the factory of the world. The production, sales, logistics and trade of many commodities rank among the top of the world. Consequently, the volume of our commodity derivatives trading also ranks ahead. The development of our commodity

YANG Maijun

PENG Junheng

YAN Hong

futures goes hand-in-hand with our national economy. It relies on the real economy.

The second principle is that we must take precautions against systematic risks. The futures market gained recognition from different sectors of our society only recently. We might lose such recognition should systematic risks occur, and obstacles would arise for subsequent innovation and development. This is the bottom line that must be upheld.

And in terms of our fundamental rationale, two main points:

Firstly, due to China's current reality and the stage we're in, we mostly innovate by introducing new products and new contracts. In the commodity futures system, we already have most of the major commodities other than oil. Now we're preparing for the introduction of oil futures. This, along with national bond futures, are two distinct product that carry strategic implications. Their introduction would greatly enhance the status of the futures market in our national economy.

Secondly, boosting market efficiency is also an important aspect of our development. When compared to the US, we're still behind. Even for the relatively efficient products, such as copper, the fluctuation in our markets is more intense than in the US. The operational cost of our market is also higher than our American counterpart. Currently, the American is the most efficient one in the world. Hence when we talk about gearing up to international standards, we're mainly talking about American standards.

We are in the lead in terms of trading volumes and market activities. But much remains to be done in promoting market efficiency. Only after this is done can we have a relatively solid market foundation for future participation in world pricing.

YAN Hong
Deputy Director and Professor, Shanghai Advanced Institute of Shanghai Jiao Tong University

The Chinese economy has been growing rapidly in the past 20, 30 years. The demand for bulk commodities has also been on the rise, and it is now an important force in the market. But it seems that we're always at the mercy of others in terms of pricing on the world market, and we hope for our own voice.

In order to have this voice, we must have our own futures market. We must reduce trading obstacles in the market. This is necessary for providing the market with sufficient liquidity and depth, which in turn facilitate effective value discovery.

The design of market mechanism is very important. With a relatively complete design, we can give free rein to the market, because everyone knows the game rules. Therefore in an efficient market, the role of administrative guidance must be minimized, for it brings lots of uncertainties to an efficient market, affects institutional participation, and hence affects the effectiveness of the market's value discovery process. On the other hand, rule-breaking must be strictly and effectively punished. Rules are pointless without punishment. These are the questions that we might need to address in future efforts of innovation and reform.

I'm also going to clear the names for speculators. The development of financial market, to a large extent,

MA Wensheng

ZHAO Lei

Andrew WANG

cannot do without speculators. Speculators speculate, because they chase profits. As long as they follow market rules, investment or speculation, it's merely a choice of words. In fact they both play important roles to provide liquidity and market depth. As long as we have confidence in our market mechanism, the role of speculators is still very, very important.

Should we increase products in the futures market? Yes, and inevitably. With more financial products in the future, investors can diversify their investment portfolios. We need not worry that too much capital flowing into the commodity futures market would cause major shocks. The role of financial investments in bulk commodity futures market is subject to much debate in recent years.

Recent research shows, portfolio investments that target index futures have not affected the pricing mechanism of the futures market. As long as we have a sound market mechanism, their participation only boosts liquidity and market depth while introducing little negative effects. A sound market mechanism, and a good admission and trading system will be decisive for having our own voice in the world bulk commodities pricing.

MA Wensheng
Chairman, Xinhu Futures

The bulk commodity futures market is indeed fluctuating increasingly violently. It's influenced by not only its own supply and demand, but also increasingly by global macroeconomy, monetary policies and fiscal policies. Under such fluctuations, if an enterprise or an industry does not have better risk-management abilities, its competitiveness will take a hit in the globalization process.

China's bulk commodity futures market has formed a relatively complete system. We now have 28 bulk commodities ranging from nonferrous metals to precious metals. For the 28 bulk commodities, trading volume this year seems to be lower than last year and the year before. But the amount of open positions is much higher than last year. This indicates that the size of hedge positions is growing relative to speculative positions. More industrial companies want to participate in the futures market to hedge against risks of more volatile prices due to increasing uncertainties in the economy.

It is strategically important for China to introduce crude oil futures. We rely heavily on crude oil import, which accounts for 57% of all demand this year, totaling 270 million tons. In comparison, the US market is becoming more independent. Its foreign dependence of crude oil dropped from 60% in 2006 to 48% this year. The global setup is changing dramatically. China's oil security is no longer a supply problem. It is a price risk problem.

Much of crude oil's condition today draws comparison with that of copper 20 years ago. In the 20 years of copper futures development, the global influence of Chinese copper market has grown significantly. The same can be said for non-ferrous metals in general.

We have strengthened our influence globally in three aspects through the domestic copper futures market. Firstly, we used to rely on the London Metal Exchange for copper pricing. Now we can rely on the commodity exchange in Shanghai. Secondly, 40 percent of copper trade volume in London comes from

China. Chinese positions are influenced by China's fundamentals and its industrial policies, which in turn would be reflected in the London market. Thirdly, we accept LME-standard copper for futures delivery in China. We've also established bonded delivery.

Copper delivery of the Shanghai Futures Exchange allows London brands to deliver domestically. We've established bonded delivery, which shows our ambitions and foresight. We need to align ourselves with international standards. In doing so, we would strengthen China's influence in global commodities pricing.

ZHAO Lei
Chairman, CITIC Newedge Futures

Two main trends will dominate Chinese financial market in the next decade. First, the internationalization of the yuan. Second, the development of Shanghai as an international financial center. Against this backdrop, the future of Chinese bulk commodities will see a new historic opportunity. That is to say, the era of bulk commodity internationalization has arrived.

In strategic and basic raw materials that affect the Chinese economy, our voice is still feeble. Take crude oil for instance, some estimates show that 40% of all crude oil shipments by sea eventually head towards China. Yet China has only 9% pricing power in this particular variety. We face similarly embarrassing situations on other commodities. The main reason is that our futures market is largely underdeveloped.

Though much has been achieved in 20 years of development, one core defect yet to be addressed is the restrictions on market participation. We still don't allow foreign investors to participate directly in our market, nor do we allow most investors and enterprises to compete in the world market. As a result, most prices that arise in our futures market, except copper, are not representative of the world market.

The Chinese futures market needs a real 'Reform and Opening-Up', which would enable our investors to become more competitive by using their investment and risk management tools on the international market. At the same time, this would expand the realm in which overseas investors can participate in our domestic market, which makes our futures prices more representative of the world.

Opening up China's bulk commodities market is a strategic need for China to compete globally. It also facilitates the internationalization of the yuan. But in terms of the specifics such as the path and pace of yuan's internationalization, it's a hotly contested field in the academia.

However, consensus views exist. Several problems must be solved for the internationalization of the yuan: 1) international recognition of Chinese social and legal system; 2) China must participate in the drafting of global monetary rules; and 3) as a prerequisite, all systems related to the pricing of yuan must be refined and shall operate effectively.

On this note, the internationalization of bulk commodities is an indispensable and important link. Without it, yuan internationalization is empty talk – it would never be fully realized, and great risks are involved.

Andrew WANG
General Manager, Precious Metal Department, Standard Bank

The gold industry has developed a lot over years. In terms of trading volume, production and consumption, we probably stand at the top of the world. In terms of companies and institutions involved, such as banks, most countries have at most one or two banks that have gold businesses. China has 20 to 30 on the other hand.

But we still don't have much pricing power. Though foreign institutions are willing to recognize prices in Shanghai, they cannot buy or sell gold here. There're also problems associated with foreign exchange control and taxation.

Once these problems are solved, I'm sure that the Chinese will have pricing power. I am pleased to see the developments in recent years, such as the progress of yuan's internationalization. By my reckoning, at least in gold and silver, China will have pricing power in 5-8 years.

Next, gold reserves. In the past few years, the People's Bank has been pressured by experts and scholars constantly advocating for more gold reserves.

Regarding the status of foreign central banks' gold reserves, according to statistics released by the World Gold Council, which represents global gold production concerns, the total gold reserve of global central banks amounts to more than 30,000 ton, which is worth about 1.5 trillion dollars. The top seven countries, which holds the vast majority, were racing each other to sell their reserves in 1999 and 2000. Yet for many countries, even if they sold all of their gold, the proceeds would cover only a tiny fraction of their debt. It has been realized since then that selling off gold reserves cannot solve debt problems.

In light of this, we should not keep urging the Chinese central bank for more gold reserves. Gold is still a financial instrument, but its monetary attributes have long gone.

Panel Discussion III

Paths of RMB Capital Account Convertibility

Moderator: Henny SENDER/ Chief Correspondent of International Finance, Financial Times

SHENG Songcheng
Director General of Department of Statistics & Analysis, the People's Bank of China

My views are summed up in two reports we published recently. Both have attracted much attention from the academics, the professionals and the media alike, and received generally favorable response. The reports outlined three main views.

Firstly, we think the basic conditions for accelerating the opening-up of capital accounts in China have matured. Secondly, we suggest a roadmap for opening up the capital accounts. Thirdly, we maintain that the promotion of interest and exchange rates reform and the opening-up of capital accounts should be coordinated and pushed forward at the same time.

China is facing a strategic opportunity to speed up relaxing restrictions on the capital account, because, first of all, Chinese companies and individual businesses are rapidly expanding overseas, which demand more convertible capital accounts. Secondly, we're endeavoring to build Shanghai into an international financial center. This cannot be done without liberalizing the capital account. We're making progress in this respect. In this May alone, we had cross-border yuan trade settlement worth 216 billion yuan, up between 50 and 60 percent from the same period last year. This means the yuan's internationalization is gaining speed.

The internationalization of the yuan is not only important for China's economic reform but also crucial for our long-term development. We've got 3.2 trillion dollar worth of foreign reserves and have launched a pilot program in Wenzhou to experiment with allowing domestic residents to directly invest abroad.

Regarding the roadmap of opening up China's capital accounts, for the first 1-3 years, we will loosen restrictions on direct investments with real trading background, which is to encourage enterprises to 'go abroad'. In 3-5 years, we will loosen restrictions on commercial loans with real trading background, which is to support our trade. In 5-10 years, we suggest cautiously opening up all fields, including real estate, stock and bond.

More importantly, we should coordinate efforts to implement interest and exchange rates reforms and removing restrictions on cross-border capital flows. Traditional wisdom says we need to complete interest and exchange rates liberalization first before start opening up the capital account. This is based on foreign economists' theories that don't necessarily apply to China. Reforms in these two areas are going to take a long time, and if we wait for the completion of one to start the other, we will miss too many opportunities.

PEI Chuanzhi
President, China Foreign Exchange Trade System

I'd like to share my thoughts on the convertibility of yuan capital accounts.

First, an open capital account is important for enhancing the convertibility of the yuan. Second, it has been a major goal of China's economic reform and opening up. Third, we gauge the convertibility of yuan according to internationally accepted standards, which divide a nation's capital accounts into four categories and 40 sub-categories.


SHENG Songcheng


PEI Chuanzhi


ZHOU Yuan

Lastly, we're progressing much faster than imagined in terms of relaxing capital account restrictions. Now we're in the final and most difficult stage of realizing an open capital account. Much preparation is needed to overcome difficulties in areas such as allowing individuals to invest abroad and permitting foreign capital to trade derivatives in domestic markets.

The obstacles are obvious. For instance, once the capital account is open, companies are going to diversify their assets into a mix of Chinese and foreign assets. But our banks and financial institutions still rely on the local currency for accounting purposes. There is no guarantee that they have been ready to cope with the change.

For a long time, we've insisted on a controlled and progressive approach on promoting yuan's convertibility, and we've done the same for capital account convertibility. This is a principle that must be upheld.

There has been controversy over the timing and specifics of opening up the capital account. The ultimate judging criterion in these areas should be whether the move benefits the domestic real economy, the stable development of our economy, the amelioration of international financial order, and the prosperity of international economy. We need to strike a balance between the capital account convertibility and appropriate regulation of cross-border capital flows.

ZHOU Yuan
Chief Strategy Officer, China Investment Corporation

I would like to talk about the internationalization of the yuan and the capital account convertibility from three aspects.

The first aspect is the use of yuan in cross-border businesses. The central bank has actively promoted the yuan's overseas use. The size of yuan capital in Hong Kong is about 600 billion yuan, and 200 billion and 500 billion yuan in London and Singapore respectively. It is yet to be seen whether New York and Chicago can form a yuan capital pool. Some foreign banks and many Chinese banks' overseas branches would play a significant role in this.

We've taken solid steps toward enhancing yuan's use in overseas market. I think few people would disagree that we have make huge progress in this respect. Most would agree that this is beneficial to the people, the country, and to other financial institutions of the world.

The second aspect is the capital account convertibility. We have also achieved much in this area. The number of open capital account subcategories is steadily on the rise. In the next stage, we need to figure out targeted policies to relax capital flow restrictions. This is a demanding task, considering that delineating the boundaries of various industry sectors and financial services would be difficult, if not impossible at all. The impact of cross-border capital flows on the central bank's management of yuan liquidity must be controlled as well.

The third aspect involves the pricing and trading of the yuan, which I believe is the thorniest issue. It is absolutely necessary to carry forward with the exchange rate reform, but this is not to say we have been adequately prepared for it.

Two years ago I had a discussion with an economic advisor to the US

Andy XIE

HE Dong

CHANG Chun

White House. The question was how can you rationally determine a currency's fundamental value. He said there are two ways to measure, one by comparing the Purchasing Power Parity and the other by gauging the government's interference in the country's exchange rate formation.

Regarding the same method, I asked if he meant the market is always right. He replied, "The market's always right, till it goes wrong." So we can see there is no definitive answer to what level of exchange rate is appropriate. The proper choice is to set up a floating range, in which the exchange rate could fluctuate without the government's interference.

Andy XIE
Independent Economist, Director of Rosetta Stone Capital Limited

Chinese reforms always favor gradual measures. Like the special economic zones, financial reforms have also taken this path. But what worked for special economic zones have failed for the financial sector. China's financial system is not in a healthy state.

The financial market and the real economy must be treated differently, because money flows instantly. Therefore, all reforms relating to capital, such as QDII, yuan investments abroad, yuan trade settlement, all are subject to great restrictions. These programs mean little to the broader objective.

This type of gradual reforms has harmed China's economy. If it were not fall the rigid exchange rate formation system and the defect banking sector, the bubble in the property sector would not have grown so large and impacted local economies so heavily. Unfortunately, however,many local governments are yet to acknowledge the necessity for fundamental reforms.

Many people advocate incremental reforms because they know policy makers are averse to shocks. But I think reforms always come with much pain.

China has already missed two opportunities for exchange rate liberalization. The first came before 2004 when hot money speculators had their eyes fixed elsewhere - China could've done the reform on its own term. The second came during the 2008 financial crisis. Now we see another chance, which might well be the very last one. If China doesn't go for the floating exchange rate now, all other reforms – opening up the capital accounts and developing interest rate-based financial derivatives – will face enormous risks, because fixed exchange rate will magnify the error.

Now is the best time to let exchange rate float, because China's foreign reserves are nearly balanced. If we have the banks stop buying and trading US dollars, let exchange rate find its own level, fluctuation won't be too large at this point, and the effect on the manufacturing sector won't be too large.

It also has great implications on China's financial security. We have such huge uncertainties in the banking sector, and in China's financial market. China's foreign reserve plays a huge role in our national financial security. If it slips substantially, China's finance will be in deep trouble. One of the major purposes for a floating exchange rate is to protect our foreign reserve. We should stop fiddling with the foreign reserve, for it's the foundation of China's long-term financial stability.

We can only talk about opening up

capital accounts and internationalize the yuan after we've let exchange rate float. With risks as huge as they are, it's still too early. Our current goal is financial security, financial stability, and avoiding financial crises. That's our greatest concern.

HE Dong
Executive Director (Research), Hong Kong Monetary Authority

I agree with the view that the interest and exchange rates reform and the convertibility of capital accounts need to be coordinated with each other. An open capital account is a natural result of China stepping into the ranks of high-income economies, and of the transition from planned economy to market economy. Natural as it is, there's no need to avoid or resist, or indefinitely delay it. We tend to see in many countries' experiences, that financial crisis comes with capital account convertibility. But the fact is we never took the time to sort out the causality, and we never saw that great risks would arise if capital account convertibility is deliberately held down.

We can see from the structure of China's balance sheet, which is highly unreasonable, that our liabilities as foreign direct investments carry very high costs, while out assets (mostly foreign reserves) have extremely low returns (less than 0.5% of GDP) because private entities are not allowed to invest this money. China is already an upper-middle income country. GDP growth will diminish. So the distinction between GNP and GDP is becoming increasingly important. On this note, Hong Kong and Japan both provide valuable experiences.

The ultimate purpose for capital account convertibility or yuan internationalization is to give Chinese residents the freedom to diversify their investment in either Chinese or foreign assets, thus becoming more resilient against risks.

Regarding regulations, I think a certain level of administrative regulation is always needed to prevent systemic risks. We need an administrative system that's more transparent and explicit.

China's road of reform is a process of value discovery. From strictly planned to opening up, prices are found gradually. It is the same in exchange and interest reforms. Only when we see genuine capital flows can we find real interest and exchange rates determined by market forces. But this exchange rate is unlikely to be genuinely market-oriented, if our capital accounts are not open.

There's an irrational anxiety that capital will flee China if outwards flow restrictions are loosened. This is extremely unlikely unless we run into major domestic problems. Currently, yuan assets take only a very small proportion in the portfolios of foreign investors. Though the demand for yuan assets will increase as we relax capital flow restrictions, Chinese demand for foreign-currency-denominated assets will increase as well. Therefore, the most likely consequence of opening up the capital account is increased capital flows both ways.

The ultimate purpose for capital account convertibility or yuan internationalization is to give Chinese residents the freedom to diversify their investments

CHANG Chun
Executive Director of Shanghai Advanced Institute of Finance, Shanghai Jiao Tong University

My view is that we should emphasize the liberalization of capital outflows. What is the goal of liberalizing capital accounts? The main goal is to reach an equilibrium with external cash flows. In a country like China, a large country with a large population, I personally think that a three percent daily account profit is sustainable. The key question is how to use capital accounts to balance this three percent daily profit.

I think individual securities investors should support this. There are many benefits for them: it allows the risk to be dispersed, for the country's resources to be allocated, and there are fewer obstacles in terms of international politics. I don't think that every individual should open an account, probably they will have to go through investment structures, particularly index funds, where the risk is distributed among investors. This would be good for Chinese citizens, balancing external cash flows, and the stability of the exchange rate.

There is risk. For example, the outflow of capital. China's forex reserves are more than 3.3 trillion. If add on the several thousands of millions from investment companies, I don't think there is much need for worry. If there are issues, capital accounts can still be closed; there is no risk and the most important exchange rates don't have to increase.

I also think that the timing is right. The exchange rate has balanced out and Chinese citizens are willing to invest. Two years ago, when the QDII had just been created, the pressure of appreciation was very high, so no one wanted to go outside.

Panel Discussion IV

Local Financial Regulatory Capabilities and Risk Management

Moderator: YANG Yanqing/ Deputy Editor-in-Chief, China Business News

WANG Hong
Director, Beijing Municipal Bureau of Financial Work

The central government has requirements of how local governments should manage their finance and there are policies that outline these requirements in detail. But none of these policies have been written into the law. They are still in the realm of administrative regulations. Based on our experience, however, local governments' rights and obligations in regulating financial activities need more clarification than administrative rules, because without clear and targeted legislation in this repsect, enforcement will encounter problems.

To achieve this purpose, we should, on one hand, establish laws that delineate the responsibility of local governments in supervising and regulating local financial activities; on the other hand, set up a unified regulatory agency that can oversee a variety of financial sectors where the current regulation has been quite fragmented to my knowledge.

In addition, there needs to be a coordination mechanism between local regulators and regulators at the central government level.

The new regulatory scheme in the areas of loan guarantee businesses and stock exchanges management may be a good example, where the central government establishes principle regulations and leads the work, while local government draw out their operational details in the spirit of the central government's policies. The central government's leadership is necessary because it enables nationwide supervision and coordination. Local governments' role in this scheme, on the other hand, is to promote industrial self-discipline while improving their regulatory work efficiency.

Our financial regulatory system has failed to catch up with the demand of the private financing sector. It doesn't suit the needs of urbanization

DING Minzhe
Vice Secretary General of Zhejiang Provincial Government and Director of Financial Affairs Office, Zhejiang Provincial Government

Our financial regulatory system has failed to catch up with the demand of the private financing sector, as reflected in three areas.

First, it doesn't suit the needs of urbanization, which has been carried out in China at a fast pace.

Second, regulations of informal lending and financial activities of small and family businesses are inadequate and unsuitable.

Third, reforms to the informal lending sector need to be implemented from the bottom to the top rather than the other way around. In light of this principle, we have launched a pilot program in Wenzhou to encourage grass roots' participation and innovation.

We need a two-prong approach for private financing reforms to have breakthrough progress. On one hand, we need to improve legislation by enacting laws that target private financing. This cannot be done without the support of the State

WANG Hong

DING Minzhe

XIAO Yafei

Council and other related central government agencies. The laws and regulations have to provide guidance to how informal lending can be formally supervised and protected. On the other hand, we need to promote financial innovation, encouraging private investors to put their money in businesses that contribute to real economic growth.

We should also explore a regulatory structure that assigns differentiated rights and obligations to central government agencies and local governments. This is necessary for improving regulatory efficiency. With the central government steering the reform direction, local governments should take on more responsibilities of finding innovative paths to reforms. They should play a more important role in the supervision of innovative financial organizations and financial market players to avoid regulatory blind spots.

XIAO Yafei
Director, Shenzhen Municipal Government Financial Services Office

Based on Shenzhen's experience, local financial service offices should only be a services coordination structure; the main function of a financial services office should be to coordinate services among financial institutions. Regardless of the amount of reform and innovation in finance or the development of China's economy and society, financial services offices should not be players in the game or even referees, they should be a good groundskeeper.

Local financial services offices have three main functions. The first is to act as a guide, to make sure local policies conform to macro-level policies. Local financial services offices should also stay within reasonable boundaries, maintaining a balance between the two sides. Secondly, they should fulfill the role of an inspirator that mobilizes and integrates all local resources for greater economic and financial development. The third function is to ensure stability and act as a stabilizer.

With the central government steering the reform direction, local governments should take on more responsibilities of finding innovative paths to reforms

In regard to the reform of supervisory structure, I have two suggestions. The first suggestion has to do with the structure of financial supervision. There should be research into how to put into law the responsibilities of local financial services offices. Second is the issue of negotiations by supervisory structures. Because we are uncoordinated, it would be difficult to regulate companies that operate in several regions.

FANG Xinghai
Director-General of Financial Services Office, Shanghai Municipal Government

What do local financial services offices actually do? Should they be involved on the level of legislation? Or should legislation be left within the jurisdiction of the State Council to define and formulate?

This is an important issue. Right

FANG Xinghai

FEI Fangyu

now, many local regulators have their own rules and regulations that don't suit the situations elsewhere. We should take this into consideration when defining the responsibilities of local governments when it comes to financial regulation.

Currently the central bank and the regulatory commissions of securities, banks, and insurance regulate all activities of private equity investments in their respective area. This needs to be changed. We should classify financial activities into either private finance or public finance. This classification would provide local governments with a firmer theoretical basis to regulate financial activities accordingly.

Certainly, many people might ask, if you let local governments supervise private financial activities, what happens if things go wrong? Since the law enforcement of local governments may be perfunctory, the supervisory power should be in the hands of central government. But we cannot ask the central government to take care of all problems. In fact, as long as local regulators are obliged with clear responsibilities, it is only a matter of time before they build up capacities strong enough to control risks.

Our economic development has reached the phase where it is dependent on innovation. In response to this, the financial supervisory system needs to decentralize a bit. Everything can't be left up to the central government. Otherwise, innovation would be hindered.

FEI Fangyu

Vice Dean and Professor of China Academy of Financial Research, Shanghai Jiao Tong University

I think local financial service offices should be charged with the responsibility of regulating businesses including small loans, loan guarantee services, OTC markets and equity exchanges. One of the reasons is that these areas are yet to be classified as regular financing, and their regulation shall therefore be different from regular financing.

Since the law enforcement of local governments may be perfunctory, the supervisory power should be in the hands of central government

Moreover, activities in these areas are less likely to create systemic risks and their problems are less likely to be contagious. Therefore, they can be regulated by local authorities, while the central regulator attends to systemically important areas. In addition, local authorites are usually in a better position to manage small and medium-sized businesses with lower administrative cost because they are better informed about local business conditions.

Of course, having local authorities in charge has some shortcomings, such as low regulatory efficiency and unequal enforcement.

Theoretically speaking, however, we can find a balance between the positive and negative effects of this arrangement. In practice, we can take advantage of public supervision and establish a mechanism to facilitate and strengthen coordination with the banking regulators.

Panel Discussion V

Maritime Finance in China

Moderator: YU Shicheng/ Communist Party Committee Secretary, Shanghai Maritime University

SU Min
Chief Accountant, China Shipping (Group) Company

In terms of building a shipping center and a financial center in Shanghai, both shipping and finance has developed quickly this year. However, there is still a lot of room for improvement compared to London or New York. First, the development of these two industries needs a financial structure that is able to provide comprehensive services. There are times when the Chinese financial structure is unable to keep up with the pace of the development of these businesses; there are products that aren't covered and that the network doesn't support. Second, the types of products are not diverse enough. Third, we need to update financial services that accompany the development of shipping industries. For example, we have large amounts of overseas income that are denominated in foreign currencies, so the risks are higher because of foreign exchange controls.

I have several suggestions for the development of the shipping and financial industries. First, I hope that financial institutions can support the development of the shipping industry. When the shipping industry is at a low point, hopefully financial institutions can understand the characteristics of the cycles of the shipping industry and the industries can support each other and make common progress. Second, support from the government in terms of policy is needed. China's shipping industry is not on the same level as other countries in the world in terms of the taxation system. I hope there can be exploration in each area of the taxation system. Third, we hope financial institutions can explore new products. Fourth, we hope the government can launch new policies that can attract talent to the shipping industry.

The development of shipping derivatives in Shanghai needs innovation. Innovation requires breaking the rules which means that naturally there will be risk

ZHANG Ye
President, Shanghai Shipping Exchange

Up until now, 90 percent of global trade occurs through shipping. Without shipping and transport, global trade cannot happen. Shipping derivatives are an effective channel for financial development. The US subprime mortgage crisis reflected problems in the real economy. The shipping industry is extremely strong so derivatives are definitely an option. Shipping derivatives already have a great foundation. In reality, derivatives are a type of securitization.

The development of shipping derivatives in Shanghai needs courageous innovation. Can you have innovation without risk? Then that isn't innovation. Innovation requires breaking the rules which means that naturally there will be risk.

Mathis CABIALLAVETTA
Vice Chairman of Board of Directors, Swiss Re

Why is maritime finance so important? Let us take a look at the


SU Min


ZHANG Ye


Mathis CABIALLAVETTA

current global economic landscape. The world economic outlook looks highly uncertain. With the sovereign debt crisis lingering over Europe and the recovery in the U.S. remaining very fragile. Emerging markets, especially here in Asia, will be the key contributor to global growth. Despite sometimes depressing headlines about trade figures in recent months, international and regional trade will be a key growth factor for Asia in the coming years.

In its Global Economic Outlook, the IMF predicts the trade will increase by 4 percent this year, increasing by 5.5 percent in 2013. Trade flows to and from emerging markets will become ever more important and so is maritime finance.

Let me turn to some of the challenges. The shipping industry is at the point of inflection given the collapse of freight rates, declining asset prices of ships, overcapacity and the retrenchment of the industry's biggest lenders.

The regulatory changes underway in the banking industry with Basel III are forcing banks to deleverage particularly in Europe. These developments, together with other factors, have sharply increased the cost of traditional lending in ship financing. The circumstances for maritime finance are difficult. There are three things we need to discuss in confronting these challenges: financial innovation, shipping and trade finance, and maritime risk and credit insurance.

ZHANG Xing
Chairman, Dazhong Insurance Company Limited

Shanghai's shipping insurance industry has developed quickly with a favorable policy environment. In 2011, Shanghai's shipping insurance premium reached 2.8 billion yuan, an increase of 109 percent from the previous year. By the end of 2011, there were 39 companies in Shanghai that offer shipping insurance services and more than 100 agencies with specialized knowledge in shipping insurance

Shanghai faces competitions in the shipping sector both at home and abroad. There are five global shipping hubs, namely, New York, London, Tokyo, Hong Kong and Singapore. Since 2009, the State Council has approved Dalian, Tianjin, and Xiamen to build shipping centers.

The world's five largest shipping centers are also the world's most famous financial centers. The financial industry is also able to resolve some of the difficulties that shipping companies and ports face. Financial institutions can provide investment and insurance. There is still a large gap between the quality of Shanghai's shipping insurance services and the ambition of a shipping center as opposed to other places in the world.

China's shipping insurance businesses are concentrated in a few companies. On the one hand this is

Despite sometimes depressing headlines about trade figures in recent months, international and regional trade will be a key growth factor for Asia

ZHANG Xing

JIN Qi

because these companies were the first to emerge and have gained an upper hand; they have accumulated excellent technology after years of development and developed into well-known brands. On the other hand, this is because there is a lack of small and medium sized companies in this industry. On top of that, the entry barriers for some markets are too high. Restrictions on small and medium sized companies exclude them from competion. Beside encouraging firms to take initiatives, the government and industrial associations should also lend support.

In order to strengthen the development of shipping insurance, first we need to create a good environment. Right now the law for Chinese shipping insurance is not very sound. There are still restrictions on the healthy development of this industry. Disorderly competition results in unreasonably low premiums.

Creating a favorable environment is a top priority. This means creating a robust legal system, strengthening supervision, expanding the scope of insurance schemes, and attracting talented people. Second is building a specialized association for the shipping industry to serve as a platform for cooperation and to help with self-regulation. Third is to increase cooperation. Lastly, we need to keep opening up and match Shanghai's shipping insurance businesses to internationally accepted standards.

JIN Qi
Deputy General Manager, Corporate Banking Department, Bank of Communications

There are four areas to consider when judging whether the financial sector has effectively supported the shipping industry.

First is whether the former has been able to process the account settlement request by shipping companies and their branches that spread across the world. If Shanghai wants to become a shipping center, the headquarters of all shipping companies would be drawn to the city while their shipping routes are all over the world. It can be debated whether all financial institutions handling businesses for these shipping companies need to wire the firms' money to Shanghai for settlement.

Second, there is the financing capability. We don't have established consultancies such as law firms and asset evaluation companies, which are important aids when a firm decides to raise money. The third gauge is whether the trading of shipping related products is actively in the financial market.

The fourth aspect is wealth management. Superior wealth management capacity is a component of a financial center. We have been working to integrate the banking and the shipping industries. This way we can provide more value-added services to shipping companies and allow banks to access more valued clients. There is still a lot of room for improvement in this area.

Creating a favorable environment means creating a robust legal system, expanding the scope of insurance schemes, and attracting talented people

Panel Discussion VI

Sino-European Financial Cooperation and RMB's Roles

Moderator: HE Gang/ Managing Editor, CAIJING Magazine

Denis BEAU
Director General of Operations and Member of the Executive Committee, Banque de France

On the internationalization of the yuan, it's an important step for the international monetary system. A greater use of the yuan internationally should be a balancing factor in global financial stability. This is one of the reasons France decided to add the Yuan to the SDR during the G20. Paris' position as one of the major financial centers should be able to provide a lot of support.

Starting with the French corporates, as significant investors in the Chinese yuan they're especially important for the promotion of the yuan as an international currency. They were also among the pioneers to issue yuan-denominated corporate bonds. Our banks have developed a first-class expertise regarding Chinese financial markets, both offshore and onshore. It's possible to have a yuan-denominated bank account in Paris, and recently a long-term fixed rate loan in yuan was issued out of Paris. French-based banks, including Chinese banks, know how to manage a wide set of yuan-based transaction. Therefore, Paris is well-equipped to serve as a gateway for RMB-based financial activities.

Bernard POIGNANT
China Advisor of Paris EUROPLACE and Senior Advisor of Bank of China Paris Branch

The internationalization of the RMB is a prime opportunity for the team of Chinese banks to internationalize themselves. The Chinese players, the banks, are not accustomed to thinking totally internationally, and when they do they will have to use a different approach. The main driver of internationalization has been the decision to increase the settlement of trades between China and the rest of the world in RMB, which has had a huge impact on trade between China and its neighbors. And Europe, the Eurozone, is the top client of China.

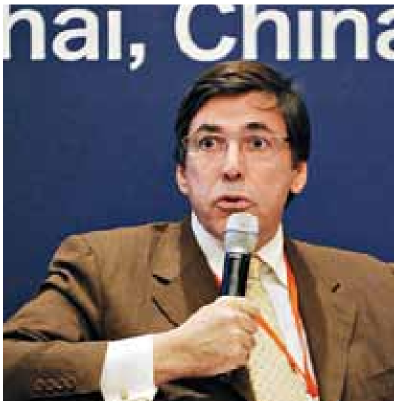
A survey conducted recently of many investors concludes that the RMB's internationalization would still be developing, which would have a greater and greater impact on international trade.

I've just been informed by the Banque de France that 10 percentage of cross-border trades with China are settled in RMB between France and China. I believe Germany also has a large percentage.

The Chinese players, the banks, are not accustomed to thinking totally internationally, and when they do they will have to use a different approach

John McCORMICK
Chairman and CEO of Markets & International Banking, Asia Pacific, RBS Group

While the globe is dominated toward a monetary system dominated by three currencies, one of them the RMB, there is still a lot of work to do before the RMB can become a true global currency. And China's



Denis BEAU

Bernard POIGNANT

John McCORMICK

reserves are not necessarily the answer to Europe's debt problems. Second, we have witnessed trade between China and Europe growing steadily in recent years. Sustainable growth is set to continue in a number of areas. And third, investment in Europe by China, be it by the state or though Chinese companies must be prudent. Though there's ample opportunity for bargain hunting given current prices, there's also plenty of potential pitfalls.

Now first, let's consider the move to develop the RMB as an international currency. The debasing of the US dollar and the Euro suggests that multiple currencies is the preferred mode in the future world of finance. Gold has shot up in price, and everyone knows the pitfalls of the international financial system reverting to gold standard.

For this reason, world leaders have unofficially backed the idea that the Chinese currency becomes an international reserve currency. So what does that actually mean for China? China will have to open its domestic capital market to test the value and worthiness of the RMB. Then, market forces can keep it valued fairly at all times, ensuring balanced supply and demand. It raised China's political clout, and brings China into other financial centers.

China will have to open its domestic capital market to test the value and worthiness of the RMB. Then, market forces can keep it valued fairly at all times

Arnaud de BRESSON
Managing Director, Paris EUROPLACE

Since its creation 15 years ago, Paris Europlace has pursued one goal: to make the financial industry promote serve the needs of the real economy. This is a very important and original characteristic of our organization, building a financial sector to serve the economy. Since the crisis in 2009, we have been in a position to connect to financial centers like Dubai, Qatar and Moscow, and more recently in Shanghai.

What are the priorities for the Paris financial center in the post-crisis period?

The first priority for Paris is to develop long-term savings and investments, and second is to combine the needs of the population (in terms of long-term savings). One key instrument for that is the strength of our asset management pool, and our key strength in Paris is the present of very strong international asset management companies.

We also want to develop more active equity and corporate bond markets. The situation of stock markets and corporates is that we match undervalued companies in the financial companies in the financial crisis, and offer Chinese investors the chance to invest in European equities.

Humber de WENDEL
Treasurer, Total Group

The RMB market internationally has opened, and we are currently looking at ways to use bonds or all sorts of offshore credit lines.

All these instruments are now at

Arnaud de BRESSON

Humber de WENDEL

WANG Tao

our disposal in places like Paris and Hong Kong, and we hope that soon they will be in Shanghai as well. What we need is to have all these instruments at our disposal at the same time, to have the utmost flexibility and liquidity.

But these are the technicalities. The grand scheme is beyond this, to gain access to the equity markets. Then we could finance the very large projects that we have in China. It would also give us access to the very large pool of Chinese investment capabilities, and access to a variety of other resources in China that we don't have at the moment.

It would create the sort of overall partnership we already have with Chinese oil companies worldwide, but which we would like to have with Chinese investors as well.

As I said we are listed in various places in the world, but at the moment less than 5 percent of our investors are from Asia, and the way to do this is to bring Chinese investors with us. To do that, we have been working with China Securities and Regulatory Commission and the Shanghai Stock Exchange. We know it's going to be a long path with a lot to be done, but we are entirely committed to this.

WANG Tao
Managing Director and Head of China Economic Research, UBS

The euro area is experiencing a sovereign debt crisis. There is a lot of risk and uncertainty, from Chinese on behalf of their own political and financial considerations, and with European cooperation they're now feeling much more cautious. But cooperation can be done through multi-lateral cooperation schemes, such as International Monetary Fund. It should also be carried out multilateral cooperation.

In the near future, China's participation in Europe is a good opportunity to stabilize the European economy and to stabilize China's export and trade

In the near future, China's participation in Europe is a good opportunity to stabilize the European economy and to stabilize China's export and trade.

European banks, especially the French banks in trade finance in Asia, before doing very more. Now, some European banks do not do this business, because they are deleveraging.

Therefore, the Bank of China has the opportunity to play more roles to support Chinese exporters. Europe's real economy is very solid, and has very good companies with a great demand on Chinese products. China also continues to import a lot of products from Europe. So financing trade supports the real economy. But China's financial industry can do more than trade support to support Chinese enterprises.

At present, our assets and liabilities do not match. Our liabilities are denominated in yuan while our assets are in in the form of Euro-denominated assets and bonds. In order to solve this mismatch, we should hold more yuan-denominated foreign assets and launch the international board.

Panel Discussion VII

Future of China's Bond Market

Moderator: SU Manyi/ Deputy Director, Financial News Center, China Business News

QI Bin
Director General of Research Center, China Securities Regulatory Commission

On the whole, the development of China's bond market has been relatively slow. There are problems with the system, problems with the credit system, a lack of investor development mechanisms. Nevertheless, the quick development of China's bond market is a common desire.

Recently, the construction of the bond market has had two big developments. The first development is the establishment of a coordinating board among various ministries and committees that has already started operating. I hope this will promote cooperation and consistency in unifying regulations in areas such as bond issuers' qualification requirements, information disclosure, investor protection and credit rating. On the other hand, we have permitted small and medium-sized enterprises to issue high-yield bonds.

High-yield bonds are successful in two aspects. First they provide an alternative channel for small and medium sized enterprises to raise

QI Bin

money. Secondly, they represent a correct direction for the reform of stock issuance system. Secondly, throughout the process of issuing high-yield bonds, the involvement of China Securities Regulatory Commission is very limited. Instead, we introduced the concept of qualified investors. This is also a progress.

We still need to research how to deal with the risks of high-yield bonds. Securities firms have a heavy responsibility. They need to do their work diligently

ZHANG Yi
Vice President, China Foreign Exchange Trade Syste

Most financial reform and innovation we have seen were not carried out rigidly according to a blueprint. This not only applies to the bonds market but also the internationalization of the yuan. The reform policies are the result of a combination of many factors, including the results of previous reforms. Developing the market needs only to suit the market's demand and try maximizing all participants' interests.

Right now there is the development of government bond futures. The linking of futures and commodities is certainly the best structural plan for the bonds market. The reason why we don't have this product yet is probably because the regulators are concerned that theories may not work out in reality.

An increasing number of institutions trading in the interbank market are entering the stock exchange market. Many stock exchange players are already an important component in the interbank market. These markets should be separated.

ZHANG Yi

LIU Shian

JIN Xiaobin

LIU Shian
Executive Vice President, Shanghai Stock Exchange

There are four ways the future development of China's bond market can make a breakthrough. First is to centralize regulatory authorities in building the bonds market. Second, we need vigorous expansion of the credit bond market. Third, we need to focus on the securitization of assets. Fourth, we need to develop the bond derivatives market.

Currently, there are still several obstacles facing the development of the bonds market that haven't been resolved at a fundamental level. The market is still inefficient.

During the future development of the bonds market, principles regarding marketization and risk must be firmly set up. The goal of developing the bond market isn't blind expansion but rather giving sufficient consideration to the needs of the real economy. The responsibility of government departments or industry supervisors is to provide the market with a transparent environment and to formulate a reasonable and scientific set of regulations.

JIN Xiaobin
Vice President, Haitong Securities

China's bond market has three characteristics: a small size, low liquidity and low participation of natural persons. Most participants in our bond markets are domestic institutional investors. It has five problems, namely, homogeneous products, discrepancies in supervision, inconsistent pricing mechanisms across regions, high threshold for issuers and a lack of innovation.

In response to these problems I have five suggestions. The first is to loosen regulation. Second is to unify and integrate supervision to improve regulatory efficiency. Third is establishing an integrated and interconnected custodian mechanism to promote the development of exchange bond markets and OTC markets at the same time. Fourth, improving laws and regulations to encourage more investor participation and better protect investors' interests. Fifth is fostering the development of independent credit rating agencies.

With regard to high-yield bonds, on the one hand the authorities need to strengthen requirements for information disclosure on the issuers' part, and adequate risk tolerance on the investors' part. On the other hand, they need to encourage innovation to create more investment instruments and methods.

HU Zheng
Deputy Chief Executive Officer, China Financial Futures Exchange

For bond market growth, we need to strengthen risk management. This requires a wealth of different tools, currently the most efficient one is government bond futures.

The risk related to the bonds market has to do with credit and interest rates. The risk of government bonds is more about interest rate fluctuation, while the risk of high-yield bonds is more of a credit one. Both government bond and high-yield bonds require give rise to demand for risk-hedging tools. When we have these tools we can create a diverse financial market including various derivatives. This means better risk management and the bonds market can become more robust.

Government bond futures are the most important hedging tool against

HU Zheng

GAO Feng

Ping CHEW

interest rate fluctuations. The great majority of futures are financial futures, 20 percent of which are government bond futures. Globally speaking, we have 24 exchanges in 20 countries conducting government bond futures businesses. Even some southeastern Asian countries that were victims to the financial crisis have government bond futures. We are the single countries in the world's major economies which doesn't have government bond futures now.

China Financial Futures Exchange has done a lot of preparation. We started last year preparing for the launch of government bond futures in areas including regulations, the trading mechanism and risk management system. Mock trading started last October. We think the conditions are ripe for us to officially launch the product.

GAO Feng
President, Deutsche Bank China

China's bond market has gained in size and developed in diversity. Now it's time for the regulators to stop being a nanny. What they need to do now is for the market to take care of itself as much as possible. Their work focus should be on institutional infrastructure building.

For example, they should leave the market to decide the yield of bonds. In addition, the upper limit of an issuer's capital leverage ratio is best left to the issuer and investors to figure out. This principle also applies to bankruptcy liquidation. One of the most serious problems facing our bonds market is that we're still sensitive to the word "bankruptcy". No matter how much regulators lecture about the risks, the result wouldn't be as effective as simply allowing one company to go bankrupt. A fair, transparent, and effective bankruptcy and liquidation mechanisms is better than any preach about being cautious about investments.

Educating investors of different levels of risks associated with different financial product would certainly have a positive effect on the developing of pricing mechanism. Whether it is government bond futures or interest rate derivatives, it provides a risk managing tool and improves market efficiency by enabling investors to choose investment targets according to their risk tolerance.

Ping CHEW
Managing Director and Head of Greater China, Standard & Poor's

We need to increase investor protection and improve the investment environment. An appropriate pricing mechanism should take risk into the equation. This is tied to reforms to the interbank market.

Why are many people terrified at even the mention of default? In the US bond market, there are defaults every year, but it still runs well. In China, on the other hand, excess emphasis on maintaining stability has given rise to moral hazards, where the bond issuers count on governments for bail-out.

We should have a more open attitude to market reforms, accepting temporary fluctuations in return for long-term development. The internationalization of the yuan also needs our market regulation to match international practice. We have come to a stage where incremental progresses no long work. We should be bolder in pushing for reforms. China has a huge market. We're resilient to temporary fluctuations that many consider as destabilizing.

Panel Discussion VIII

Innovation in the Insurance Market and China's Pension System

XU Wenhu/ Professor, Insurance Department, Fudan University

CHEN Wenhui
Vice Chairman, China Insurance Regulatory Commission

A common trend exists in the reforms of pension systems around the world. Starting with Germany, we've seen successful experiences, and also numerous problems. Paths may differ, but I feel there's a return to a concerted effort between governments, corporates and individuals, under an efficient market mechanism.

My views are two-fold: firstly, the role of the government shall reduce from all-round responsibilities to focusing on basic retirement needs and those of the vulnerable and disadvantaged. The British and German governments are already pushing for reforms in this direction. Secondly, through guidance, regulation and monitoring, the government shall establish a multi-faceted, multi-layered pension system. We've seen during the European debt crisis that governments cannot take on too responsibilities.

There are three challenges facing China's pension system. First of all, the program of basic old-age insurance system faces a large financial shortfall – this is a consensus among various researches.

Secondly, the program's coverage is neither universal nor fair – we have a vast rural population, fragmented and parallel policies, and east-west disparity. Companies are under a heavy burden to contribute to the scheme, which strangles their competitiveness. Compared to basic old-age insurance, the other two important pillars of old-age insurance – corporate annuity and voluntary private pension scheme – are still feeble.

Lastly, we need to clarify the respective roles of the government and the market in the pension system. The government may step in where the market fails; but when the market works well, the government shall monitor on the side. Also, basic old-age insurance must extend to all regions of the country and to all occupations equally on a sustainable basis. We need the market to boost the efficiency of the system, and minimize the cost. In addition, it's crucial to provide policy support for the second and the third pillars' development, because the basic insurance system only covers fundamental needs.

LI Chunping
President, Changjiang Pension Insurance

China is getting old before it gets rich. The accumulation of our pension fund is severely insufficient. Adding the pension funds from all three pillars and the balance of national social security fun, we've got only 7 trillion yuan. The US, on the other hand, has US$ 18 trillion yuan. There is a huge gap between the two countries.

Chinese people are known for their habits to save. American people also save for old age, but their savings are invested in the global capital market, while ours stay in the bank. China's pension funds have not benefitted from our high economic growth.

So how do we solve this problem? Two things: first, more sources of contribution. We cannot rely completely on the government for solving China's pension problem. Every enterprise and every individual must play his own part. In future, corporate annuities and private pension schemes must play bigger roles in the accumulation of pension funds.

CHEN Wenhui

LI Chunping

DU Yongmao

Second, we need to speed up the marketization of pension funds. The US has provided a great example of investment-driven pension system, with 40-45% of its pension funds nationwide coming from investment returns. In the past decade, the average annual return rate on China's national social security fund is 8.41 percent, which means 280 billion yuan out of the fund's current size of 800 billion yuan came from investment returns. On the other than, the basic old-age insurance, which is worth 1.9 trillion yuan, is almost all deposited in banks with an estimated annual return of only 2 percent.

In terms of investment modes, we would like to see more entities participating in the management of pension and social security funds. We need to broaden the domain in which our corporate annuity funds can invest. On that front, we've been making tentative steps in recent years. We also need more professional, specialized asset managing companies to manage our pension funds. In this respect, insurance companies can take advantage of their strengths and play significant roles.

DU Yongmao
Chairman & CEO, Ping An Annuity Insurance Company of China

The fundamental reason that our pension funds are severely lacking is the unbalance of our pension system. We are too reliant on the basic old-age insurance system. Our pension accumulation is lower than not only developed countries but also developing countries such as India, Brazil and Russia. It's mostly due to the insufficient development of our second and third pillars. The third pillar is almost non-existent, while the second is barely established. It's imminently important to develop the second and the third pillars.

The growth of pension funds cannot entirely rely upon contributions. Investment income is the key. The reason why we don't have enough pension accumulation is because we haven't invested the pension money wisely. Investment incomes can be boosted if we manage the money in a market-oriented way. This is yet to be fully recognized by the government and the society. The specialties of professional financial institutions are yet to be fully utilized.

To improve our pension system, I suggest we 1) make up for the 1.7-trillion-yuan deficit in the basic old-age insurance scheme as soon as possible; 2) expand the scheme of corporate annuity from enterprises to government agencies; 3) introduce tax-deferred pension saving program; and 5) expand the investment channel and domain allowed for pension funds, so that they may benefit from our national economic growth.

John R.DACEY
AXA Group Vice Chairman for Asia-Pacific

I'm going to talk about mainly three points. First of all, the pension challenge of china is truly unique. Most governments of the western world have a pension crisis. But that crisis was created because politicians and to a lesser degree some corporations made great promises to the people, and they haven't found the money to pay for it. It's easy for a politician to make promises, but it's difficult to find the money. China's deficit for the first pillar however, accounts for only 2% of the GDP,

John R.DACEY

Bob PEI

Steven CHANG

which is manageable. I have no worries about the Chinese government's ability to manage the first pillar.

China's challenge is a demographic one. The traditional population pyramid has been inverted in China. The maximum number of Chinese people in working age will peak in 2016, and in the next 50 years this number will keep decreasing. The challenge facing China's pension system is how to manage a true pension system for people retiring in the next 50 years. The second and the third pillars, namely corporate pensions and individual private pensions, must develop quickly. The good news is, the population is used to saving. The bad news is, those savings tend to be in relatively short-term instruments. We need to develop the second and the third pillars to allow people to have the kinds of assets when they retire, that accrue not just from the contributions, but also from the investment income.

So a couple of quick thoughts. First we need to start accelerating the development of these pillars, and we needed to start it yesterday. The delay that's occurred for the tax-deferred incentives on pilot programs must stop. We need to launch these pilots, and expand them quickly.

Secondly, we need to make it easy for people to participate. One of the things the government can do in addition to providing tax benefits for pensions is that they can, at least for the corporate pensions, challenge corporates to provide this coverage to everyone, and make it difficult for people to opt-out.

Thirdly, we need to be able to put these funds in either insurance companies or dedicated pension funds where the time horizon is correct. With the 20, 30, 40-year time horizon, people can then make investments in risk assets. The pool of assets available for retirement funds should be large, and people should be able to make choices - and take risks - so that the return can be a lot more than the simple return on their checking accounts in a bank.

There's a big role for insurance companies. The challenge of a changing demography is not unique to China: people are living longer worldwide. Insurance companies globally have been working through this kind of challenges. We look forward to playing a role in thi.

Bob PEI

CEO, Sino-U.S. United Metlife Insurance Company Limited China

It's apparent that among the 'three pillars' of China's old-age security system, one is disproportionally large. If continuing like this, it's going to be a huge problem. The cause of the current situation is not that the government is doing too much. It's that companies and individuals are doing too little. In that respect, I think we need to create more awareness. That's the first step towards a real solution. Self-awareness is precious. Once all the sides, including the regulators, government agencies and the insurance industry, have realized that the problem exists, it's going to be a very good opportunity.

How do we strengthen the other two pillars?

First we need to let everybody know, that our system is not complete. We've got a social security coverage of only 43%, totaling about 3.2 trillion yuan. More must be covered, and this must be done through adjustments to government policies. Another aspect of the solution is institutional innovations. There are a couple of very good examples, such as Shanghai's corporate pension pilot, and the compulsory universal pension of Taiwan. Of course these pilots are not perfect, they cannot solve all the problems, but at least it's a start. On the policy side, we need the audacity to take steps.In terms of the entity of insurance, we can push for reforms through introduction of new products. Our company has done pilot works. The sales volume is not large yet, but everything takes time. The purpose is to convert to an investment-driven pension.

This requires two conditions. First, for individual accounts, tax incentives must be provided. Individuals should be able to choose between different options, and between different combinations of options. For publicly pooled decisions, the company faces an awesome responsibility, to match assets and liabilities.

In conclusion, we need to create awareness that our pension system is in a sound state. Secondly, we need to have the courage to implement reforms and policies, especially in terms of corporate pension pilots. Instead of striving for perfection, let's first get it started, because once it is, people can feel it, and may be encouraged to participate.

Steven CHANG
CEO, Munich Re China

China is an aging society. In the years of 2025-2030, we might become an ultra-aging society. For the problems of pension that will arise then, the government, enterprises and individuals must plan ahead today. Currently, among the three pillars in a pension system, our second and third pillars are severely underdeveloped.

I'm concerned about two things. First is the pension provision for blue-collar workers. For the cohort with lower incomes, how the pension fund will be operated, how big of a hole there is, these are all causes for anxiety. The only way to dissipate such anxiety is through the government's first pillar, which needs more transparent operations, and openness to the community. Second, for white collars, which refer to the cohort with middle to higher income, their post-retirement living standard will be severely affected because the current basic insurance system caps contribution at three times the societal average income. To maintain living standards for this group of people, we need to develop our second and third pillars.

To solve China's pension problem, we need the government, enterprises and individuals to all be responsible and work together. A responsible government must have a top-level design for China's pension system for the next 30-50 years. This should include not only the first pillar, but the second and the third as well. Enterprises, on the other hand, must think about how to push further for corporate pensions. Those of us who run pension businesses must think about how to invest responsibly. Finally, as an individual, we are all responsible for securing our own old-age provisions.

John CAI

John CAI
Chief Executive Officer, AIA China

The roles of government, corporate and individuals must be clearly defined in the pension system. Other than government support of the second and the third pillars, the basic infrastructures that are needed for the refinement of our pension system is a task beyond the ability of enterprises.

Hospitals, long-term care providers, community hospitals, etc. – these shall be prepared early. The US had a baby boom between the years 1946 and 1964 – these people counts for 1/3 of their entire population. Many economists believe that what drives economy and social development internally is population. The twenty years of bull market between 1982 and 2002 was in fact driven by the baby boomers when their income and savings peaked.

That requires government policies with foresights. Infrastructure support needs to be provided as soon as possible.

Secondly, once the roles are clear, we need to figure out a way to fill up the funding gap. The government, enterprises and individuals must work simultaneously. The early introduction of tax-deferral is going to benefit all three parties.

Finally, with such a huge funding gap, many see a huge crisis. But danger and opportunity goes hand-in-hand. Statistically, the consumption power of a retiree is four or five times as large as a working person. So we shall pay some real attention to the research of the retiree market.

Panel Discussion IX

Shanghai as an Asset Management Center

Jason SUBLER/ Shanghai Bureau Chief of Reuters News, Thomson Reuters

WANG Zhe
Chairman, Shanghai Gold Exchange

Currently the savings rate of China's citizens is 38 percent of GDP. China is already becoming a country with a large population of elderly with social and welfare needs. Both of these facts show the importance of having wealth management. At the same time, a government report mentions raising property income for citizens. I think creating a financial center in Shanghai is extremely important. In order to do this, first we need some specialists, professionals in this field. These professionals must be held to a high standard of ethics and values.

Secondly, we need complete and appropriate legislation regarding assets management. Disputes will arise we don't clearly define the responsibilities of all relevant parties involved in the wealth management business.

Thirdly, we must have an open market. We cannot attract excellent financial organizations or businessmen to Shanghai without a free and open market. Exchange wouldn't be able to occur between China and the rest of the world and it would be impossible for Shanghai to have a true financial center.

Lastly, we need a complete, coherent infrastructure consisting of lawyers, accountants, and other relevant business professionals. We should have an educational structure to teach and protect investors, to tell investors that finance is a serious business which takes long-term commitment; it is not just a way to get rich in one day. We need an appropriate oversight mechanism, there always have to be some rules to follow, but excessive oversight is obviously not the answer either.

GUO Tianyong
Professor, Central University of Finance and Economics

Wealth management constitutes an important part of finance. Shanghai wouldn't be an international financial center if it is not also built into a global wealth management center. In the past few years many foreign people have come to China. If we don't have a good wealth management platform, they will expatriate their earnings abroad. This way a lot of money leaves China, which is exactly the opposite of what we need in order to build a financial center.

Last year we conducted a study of private banks to find out the number of high net-worth individuals, people with assets and investments worth more than 10 million yuan. At the end of 2001, this figure was 1,185,000. That is an increase of 17 percent. By 2015 the number may rise to 2,193,000. Fourteen percent of these high-net-worth individuals are in Shanghai. This is a high proportion, so it's very important for us to create an international financial center in Shanghai.

Banks are in an advantageous position when it comes to wealth management, because they have the most distribution channels are traditionally trusted by the public. But as investors diversify there will be demand for more complex wealth management products. This is good news for high-net-worth individuals because the competition among wealth management firms means better services for them. We need to encourage the diversification of wealth management products. There still a lot of work to do. First, we need to


WANG Zhe


GUO Tianyong


WANG Shuidi

work towards the diversification of the financial management market. Second, we should provide more space for innovation and improve the supervisory mechanisms.

China's financial sector got to a late start compared to the West. This mostly has to do with structural issues, but traditional Chinese views towards risk are also related. This has led to some inefficiency in the financial sector. The reason supervisory structures have become more stringent is to control risk. The government is very concerned about risk, but this has resulted in excess interference which decreases the efficiency of the financial market.

WANG Shuidi
Deputy General Manager of Private Banking Department, Agricultural Bank of China

Banks are increasingly treating wealth management products as an alternative means of deposits. They use wealth management products to attract deposits toward the end of each month. This creates large fluctuations in deposit levels and is bad for banks' management.

In addition, some asset management firms tout their wealth management products with forecast high yields without revealing the fact that the risks are high as well. Investor themselves are also partly responsible for this, because they frequently move their cash among various asset management firms in pursuit of higher short-term interest rates.

I have three points of view about building an asset management center in Shanghai. Firstly, we need to make it clear that the capital market serves not only the real economy but also investors. There should be more institutional investors participating in the market. Secondly, the city needs to develop various wealth management firms and build a network that involves the firms as well as research centers and rating agencies. Thirdly, we should cultivate talents, and have them ranked and certified for promoting products at different risk levels. This is also very important.

QIAN Jun
CEO, Hwa Trust

There is a misconception in China that only the rich can do wealth management. In fact, common people should be able to do wealth management as well, through the services of a variety of financial institutions, including banks, securities brokerage, trusts and mutual funds. In this regard, Shanghai definitely has the capacity to become a wealth management center. To achieve this goal, we also need unified regulatory standards and better cross-department coordination.

Trusts have grown rapidly over the years. Now the sector has expanded to more than 5 trillion yuan. Despite cheering statistics, there is still a sense of crisis, partly because trusts are still a peripheral sector in the financial industry compared to other businesses. Trusts firms are not allowed to go public yet. They are also subject to many other restrictions.

China's capital markets are developing fast. Yet we still need to pay more attention to the improvement of regulations, the quality of financial professionals and the maturity of investors. We don't' have enough institutional investors in the market. Much money in the insurance and

QIAN Jun

HE Yong

WANG Jingbo

pension businesses is yet to be invested in the capital market.

We also need to improve the financial infrastructure. Installing a coherent structure, set of management facilities is related. In the past, we have admired the U.S. in terms of financial innovation. But then there was still the financial crisis there. On top of that our fundamental facilities aren't as good as the rest of the world, but they are developing quite quickly.

HE Yong
Vice President, Ping An Trust

To build Shanghai as a financial center, we need to have a stronger trusts sector. We need to provide a comprehensive and supportive service network for trust companies and explore innovative methods for trusts products to have more liquidity.

Ping An Trust has been devoted to private wealth management for years, providing China's high-net-worth individuals with customized asset allocation and wealth management services. We have focused on developing products and distribution channels. Our wealth management products are diversified with various risk levels and with maturities ranging from one week to eight years. We develop new products partly through internal-driven innovations and also with the benefit of cooperating with other companies. This year we are under a lot of pressure to seek investment projects. By around 2015, Ping An Trust will be transformed into either a private bank or wealth management firm.

WANG Jingbo
Initiator, President and CEO, Noah Holdings

Developing an international financial center isn't simply increasing the number of licenses for banks and trust companies. It's a matter of developing independent, specialized asset management companies.

Noah Holdings is an independent wealth management firm in Shanghai. We are the only company in the industry that is listed on the New York Stock Exchange. We are a part of the services industry, especially for providing asset allocation and financial services to individuals with high net worth. The development of Noah Holdings has some resonance with the overall development of financial management in China. 2002 to 2005 is when we noticed many of China's high net worth individuals weren't using wealth management services, and we saw that there was a market for this, that there was potential.

Starting three or four quarters ago, investors have become more cautious. One reason is the changes in the slowdown in international and domestic markets. This year it was very obvious that investors like fixed-income investments and are cautious about buying products with a long maturity. This means wealth management market is entering a new phase. In the past, investors were mostly interested in stocks and real estate investment.

Now they are increasingly diversifying their investment portfolios. The longer Chinese investors invest in wealth management products, the more internationalized their views would be. Throughout the last decade, many wealth management firms focus on domestic yuan businesses. In the next five years, they may start US dollar businesses as demand grows.

Panel Discussion X

New Opportunities for PE Cross-border Investment

Moderator: LI Bin/ Vice Editor-in-Chief, Shanghai Securities News

WANG Zongnan
Chairman of the Board, Bright Food Group

After three decades of economic reform, state-owned enterprises that survived the changes are all outstanding. But their competitive edges are still limited to the domestic market. In order to compete internationally, we need to accelerate overseas acquisitions, which is a very effective path. In recent years, Bright Food has made acquisitions in many foreign countries. During the process, I have witnessed the effectiveness of private equity investments, through which all these acquisitions were made. Thanks to their global vision, professional analysis and expertise, private equities can help Chinese state-owned enterprises explore overseas.

There are two major problems with domestic policies in this respect. The first has to do with the SASAC's regulations of state-owned assets management. If the same rules apply to firms making overseas acquisitions, there will be operational problems. I suggest the regulations be relaxed to allow for more flexibility. Secondly, the current practice in our feasibility analyses focuses on the profits of the target company. But for overseas acquisitions, due to different financing interest rates, tax systems and accounting principles, it's sometimes difficult to reach a consensus. The ideological conflicts – such as our assessment of target companies for overseas acquisitions – are equally important, if not more so. For Chinese enterprises to 'go abroad, ideas are more important than policies. The managerial style and approach of Chinese companies and the regulators need to be improved to match international standards.

Nick GOOD
Managing Director, Asia-Pacific Head of Strategy and Business Development, Blackrock

One of the biggest areas of Blackrock's focus is cross-border investment. As you look at the opportunities for Chinese companies, clearly the depressed prices that we see around the world, creates tremendous opportunity to acquire talents, know-how and distribution in markets outside of China. When we look the other way, despite the valuations in the stock markets, many corporations are sitting on very large cash pools. And the opportunity for them to invest that in China is one they're looking to do, but often don't know how. Private equities traditionally focus on raising capital, and using the leverage to generate higher return. While that still has value, particularly for small and mid-sized companies, we believe the real value-add comes from partnering with and helping these firms to grow through the provision of expertise.

I think that private equity is changing and that's where we see opportunities to differentiate in really credible private equity firms whether it's cross-border into China or out of China. The ability of private equities to identify opportunities is important for Chinese firms wanting to go out, as well as for firms looking to come into China. It's hard for smaller firms in particular to identify opportunities for potential acquisitions.

We believe there are three other ways that private equity firms can really differentiate. The first is on the

WANG Zongnan

Nick GOOD

Henry CAI

way in. Structuring these deals effectively is very challenging, whether that's capital raising, political considerations or legal structuring insuring regulations are covered – all those things are hugely important to insure that the deal is set up in the right way, and that's an area of value-add on which private equity firms are very strong.

The second way to different is in post-deal management. To integrate and get the most out of cross-culture acquisitions is very difficult. To motivate employees and maintain the focus, deal with counter parties, negotiations – many of these things are very different for Chinese firms going off-shore or for foreign companies coming into China. The level of expertise that we can provide in that process is tremendous. In addition, private equity firms can help source unique experts from around the world, who can advise and help ensure that the growth goes beyond the provision of capital.

And finally the exit from a deal. Private equity firms can make sure that's monetarized effectively.

As we look at the potential of private equity firms to support cross-border trade, it's in our ability to create value, and to go beyond simply providing capital. That's where we are looking to differentiate for PE firms to move forward in China.

Henry CAI
Asia Chairman of Corporate Finance and Member of Pacific Executive Committee, Deutsche Bank

The world has changed astoundingly. Stock prices have never been lower. Chinese stocks, whether in the US or Hong Kong or China, are all worth nothing. 60% of banking stocks are all low-grade assets. The economy has never been so bad, with so many uncertainties. This time it's real. Don't expect it to get better within 15 years. Europe is doing badly, the US relatively better, and many uncertainties in China. We always say, oh it'll get better. We hope so, but the challenges are apparent. The American market has never looked at Chinese companies with such a grim view. Of course there're many other challenges, for banks and for private equity firms. What does all this entail? I think, for Chinese companies and for PE firms, this is a great opportunity.

In the past, what China didn't have we bought from abroad. It's the same today. Secondly, don't buy equities willy-nilly, especially those not listed yet. We buy what we lack, that pertains to assets as well. Thirdly, upgrade our industries. To really have the ability of core technology researches, we need upgrades. What about things necessary for such upgrades that we don't have? Buy them.

Domestically viewing, reforms at state-owned companies have started, while the children of the newly-rich have begun taking over business management from their elderly. There is a process of asset consolidation and integration going on.

Money is not equal to successful acquisition, especially in industries such as pharmaceuticals. Brand recognition is also very important. The acquisition process is a dynamic one, and one of collaboration, mutual respect and trust. The government needs to strengthen its credibility and improve its regulatory strength and effectiveness, especially when it comes to the regulation of domestic

Neil SHEN

Richard ZHANG

John ZHAO

acquisition market.

Neil SHEN
Founding Managing Partner, Sequoia Capital China

Most Chinese enterprise acquisitions in the early years were in the fields of mining and energy. In recent years, we see more and more technology-driven industries joining this trend, such as high-end manufacturing, clean energies, medical industries and consumer products. These sectors generally need more human capital than the old ones. This is where global PE firms can play a very important role. Firms such as Sequoia, with our globally recognized brand and resources, can help Chinese companies to 'go abroad', and we can provide outstanding support when it comes to connections and understanding the local markets.

On the other hand, an increasing number of foreign companies want to tap the Chinese market, through forms such as establishing joint ventures companies or introducing Chinese capital investors. When we look at the internet, among the most successful American companies – Facebook, Yahoo, Amazon - none played the game well in China. The primary reason for this is that their products haven't been localized enough to attract Chinese customers. These companies would have far better development if they can integrate local resources, especially local talents and industrial resources.

Synergy is a necessary element in the acquisition process. As financial investors, we work with strategic investors because they can bring out this synergetic effect. Communication between the two sides is crucial. With overcapacity in many sectors, it is important that we upgrade our industries. Cross-border acquisitions could be a solution. You can acquire technologies abroad, but you must also have the ability to digest this technology, which is crucial for fostering our own differentiated high-end manufacturing companies. Chinese enterprises today are different from those twenty years ago in terms of the ability to digest technologies. It was difficult in the past, but we have our own technological talents who understand them. If we can digest well, with our local advantages on the Chinese market, we can exchange part of our own technologies, in addition to market and capital, for other people's technologies, instead of the old ways of market for technology. Only in this way, can Chinese companies really enhance their core competitiveness.

Richard ZHANG
Partner and the Head of Greater China, Apax Partners

The internationalization of Chinese firms and overseas acquisitions is an irreversible trend. It will only grow faster in the next few years. In 2006, Chinese overseas investment was US$ 18 billion. Last year's figure was 60 billion, which is almost on the same level with 2006's foreign investment in China, which amounted to 66 billion. This trend merits our attention.

While expanding globally, Chinese companies should keep their feet firmly on the Chinese ground and seek development in domestic competitions. The ultimate purpose is to obtain competitive edges in the Chinese market. At least in the next 20 years, China's growth potential is going to be better than that of other developing countries, for we still

HAN Weiwen

have a long way to go in terms of urbanization and industrialization.

Private equity firms can help Chinese enterprises from two aspects. On one hand, they can utilize their strengths to help Chinese companies identify good targets and opportunities for overseas acquisition. On the other hand, they can reduce the risks of overseas acquisitions with professional risk management skills.

John ZHAO
Founder and Chief Executive Officer, Hony Capital

China's development is unique in two aspects. First, it is transformed from the world's factory to a cradle of enterprises and entrepreneurs with great ambitions and ideas; Second, China has the fastest-growing and relatively deep-leveled consumer market in the world.

I pay special attention to two kinds of people in China: entrepreneurs and consumers. Starting from these two core groups, we can make Chinese companies global; and global companies Chinese. There's no lack of entrepreneurial spirit in this country, and the will to succeed. Many have established themselves domestically, and now looking to go beyond the border. For us, this has created lots of space.

On the other hand, in the past 30 years, we have been preoccupied with being the world's factory, and neglected the demand of domestic consumers. But in order to fulfill that demand, it takes years of accumulations in aspects such as technologies. We have a huge number of technological talents, 7 million graduates each year to be exact, but this is not enough, it takes a pool of technology as well. We also need to accumulate brands recognition. Take ladies' handbags for example, international brands with hundreds of years of history still have the edge over Chinese ones. When consumption is shifting from practicality to value, the Chinese companies are not paying enough attention to this. At the same time, localization becomes a new question for foreign companies as well. For opportunities in both realms, private equity firms have the expertise, the experience, and the global resources.

In addition, I'd also like to share some of my thoughts. All this originates from the urge of enterprises and entrepreneurs to develop and to expand, and acquisition is a well-known path. But scholars, experts and consultancies have noticed that many merger and acquisitions failed. But companies keep jumping in because the rewards are huge for winners. In my opinion, to succeed, you must first have a clear strategy and then prepare tactics accordingly. This is where PE firms can do a lot.

During the development of Chinese companies, government should refrain from intervening too much. On the other hand, we also hear a lot of complaints that it's difficult for foreign capitals to enter China. If China is to join the world, it must develop a market-driven economy and use its political influence to prevent other countries from pursuing protectionism.

HAN Weiwen
Partner, Bain & Company

In the past 20 years Bain has been monitoring more than 2,000 listed companies globally. We found that only one out ten maintained steady growth at about 5-6% annually. We think the reason for their success is that they have always focused on their core business. For Chinese companies, their core advantage is the domestic market.

For many enterprises, it's reasonable to make overseas acquisitions when they reach a certain growth stage. Yet it is extremely important to be prudent when choosing investment targets. Many scholars have compared this wave of overseas acquisition by Chinese firms with that of Japan in the late 1980s. But there're lots of differences in areas such as industrial structures and domestic market potentials.

Private equity firms can play a significant role in these overseas acquisitions. They are experts in investment and are more professional when it comes to asset evaluation. Traditionally, 70-80 percent of Chinese private equity firms recover their investments when the invested firms go public. But given the recent slump in the capital market, this may not be a good choice.

We began to notice recently that more and more Chinese private equity firms intend to increase their holding in the firms they invested in, until they can exit by selling the equities to another investor. This may be the trend for the next one or two decades to come.

Night Chat by the Huangpu I

Growth Economies and the Global Economic Prospect

Moderator: James AREDDY/ Shanghai Correspondent, Wall Street Journal

ZHANG Jianhua
Director General, Research Bureau of the People's Bank of China

People's Bank of China adjusted interest rates in response to both the worsening European debt crisis and the slowdown of economic growth at home. China's economic growth has been slowing since the second half of last year. The policies should be fine-tuned to adapt to the change.

Most recently, we lowered banks' interest rates and widened their floating range. This is also a step taken toward liberalizing the interest rates, which is a state goal in the 12th Five-Year Plan.

The current situations present a moment of opportunity for banks, because during this time the country's financial institutions will see an increase in autonomous pricing rights. Specifically, interest rate ceilings will increase for deposits, and decrease for lending. This should grant ample space to steer interest rates in a more market-oriented direction.

Much of the new monetary policy is a response to the global economic stability triggered by Europe's debt crisis. From this year onward, as a reflection of the Euro's relative instability, China's inflows of foreign exchange will be reduced significantly, resulting in less yuan released to the domestic market. This comes at the same time as a gradual strengthening of the yuan against the dollar -- in May of this year, the yuan appreciated by about 2.5 percent against the US dollar. If this trend continues, the yuan's credibility in the international arena will improve as well. Overall this is a very good sign for the yuan as trade and investment are increasingly internationalized.

The structure must be changed. This means increased participation by the private sector in industries which have large market dominance

But the Chinese banking system is still reliant on a stable global order, especially because the yuan is not yet fully convertible. To maintain stable conditions is especially important to facilitate the growth of developing economies, of which China is by far the largest. With a European Debt crisis and a slow recovery in the United States, coupled with weak Japanese growth, these developing economies are simply not powerful enough to stabilize the global economic system, even as they contribute greatly to the world economy.

Because the emerging economies are influenced so greatly by a fluctuating global system, we see a rapid flow of capital into and out of the stable economies, which is not a good thing. Both the emerging and developed economies have work to do if we want to stabilize the global financial system and ensure future economic cooperation.

PENG Wensheng
Chief Economist & Managing Director, CICC

There are three sources of the

decline in China's economy. First, to control inflation, the government instituted restrictive policies. Second, policies to address to the real estate bubble have affected investment in real estate. Third is the situation in Europe and the decrease in international demand. We face a challenge – how to have stable growth and modify China's economic structure.

The biggest issue in modifying China's economic structure is how to control the real estate bubble. During 10 years of expansion of the real estate market, prices rose too quickly, costs rose, and resources were devoted in excess to the real estate industry. The resulting regulation of the real estate industry has caused investment in real estate to go down which has had a negative impact on aggregate demand as a whole. This causes the expectation for a loosening in regulation. But we have to think long-term – continuing to regulate the real estate market is an important part of sustainable growth.

In the past 10 years, a stark imbalance of allocation of foreign-exchange assets has accumulated among the private sector and the government. The amount of foreign-exchange reserves the government holds is 3.3 trillion US$ whereas private sector foreign debt is 1.3 trillion US$, about 17-18 percent of GDP. Foreign-exchange flows reflect short-term fluctuations in the global capital market, but in terms of a long-term trend, the issue is whether this imbalance of asset allocation is at a breaking point.

To return to the issue of economic reform, the consensus about the appropriate actions to take has grown over the past few years. First, the structure must be changed. This means increased participation by the private sector in industries which

ZHANG Jianhua

PENG Wensheng

QU Hongbin

have large market dominance, such as finance, energy, and transportation. Second, there is a lot of controversy about tax levels despite the fact that compared to other countries tax revenues make up a relatively small proportion of GDP. In the past 10 years, tax revenues primarily went to investment and public services. The government should turn its focus to welfare and public services. Third is financial reform including liberalization of interest rates and the liberalization of capital accounts. This includes flexibility in the yuan's exchange rate.

QU Hongbin
Managing Director & Chief Economist of Greater China, HSBC

The Chinese purchasing managers' Index, or PMI, is always seen as a reliable way to test cyclical changes in the manufacturing sector. But since the end of last year, the index has continued to decline. For the first time in years the index has fallen below 50, signaling a stark turn for the worse in the national economy.

Because June's PMI value was lower than that of May, the downward trend in the manufacturing sector is still in progress, with no signs of stabilizing. According to Chief Zhang, the appropriate policy response is to fine-tune the intensity of economic growth, which carries risks if left unchecked. If the growth exceeds 7.5 or 8 percent, then it would be necessary to fine-tune policies to adapt to changing conditions.

A major change along with the PMI is in the size of capital inflows. The number has been significantly reduced, along with the inflow of foreign direct investment (FDI). The decline in SDI is clearly due to external factors, especially in light

Chetan AHYA

Evgeny GAVRILENKOV

WU Enyuan

of the fact that the decline in China is much smaller than the global decline. Because of the global decline there was a large flow of capital out of emerging markets like Hong Kong and Mainland China.

We have also seen changes in China's domestic markets, especially in real estate, where a lot of past asset price inflation is expected. In addition to the expected appreciation of the yuan, our main priority is to maintain the inflow of hot money and cool down overall real estate market. Eventually, these changes will set the state for further financial reform in China, especially exchange rate reform.

China's targeted growth rate of 6 percent is largely a reaction to the downturn in the European climate, and an attempt to steer a new course toward sustainable economic growth. In terms of fiscal policy, economic growth can be contained and stimulated by making conscious choices, such as investing in housing, schools and hospitals. All of these will generate new investment demand and contribute to economic growth in the short term. Large infrastructural projects, on the other hand, like bridges and roads can spur growth in the long term.

Chetan AHYA
Managing Director, Asia Pacific & India Economist, Morgan Stanley

In response to the financial crisis, in the developed world what they had done was a debt swap from private sector to public sector. Now there's the problem that the public sector is also facing challenges. What it means for emerging markets is that we need to find a sustainable solution to create domestic demand. We have seen persistent problems in export growth for the region. The initial response from emerging markets was to just boost growth at any cost. We've seen in the cases of China and India and a lot of other emerging markets, the effort to boost growth was to loosen fiscal and monetary policy. This is a bad sort of growth that they have resorted to.

In China's case we have a situation where demographics are turning but investment to GDP was pushed up from 40 percent to 50 percent. Loan to GDP was moving up from 100 to 130 percent. In India's case they resorted to a very high fiscal deficit. The fiscal deficit moved from 5 percent of GDP to 10 percent of GDP in a year. We've seen a lot of the emerging markets getting hung up on growth and trying to achieve growth through unsustainable means. We all understand doing that for one year; 2008 was a terrible year. Doing that for one year or two years was justified. But doing that for four years has created certain side effects for a lot of the emerging economies now and they are having difficulties sustaining the growth rate. So in our view we need to start looking inwards, because no help will be coming from the developed world.

Evgeny GAVRILENKOV
Managing Director, Chief Economist, Troika Dialog

The world has never had such high leverage before. When the whole world is looking to see how 10 million people in Greece are going to vote, you know there's something fragile in the system. It's not that investors or politicians lack capacities. It's a new situation with unmeasurable uncertainty where you can't apply past experience.

For almost three years the emphasis was mainly on Greece. I'm doubtful that Greece will be able to achieve its goal of reducing the total debt to GDP ratio from 160 percent to 120 percent by 2020. I'm a bit more hopeful about Italy. Italy has industry which is quite competitive in northern Italy.

In Greece, total industry is only eight percent of GDP and agriculture is also very small after Greece joined the EU. The agriculture sector was suppressed and the public sector significantly inflated. I cannot imagine what will be the sources of growth in Greece whereas there is industry in Italy. The budget deficit is shrinking in Italy relative to last year. The economy is expected to fall 1.8 percent this year, but there are chances that with a weaker Europe, the economy may flatten or pick up next year because Italy's economy is able to respond.

Spain is a big worry but there are plenty of other political dimensions in Europe. It won't be a very smooth transition – a banking and fiscal union in the Eurozone. There are so many countries with different national constitutions. It's unclear how local regulations with affect negotiations. There will certainly be a lot of political tensions within those countries.

In terms of the impact of lower oil prices on the Russian economy, the Russian economy is much more resilient to external shocks than in the past. Oil prices fell 27 percent and Russia's currency weakened but a weaker currency is not bad for domestic manufacturing. In May, manufacturing was up by 7 percent. The fact that Russia is connected to the world through pipelines is an advantage in turbulent times because demand for energy cannot go down as much. The Russian economy is mostly getting a volume shock, not so much a price shock. Moreover, growth hasn't been driven by oil; levels of raw material extraction have remained the same. Growth has been driven by medium sized companies in agriculture, manufacturing, service, construction and this will continue to be the case.

WU Enyuan
Deputy Director, World Socialism Research Center, Chinese Academy of Social Science

When comparing Russian and Chinese economic reform, it's best to start with the former Soviet Union. The first steps of Soviet economic reform included the development of light industry and then the division of central power among regional authorities. In 1959, the Soviet Union focused on expanding the autonomy of firms. When China started reform in the eighties, there was extensive study of the Soviet Union's reform model before China pursued its own path of reform.

Gorbachev's plan for Russia was to transition from a planned economy to a market economy. The Russians have a proverb: "Don't tear down the old house if the new house hasn't been built yet". However, if you reject my plan, and I reject your plan, the new house doesn't have a roof, and the old house has already been destroyed. This is the kind of deadlock that caused those reforms to fail.

If you reject my plan, and I reject your plan, the new house doesn't have a roof, and the old house has already been destroyed

Russia's economy has been doing pretty well the last 10 years under Putin. The growth rate between last year and now was four percent. Foreign exchange reserves reached 500 billion US$ and the growth rate this year is at 4.5 percent. Russia's economy is fairly stable, but it is also weak in some respects, especially after the world financial crisis. As a result of the crisis, foreign exchange reserves lessened, outflow of capital and the unemployment rate increased, and living standards decreased.

Medvedev and Putin advocate reforms to the global financial system. Most important is the creation of a fair and transparent system. Second is reform of the single currency system dependent upon the American dollar; there should by a diversified international monetary system. Third, supervision of the global financial system needs strengthening. They believe that the fundamental cause of the global financial crisis was a lack of supervision. These objectives align with how Chinese leaders think.

We promote the voice of countries with emerging economies in the international currency system. We want to create a fair, transparent, regulated international currency fund. We want to expand the voice of developing countries and promote diversity in currency. Countries with emerging economies, like China, have contributed greatly to the world economy. In the last 10 years, 60 percent of the world's GDP has come from countries with emerging economies. These economies have grown 420 percent, whereas developed countries in Europe have only grown 120 percent. Still, the United States has a much larger voice than developing countries do.

Night Chat by the Huangpu I I

Meeting the Financing Needs of Innovative Companies

Moderator: LU Hongjun/ President and Professor of Shanghai Institute of International Finance

ZHU Xinkun
General Manager, Investment Banking Department, Shanghai Rural Commercial Bank

First, we're going to look at some features of innovative enterprises. These enterprises usually have low cash flows in their early stages of development. They don't' have adequate collateral for loans either, which makes it's riskier for banks to lend them money. Higher risks mean banks need to have greater risk management capabilities. Only those that are capable of assessing the growth potential of innovative enterprises and their defaulting risks can survive the competition.

Commercial banks should professionalize their teams, setting up a division that specifically deals with innovative business loans. Three years ago we founded such a division to handle high-tech small and medium-sized enterprises' loan requests. We also developed products and services that suit their special needs.

The launch of ChiNext Board has provided a channel for venture capitalists to exit their investment in startup companies with great profits. It has made innovative enterprises a sought-after target. Financing these enterprises can take the form of not only bank loans but also equity investment. The current regulations, however, prohibit commercial banks from making venture investments.

It is high time that the government relaxed policies in this respect, allowing commercial banks to become Limited Partners of venture capital funds on a qualified basis. Even in financially conservative Japan this is being practiced by many banks. Given Shanghai's objective to become an international financial hub, I think we should consider the possibility of rolling out a pilot program here to experiment with the change first.

The lending infrastructure is set up for lenders interested in SOEs and real estate companies, not SMEs and companies in the innovation space

Ken WILCOX
Chairman, Silicon Valley Bank

I've spent my entire career working oly with early stage, mostly venture-backed technology companies. I've been with Silicon Valley Bank for 23 years and I was the CEO for 10 until a year ago when I became Chairman and moved to China. For the past year I've been setting up a joint venture bank with Shanghai Pudong Development Bank the purpose of which is to address the needs of the innovation space in China. We have a license from the CBRC and we're hoping to complete set up very soon. At Silicon Valley Bank we work with technology companies often before they meet their first equity investors until they become acquired, so we say from cradle to grave.

Here are eight obstacles I see in China in terms of lending money to companies in the innovation space in China. First, the lending infrastructure, specifically in regard to collateral, is set up for lenders interested in SOEs and real estate companies, not SMEs and companies in the innovation space. Second, the same concern applies at a general level for lending regulations. Third, there should be a flexible rate system to enable commercial banks to take risk into account. Fourth, government agencies should provide support to commercial lenders. Fifth, there should be earlier screens for financing to shift the emphasis from quantity to quality. Sixth, entrepreneurs need to understand and utilize the distinction between debt and equity. Seventh, the venture capital community needs to be interested in getting involved at an earlier stage. Finally, entrepreneurs need to be less opportunistic and more focused.

ZHU Xinkun

Ken WILCOX

HUANG Ming

HUANG Ming
Professor of Finance (La Caixa Chair), China Europe International Business School
Professor of Finance, Cornell University

The development of innovation among Chinese firms is extremely important. In this world economy, China needs to be able to compete with very innovative companies in Europe and in America. Even though China's economy is the 2nd largest in the world, there are few innovative Chinese brands. South Korea has some of the finest companies and this is a result of innovation.

One of the reasons for the lack of innovation among companies in China is the environment the system creates. Among the examples of innovative companies, most spend many years doing research and development. During this period these companies are not making a profit. Extremely long-term investment is needed for this to be able to happen. However, many Chinese firms face periods where property rights or the legal system is uncertain, so they spend a lot of effort in making a quick buck instead of spending eight or ten years on an investment program. We're missing this long-term incentive and this type of environment. A lot of resources go to state firms where leaders are not concerned with investment or innovation.

For innovative firms to develop well they must have the assistance of financial services. They need external investments for a long period of time. This leads us to the topic of creating a Silicon Valley in China. I've always said that Silicon Valley has been successful partly because of historical legacies and, more importantly, because the facilities and services for innovative companies are already well-entrenched and can hardly be matched by other regions even today. Another reason for the success of US companies is the quality of the US financial system. This is important because innovative companies need support and financing. The miracle of Silicon Valley is the marriage of investors and entrepreneurs.

Many people criticize the ChiNext Board. I know there is a bubble and there is over-valuation. But in terms of helping out Chinese companies, the market is important. Companies that couldn't find investors before can now.

Finally, there are still many obstacles. China needs to tie together innovation and finance. The government needs to protect the interests of investors and entrepreneurs especially in terms of its legal framework. In order to get companies and investors interacting in a market there must be a flexible but rigid legal and financial environment.

Duane KUANG
Founding Managing Partner, Qiming Venture Partners

Qiming is a venture capital fund. We currently manage three US-denominated funds and two yuan-denominated ones with a total value of US$ 1 billion. Our main investments are in the areas of internet, information technologies, healthcare, and clean energy.

Innovation is not limited to technological innovation. In China, every stage of economic transformation has many types of innovation. Here's one example not related to technology, one of our investments – VANCL. VANCL is currently China's biggest clothing e-commerce company. The most remarkable thing is that VANCL is a private brand with its own designers, unlike many other e-commerce companies such as Taobao. These are great companies but their products are all third-party. For a long time, China has been a huge textiles exporter, mostly manufacturing and processing, not design much less brand creation. VANCL stands apart in this regard. The success of VANCL depends on the expansion of middle class consumers. In terms of innovation and transforming China's export economy into a consumption economy, VANCL is a great example.

But it would be irresponsible to urge commercial banks to lend to startup companies such as VANCL at the current stage. The best way to help these innovative companies is through not bank loans but private equity at their early stages of development. These companies are new in China but we can learn from American's experience. For 30 years in the U.S., each wave of innovation was inevitably linked to the participation of equity investment.

Duane KUANG

WANG Ren

QIAN Xueyu

Over the last 10 years many American venture capital funds have been investing in clean energy. Many of these investments have already failed. But there are still investors who believe this industry will grow and one day the payout will be huge. I believe that one day this will cause American clean energy to be ahead of the pack.

How should China promote the development of new, innovative companies? Originally it seemed like a long period of time was needed, but now China has an opportunity: the launch of the ChiNext Board. The launch of this market has allowed a lot of private equity structures and the companies they invest in to make money. This has attracted more than normal investors to the PE market. Despite all shortcomings of the blind pursuit, it motivates private capital better than any official campaigns. What the government needs to do now is not to repress these investments for risk concerns but to guide investors to value the firm's long-term growth potential when choosing investment targets.

WANG Ren
President, Asia and Head of Investment Banking and Capital Markets, Jefferies & Co.

The greatest waste of Chinese resources is to deprive 1.3 billion people of their innovative capacity. This repression is being carried out in three ways: first is the traditional culture that has some repressive element. Second is the education system, which prevents students from challenging their teachers' points of view. Third is the political system. The reason companies like Apple and Microsoft exist is because of a strong system of design, repair, and patent protection, among other fundamentals -- all of which China lacks at the moment. European culture, on the other hand, is still reliant on decades-old companies like Siemens and ABB, simply because it does not have a robust financial system to support innovative development.

There are several problems with the capital market when it comes to supporting innovative enterprises. On one hand, investors participating in the market are not diversified enough. In China, for example, private equity investors usually focus on the same few startup companies while neglecting others. In overseas market, most investment funds favor large companies' stocks over those of small and medium-sized enterprises. Chinese concept stocks are having a hard time in US stock markets. Small and medium-sized enterprises also find it difficult to raise money from listing in Hong Kong's stock markets, because most investment funds only subscribe to large companies' initial public stock issuance.

Another major problem is that a few businesses groups have come to dominate all financial intermediary services around the globe. After the 2008 crises we saw a substantial drop in truly innovative companies providing financial services.

There are a few things a financial consultancy needs in order to support innovative companies in the capital market.

To begin with, you need to have experts that dedicate to valuing the firms and providing services to them.

Secondly, it is very important for firms like us to facilitate transactions of small and medium-sized enterprises' stocks in the secondary market, because they are usually worth only several million US dollars, hence the low liquidity.

Lastly, you need to develop a large pool of investors for startups and small and medium-sized enterprises. Last but not least, to serve innovative companies, the intermediary agency itself needs to be innovative.

QIAN Xueyu
CEO, Ideal Energy Equipment (Shanghai)

Ideal Energy Equipment (Shanghai) Ltd. was established in August 2009 in the Pudong district of Shanghai in the Zhang Jiang technology park. We do research and development as well as produce high end equipment that uses solar cells. After two years we successfully created our 2nd generation of equipment with silicon crystal solar energy membranes. The first generation of machines will go to customers this year for inspection.

We produce three types of equipment originally only produced by European, American, and Japanese companies. The solar cell industry has expanded rapidly. However, last year European governments started reducing subsidies and within a year the equipment market decreased by 80 percent. This shrinking of the market and decreasing prices eliminated a lot of weak players. Once this low point was over, strong companies were able to quickly occupy spots in the market. A new, small high-tech business like ours needs sustainable financing and external financial support.

Chinese concept stocks are having a hard time in US stock markets. Small and medium-sized enterprises also find it difficult to raise money

The high-tech industry has the following general characteristics. First of all, the costs are very high to develop large equipment. Procuding a single unit may cost one billion yuan or more than producing them in scale. We have to release a new generation of technology every three years in order to keep pace.

Second, the risk is large. There is frequently competition between branches of high technology so products are knocked out of competition all the time.

Third is the problem of customer reception since high-end equipment is expensive.

Fourth, just to use the photovoltaic industry as an example, there is a constant need to develop new products to fulfill the demand for better conversion efficiency.

Fifth, the international companies that hold a part of the domestic market have gone through almost a decade of growth. They have the competitive advantage and it's very hard for domestic companies to survive in this environment.

There are three main types of support I would like to see. First, increase financial support for young companies in the form of venture capital. Second, the government should give an appropriate amount of preference in terms of financing and credit assessment for strong companies in the high-tech industry. Finally, the government should develop guaranteed loans as well as intellectual property rights loans. The government should set up communication channels for financial services. All of these things will help the growth of the high-tech industry in China.

Night Chat by the Huangpu III

Developments of the OTC Stock Market in China

Moderator: XU Quan/ Deputy Director, Financial Services Office, Shanghai Municipal Government

WU Guojun
Deputy Director, Professor of Finance, Shanghai Advanced Institute of Finance, Shanghai Jiao Tong University

The international academic community has reached three main achievements in the aspect of Over-The-Counter market research: information asymmetry is an important feature; the service of market makers; and lastly, competition between the market makers.

It should be noted that there have been more instances of OTC market fraud, so the U.S. Securities and Exchange Commission has issued a special warning on the OTC market transactions. Specifically, they warned investors not to treat OTC markets the same as stock exchanges. In addition, in the development of the OTC market, two things are very clear: first of all, the OTC market is unlikely to become an important financing channel. Secondly, the OTC market is unlikely to achieve very much liquidity. With the passage of time many companies will be very disappointed. They should have

WU Guojun

preparation early on.

Some recommendations for the OTC market development in China: First, China needs to establish a number of regional OTC markets and allow cross-market transactions because the number of enterprises qualified for OTC listings are too large to be managed by a single trading platform. In addition, the regulation of OTC markets should give listed enterprises the freedom to decide how much information they want to disclose, while encouraging them to aim for higher standards that apply to exchange-listed public companies. Overall speaking, the design of OTC markets needs to prioritize serving the interests of investors and listed companies instead of making the regulators' management more convenient.

XIE Geng
Director, Market Supervision Department, China Securities Regulatory Commission

Based on my experience in the early development of China's OTC market, I'm going to share with you three viewpoints.

First, it is imperative to restructure and rebalance the Chinese economy. Despite the fact that China has maintained steady growths relative to other countries struggling with the global financial crisis, the recent downturn obviously reveals that investment-driven GDP growth cannot be sustained.

Second, rebalancing the economy requires three preconditions. First, policy support for the real economy and a financial system that encourages entrepreneurship. Second, an optimized resource allocation mechanism that allows market forces to distribute resources. Third, developed factor markets where labor, capital and other productive resources can be efficiently exchanged. These three aspects are related and mutually reinforcing.

Third, we need to establish a multi-layer capital market. Measured by size, China's capital market now ranks among the top in the world. But it is far from enough to satisfy the financing needs of all Chinese enterprises. We need to develop an OTC market that suits China's characteristics. A multi-layer capital market would serve all enterprises at different growth stages. We should develop differentiated regulations for each of the layers based on their risk levels and make sure that investors can have a reasonable anticipation for returns. In addition, the regulators need to strike a balance between controlling risk and allowing enterprises to innovate. This is very important for the sustainable development of the market.

XIE Geng

ZHONG Guanghua
Executive President, Tianjin Equity Exchange

ZHONG Guanghua

The Tianjin Equity Exchange was established in September 2008 in Tianjin Binhai New Area as a pilot for the trading of equities in non-listed enterprises. We have made some progress in four years.

Firstly, we have created a channel for small and medium-sized enterprises to raise money fast and with low cost. As of June 2012, we have helped 162 enterprises raise a combined 4 billion yuan through 194 equity investments.

Secondly, we have been exploring a market-maker mechanism towards the goal of establishing a rational investment platform, which emphasizes creating lasting value in the long-term. In general, the pricing of equities in our exchange has been relatively fair and stable.

Thirdly, we are devoted to helping innovative companies to grow mature enough for a public listing in stock exchanges. Through a variety of services we provide, we have promoted the growth of enterprises in terms of profits and information discloser, which are subject to stricter rules if the company applies to go public in stock exchanges.

Lastly, we have expanded the coverage of the equity exchange. By the end of June 2012, a total of 117 enterprises spreading across 22 provinces and autonomous regions have listed in Tianjin Equity Exchange. We have created a national submarket and 16 regional ones based on the differing needs of listed enterprises. We have also signed MOUs with a number of local governments, an important progress toward establishing a coordinated trading platform that benefits all parties involved.

RUAN Lu

RUAN Lu
Deputy Director, Financial Affairs Office of Chongqing Government Director General, Chongqing Share Transfer Center

I have four points of view about the OTC market. Firstly, regional OTC markets are an indispensable part of a multi-level capital market. They provide scatter enterprises an organized platform for equity exchanges and an opportunity to grow in terms of profits and brand recognition with regulators' guidance and help. This is conducive to their corporate management that will necessary for them to further tap the capital market.

Secondly, the specifics of OTC markets need to be clarified. From my perspective, they should reflect the characteristics of OTC markets. Research in this aspect has been going on. The State Council, on the other hand, has issued policies that prohibit market markers in OTC markets. However, I believe that we need market makers in the OTC market to provide liquidity as well as facilitate and stabilize transactions.

The third point is about the relationship between regional and national OTC markets. The CSRC has been pushing for the establishment of a national OTC market. I think regional markets and the national one can complement each other, providing differentiated platforms for companies at different growth stages with differing needs and expense budgets.

Fourth, from a regulatory perspective, we need to unify regulatory standardizes for even regional OTC markets. The central government can create a principle regulatory guideline, which outlines the responsibilities of local authorities. Risk prevention and disposal can be taken care of locally.

ZHANG Yunfeng

Yeeli Hua ZHENG

CHEN Qiwei

ZHANG Yunfeng
General Manager, Shanghai Equity Exchange

Shanghai Equity Exchange (SEE) has run smoothly for four months since its opening. A total of 21 companies have listed in the exchange. The number may be small, but trading has been active compared with other OTC markets. The combined amount of transactions for shares of 11 companies has reached more than 70 million yuan.

The growth potential of SEE is reflected in three aspects. First, all enterprises listed in the exchange have met their financing needs. People familiar with the OTC market would know that this is not an easy task. Second, the amount of transactions in the exchange has been low mainly because many people have been reluctant to sell their shares, which also indicates that they believe the enterprises they bought in are of high quality. Third, we opened after the State Council launched the No. 38 document. Therefore, our operations are strictly in line with the regulation's requirement.

There are already many OTC markets and equity exchanges in China. To my knowledge, however, none of them enjoy very active transactions. Take the new Three Board for example. It has enabled many enterprises to raise 1.4 billion yuan in combination from January 2006 to December 2011, 77 percent of which were conducted through one securities brokerage firm. The combined value of transactions in the six years amounted to more than 2 billion yuan, 51 percent of which were matched by another securities firm. Out of the 62 securities brokerage firms participating in the market, only one has made profit. The reasons for this phenomenon probably lie in our over emphasis on IPOs as an investment exit channel. A lack of regulatory consistency also discourages investors from the OTC market and equity exchanges.

On the other hand, the OTC market is facing a golden opportunity for development in a preferential regulatory environment. But there are pitfalls along the way, such as protectionism. Some regional governments may use administrative measures to prevent companies within their jurisdiction from seeking capital elsewhere. They might want to create their own OTC market, regardless of its effectiveness and efficiency. It would be a waste of resources for every province to build its own OTC market.

My recommendations for avoiding the traps are as follows: first, draw up a clear and reasonable blueprint for developing the OTC markets. Build these markets in where the talent and capital concentrate, and gradually integrate them into a national platform. Second, encourage competition among regional OTC markets. Third, properly relax policies to strike a balance between risk control and active trading.

Yeeli Hua ZHENG
Chief Representative in China, NASDAQ OMX Group

NASDAQ created the world's first electronic trading system and invented many market place mechanisms. This is what NASDAQ has developed and promoted. Markets in the rest of the world are now following this trend and framework and developing the same type of electronic platforms and automated mechanisms.

In the U.S. every market is over-the-counter. I think the main board market in China is also over-the-counter, but most likely that refers to a lower level market in China. In the U.S. NASDAQ is the most important main board market. In the past the U.S. had many different types of markets, but over time they were centralized and collectivized. China is still in that process. There is also another market called the OTC Bulletin Board (OTCBB) which is one level lower than NASDAQ.

NASDAQ is the most important main board market in the U.S. It is definitely not a growth enterprise market. In the U.S. main board markets and growth enterprise markets are legal categories. There are three criteria for main board markets in the U.S. First, they receive the most stringent amount of supervision. Second, under the legal setup, NASDAQ takes the responsibility for protecting investors and issuers. Third, there are no restrictions on which investors can participate in the market.

Lastly, I'd like to talk about NASDAQ's market maker system. NASDAQ has many market maker mechanisms, but they have to be supervised carefully because it's is very easy for them run into issues. So in terms of these mechanisms, supervision and regulation are extremely important.

CHEN Qiwei
Board Chairman, Private Equity Association of Shanghai

Developing Over-The-Counter (OTC) Market is conducive to not only the improvement of the capital market but also the rebalancing of China's economy. It is necessary for the market to distribute resources more efficiently. The development of capital markets has been the most essential transformation in China's economy. We started with only eight companies going public in 1990 to more than 200 companies every year now. This is a remarkable progress.

Diversifying companies' financing channels is the most substantial approach to facilitate structural reforms of the economy. Currently, government-backed investments remain the main force behind the growth of GDP. This needs to be changed, because some of these investments usually turned out to be low-efficient.

Therefore, developing OTC markets becomes more important. It is precisely what the economy needs, because it creates an alternative channel for money to stimulate the real economy.

We must prevent efforts in this respect from going off the rails. During the reform and opening up, it happened several times that reforms went against the good wills of reformists. We also paid high prices for missing a lot of opportunities.

To develop the OTC Market without veering off to a wrong path, I think we need unified rules governing the market first. We should also learn from foreign countries' experiences in the operation of our own OTC market.

In addition, we are responsible for educating the public about the rules and how different markets operate. Regulators should refrain from interfering in the OTC market operations too much, for the majority of participants in the market are small and medium-sized enterprises that cannot afford high administrative management cost.

Frauds harm the market's reputation most. I don't think we have punished public companies committing frauds severely enough to warn off others. Economic twists and turns in the past 20 years taught us one lesson – vested interest groups obstruct reforms most. Reforms should avoid forming vested interest groups.

From my perspective, the conditions are ripe in Chongqing, Shanghai and Tianjin to introduce a pilot OTC Market. We have to be prudent in expanding the pilot to other areas, because Chinese provinces are large and the differences between them are apparent. In general, however, all regional markets need to be developed toward a unified national trading platform. Meanwhile, institutional investors that are major shareholders in a company should take on more responsibilities supervising corporate practices and caution against frauds.

Night Chat by the Huangpu IV

Reforming Local Government Financing in China

Moderator: WANG Shuo/ Managing Editor, Caixin Media

JIA Kang
Director and Research Fellow, Research Institute for Fiscal Science under the State Ministry of Finance

Improvements to local governments' financing mechanism should be integrated into a comprehensive institutional reform. To steadily develop market economy, China needs a fiscal policy that properly distributes tax authorities between the central and the local governments. The fiscal policy must clearly delineate the responsibilities of governments at various levels and allow them to collect taxes accordingly.

Revisions are under way to amend the Budget Law, which stipulates that local governments cannot directly issue bonds unless otherwise allowed by the State Council. In practice, local governments found ways to sidestep the restriction and borrow through financing platforms.

Despite the huge size of direct and indirect bank loans, the debt ratio of China's public sector is at around 50 percent, lower than the internationally accepted alarming ratio of 60 percent. But it is wrong to neglect the risks because there are institutional defects that may lead to a crisis if left unresolved.

Last year, the central government launched a pilot program to allow the governments of two cities and two provinces to directly issue bonds. This is a step in the right direction. We need to switch from financing through shadowy platform debts to transparent municipal bonds.

It is beyond my understanding why legislators recently backtracked on the progress made in last November's draft revision to the Budget Law. The proposal could have allowed local governments to directly issue bonds on their own. Now we are back to the outdated regulation that prohibits them from direct bond issuance. If this is the final outcome, the revision would completely miss the point that legislation should serve the needs of society and economy.

We should not be complacent with the current economic stability. In fact, we have many hidden problems. Pollution, for example, is the high price we paid for exploring natural resources. More prominent than resource constraints are the complex interactions among individuals and between the governments and the people. Failure to properly address these issues risks politicizing economic problems and should be avoided at all cost.

QIAN Wenhui
Executive Director, Vice President, Bank of Communications

I would like to talk about how to improve the legal framework and regulations of the operations of local government financing platforms.

There is no need to elaborate on the negative impacts, since everyone here knows about their manifestations. Local government financing platforms have many problems. However, they have contributed to the improvement of infrastructure, transport, and social welfare.

China's financing system should be open to private enterprises, though it would be very difficult to change the government's dominance in it in the short term. If we don't solve the problems in monitoring and regulating financing platform companies, it is very likely that their expansion would give rise to systemic risks jeopardizing the national economy.

To create laws and regulations for financing platforms, we need first to understand what constitutes local government debts. Are all financing platform companies' debts government obligations? The relationship between China's central government and local governments is different from that in western countries. In China, local governments own a number of resources including shares in state-owned enterprises and rights to sell land. A review judging local governments' debt burdens without considering these resources would be incomplete and inaccurate.

We cannot hide the risks, neither can we exaggerate them. A package solution to local debt problems would involve stronger supervision from the central government, third party evaluation and more transparency in government financing. When the regulatory system is in place, financing platform companies can properly utilize fiscal resources to achieve a long-term, healthy development.

JIA Kang

QIAN Wenhui

WU Jiang

WU Jiang
Deputy Director, Business Development Department of China Development Bank

How did local government financing platforms come into being? They formed under special circumstances, where governments and banks cooperated to solve the most pressing concerns of the economy.

After more than ten years' operation, the financing platforms have had obvious positive effects on the society, including improving city image and investment environment especially in 2008. This should be recognized and appreciated.

The debts from China's local government financing platforms and the European debt crisis are entirely different in nature. While the Euro debt crisis was mainly triggered by excess consumption, the debts from our financing platforms mostly went towards building assets, which will support future economic development.

We are confident about the future of financing platforms because China still has a long way to go in terms of urbanization. China's urbanization rate is approximately 50 percent at present, and we still need 20 to 30 years for the rate to rise to 80 percent. The demand for capital during the process remains large, and financing platforms may need to player an even greater role in this process. In next stage, they would probably undergo reforms to become market-oriented, according to regulatory requirements.

Nelson GU
Vice President, Industrial and Commercial Bank of China Limited Shanghai Municipal Branch

ICBC's loans to Shanghai government financing platform companies accounts for one-seventh of the total. They constitute an important part of our assets. Personally, I like to deal with financing platform companies, because the returns are stable albeit low.

Yet reforming the regulation of these platform companies and local governments' financing mechanism has become the order of the day. I completely support this reform. It would prevent local governments from investing in inefficient projects and diversify their financing channels. Currently we're too reliant on indirect financing, which refers to bank loans.

For local governments, the overall cost of borrowing from banks may be lower than issuing bonds, because bank loans can be granted in phases based on the project's status, unlike money raised from the capital market. Therefore, I think cleaning up financing platforms means optimizing local governments' financing mechanism and correcting their behaviors that violate market principles.

Chinese governments have many resources at their disposal to repay loans. Their fiscal capacity will strengthen as reforms deepen to the capital market. But we also need to supervise and control risks.

Frank FX GONG
Managing Director, J.P Morgan Securities (Asia Pacific)

Problems with local government financing platforms will compromise banks' net assets. How can we solve these problems? One way is to securitize financing platform companies. This requires progress in other aspects of market reforms.

Local government financing platforms depend too heavily on bank loans. In developed economies like the US, indirect financing such as bank loans is not the main source of fund raising for companies and governments. Direct financing includes issuing bonds to investors in the capital market. In the US, directly financing accounts for more than 80 percent of all financing. The situation is opposite in China, where bank loans account for roughly 70 percent of all financing, while directly financing makes up only 20 percent.

The root of the problem lies in the lack of transparency. By securitizing financing platforms, I mean securitize their debts and expose local governments' finances. Financing through bond issuance to the public would enable investors to assess the local government's credit and supervise the use of money raised. This can prevent to some extent repetitive construction and inefficient investment as well as dampen corruption.

Nelson GU


Frank FX GONG


Stephen GREEN

Stephen GREEN
Head of China research at Standard Chartered

There are several problems to be considered about local government financing platforms. First, whether these local projects are included in government budget; second, whether there should be a system to strengthen the central government's supervision of these platforms.

We may consider securitizing the assets of platform companies, transferring them to a separate firm that operates outside the government's budget. This firm can publish its budget and estimated income of its projects when it issues bonds. Compared with platform companies that only publish their balance sheets but not anticipated income for their projects, this is a great step toward enhancing transparency and allowing investors to make informed judgment of whether the project is worth their investment. Or we can move platform companies' assets into the government's budget. This can also improve transparency. We hope that government at all levels can in future publish their budgets.

Loans made by small and medium-sized banks to local governments are at the highest potential risk, because there is not a central body to supervise and regulate them. Perhaps the central government can alleviate risks in this respect by assigning a central government agency to supervise these financing platforms and their projects.

Nght Chat by the Huangpu V

Interest Rate and Exchange Rate Liberalization: Possible Measures in the Near-term

Moderator: LING Huawei/ Associate Managing Editor, Caixin Century Editorial Board Member, Caixin Media

Nicholas LARDY
Anthony M. Solomon Senior Fellow Peterson Institute for International Economics

When we're talking about RMB internationalization it's important to have an in-depth discussion of the exchange rate system and the interest rate system. I subscribe to what I would call the conventional wisdom. That is, the internationalization of the RMB ultimately will depend on having a fairly flexible exchange rate and having interest rates that are basically market determined rather than being determined by administrative measure. The reason for this is very straightforward. If your goal is the internationalization of the RMB you have to think ultimately of a much more liberalized capital account. If your exchange rate is not equal to some equilibrium level when you begin to open up you will have very large capital inflows or outflows depending on which direction the currency is distorted and that could be very disruptive to the domestic economy. The same thing is true with respect to interest rates. I think its very important to have basically market oriented exchange rate and basically market determined interest rate structure.

Over the last five years there has been extensive reform of the exchange rate system, beginning in the July of 2005 when the RMB was depegged and began to have more flexibility. The RMB has appreciated a little bit more than 30 percent since then. There has been evidence especially recently of two-way fluctuation in the exchange rate; it's not always moving in the same direction. Most importantly, the external surplus has come down dramatically from over 10 percent in 2007 to less than 3 percent last year. However, the interest rate structure seems to be less reformed with more administrative controls from the Central Bank.

XU Zhen
Chairman of the Board, Shanghai Clearing House

The reform of interest and exchange rates would no doubt bring development opportunities to the financial market; yet it demands higher quality of our financial infrastructure.

Along with deepening interest rate reforms, investor demand for financial derivatives to hedge against price fluctuations is going to rise. As more derivative products are introduced, it would be imperative to develop a central counterparties (CCP) clearing mechanism for over-the-counter derivatives trading.

The mechanism would, in return, boost the reform of interest and exchange rates, since the core of the CCP system is to appropriately price OTC financial derivatives. In other words, it would provide reference to the formation of market-based interest and exchange rates. Therefore, a prosperous OTC financial derivatives market is important in not only countries seeking to reform its interest rates but also mature markets where the interest rates are already determined by market forces.

Shanghai Clearing House is dedicated to creating this mechanism fast. We will strive to introduce a CCP system for derivatives based on interest rates first, and then move on to developing one for exchange rate-based financial derivatives. We will expand the system's coverage to OTC derivatives trading platforms which now use bilateral clearing for transactions.

The CCP system is an effective tool that can reduce risks of financial derivatives. We learned this lesson from the 2008 financial crisis. We will introduce a CCP system for interest rate this year and will stick to it even after the reform is completed. Meanwhile, we are also prepared to introduce the CCP system for exchange rates derivatives.

CHEN Zhiwu
Professor of Finance, Yale School of Management
Chief Advisor, Permal Group

First I want to restate and emphasize my point that any administrative interference in market prices would without exception lead to inequality, benefiting some people while hurting the interest of others.

Take interest rates for example. Low saving interest rates means more than a billion people who deposit their money in banks are in effect subsidizing SOEs and many other politically well-connect interest groups. For another example, we know that peasants are living a difficult life because the prices of their produce are too low; yet we support the government's restriction on food prices whenever inflation rises. We are the ones to benefit from inflation control, including myself and everyone present. But why does controlling inflation always mean hurting the interests of peasants?

Exchange rate is the price of currencies. We usually say that yuan's appreciation works to the disadvantage of China. But it actually depends on who's speaking, because, when yuan becomes more expensive, exporting enterprises would lose while others, such as downstream enterprises in the energy sector, would benefit from lower prices of importing crude.


Nicholas LARDY


XU Zhen


CHEN Zhiwu

Regarding monetary policies, Chinese banks should more often use interest rate instruments than quantitative tools, because the latter is a relic of planed economy.

Moreover, it is very important for the government to realize that it cannot rescue every financial institution in trouble. If the interest rate reform is carried out without implementing this principle, many financial institutions would become reckless.

Bottom line is, without liberalizing interest rates, the gap between individuals' welfare and China's national wealth as a whole would continue widening.

This is also a very good time to push forward the exchange rate reform, especially when China's trade surplus narrowed and the yuan started fluctuating both ways. When exchange rate reform is completed, foreign politicians will have one less excuse to criticize China.

Fred HU
Chairman & Founder, Primavera Capital Group

The recent interest cut by the central bank is more than a countercyclical move to stimulate the economy. It widened the floating range of interest rates, a significant step toward interest rate liberalization. Only when we have liberal interest rates can we truly improve the structure and efficiency of our credit system and better the risk management capabilities of commercial banks.

Interest rate liberalization has another implication. It would allow market forces to allocate capital resource. As a price signal, interest rates play a very significant role in market-oriented resource distribution. Interest and exchange rates reforms are along the same way of our reforms that have been going on for 30 years. Absent the success of these reforms, we would not be a thorough market economy.

Many countries have completed interest rate liberalization. The risks of China implementing this reform would not be as large as imagined. Few countries that have liberalized their interest rates enjoyed the luxury of having sound fundamentals as China does. So if China cannot roll out the reform today, no one could have. I think China can smoothly complete interest rates liberalization in up to three years in future.

Helen QIAO
Chief Economist, Greater China, Managing Director, Morgan Stanley

The actual level of interest rate liberalization is higher than most people think. For instance, people are increasingly invested their money in wealth management products instead of depositing in banks. Many wealth management products with an annual interest rate of 4.2 percent can guarantee the safety of principles. This is to a large extent a reflection of interest rates becoming more liberal.

The primary issue in interest rates reforms is to let the market take the reins. We should give banks more operational freedom, once the regulatory rules are laid out. Unfortunately, some policy measures we saw recently backtracked on previous progress. For example, new regulations that prohibit banks from charging more than interest payment on loans. This is intended to constrain companies' financing cost, but it is essential a step in the opposite direction of interest rate reforms. New loans have grown much more slowly since the rules were implemented in March, because banks are reluctant to lend if they can only lend to small and medium-sized enterprises at low interest rates.

Fred HU

Helen QIAO

ZHENG Anguo

ZHENG Anguo
General Manger, Hwabao Investment Ltd.

Trust companies can be the pioneers in interest rate reforms, because their utilization of capital resource has already followed market principles. The size of trust products by the end of last year was 4.8 trillion yuan, among which 51 percent were financing trusts, according to official account. The value of financing trusts grew by 600 billion yuan, accounting for nearly 9 percent of all new loans. By my own calculation, financing trusts amount to more than 70 percent of all trusts.

The yields on trusts average at around 8 percent. It must be higher than bank deposit and lending rates as well as inflation rates. The size of trust assets in 2006 was only 460 billion yuan. It has expanded by 13 times. This is the force of liberal interest rates.

Trusts can provide much more than financing. Their clients are more affluent and more tolerant of risks. Therefore, carrying out interest rate liberalization on the platform of trust companies can be least disruptive to the market. Trust firms, of course, need to make improvements by, for example, optimizing their structures and enhancing the liquidity of their trust products. With these improvements, trust firms can be a pathfinder for China's interest rate reforms.

Night Chat by the Huangpu VI

Promoting Financial Services for Small and Micro Enterprises

Moderator: QIN Shuo/ Chief Editor, China Business News

TAN Weixian
Deputy Director of Shanghai Office, China Banking Regulatory Commission

China has written into law that small and medium-sized enterprises should be promoted, but there is no legal statement that they can enjoy credit support. China Banking Regulatory Commission has formulated policy to guide commercial banks in giving credit to SMEs. However, the policies are toothless.

This problem is better solved through legislation. I suggest the National People's Congress revise the Commercial Banking Law to include a provision that sets a floor to the share of commercial bank loans to SMEs. Failure to meet this requirement breaks the law.

Secondly, we should create a specialized agency for SMEs in light of the experience of many foreign countries. The US government has a federal agency as well as many banking communities to support the development of SMEs. The EU created the Europe Investment Bank, while the Japanese government has financial institutions dedicated to serving SMEs. China still lacks a policy bank to provide services for small firms.

TAN Weixian

The third is creating a comprehensive loan guarantee system. It promotes efficiency among the financing of SMEs. Every country has their own system in order to promote SMEs; they are nonprofit.

Lastly, we need to support SMEs with targeted preferential policies. We have launched many policies in this respect before, but many of them have failed to deliver real benefits.

FAN Yongjin
Chairman, Shanghai AJ Corporation

Based on my experience, small enterprises have stronger financing needs than large companies, but they face more obstacles than large businesses in raising funds. The US capital market is a multi-layer system, which makes it more resilient in times of crisis. China used to have only the main board in stock exchanges. Now we have the Zhongguancun Science Park OTC market as a complement.

Private enterprises can player a big role in small enterprises financing. The Shanghai municipal financial service office has approved 87 small loan companies, which have lent a combined 50 billion yuan in three years. We have established 77 loan guarantee companies, which guaranteed 50 billion yuan of loans last year. These grass roots initiatives can thrive and contribute more as long as the policy environment is good. Regional regulatory authorities need to take more responsibility of mobilizing local small businesses.

In implementing the policies, regulators need to lay out clear rules and responsibility assignment. On the part of financing service providers, we should pay more emphasis to the rural areas. In addition, we need to maintain a prudent approach to development, for our foundations are not solid yet.

SHI Meiliang
Vice President, Shanghai Rural Commercial Bank

The relationship between banks and small business is like that between a fish and water. The support and development of the banking sector is inseparable from the development of the real economy. Moreover, big companies all started out as smaller companies that then developed. The financial services of small businesses should embody the ideal of equality by making loans equally accessible to small businesses.

Shanghai Rural Commercial Bank mainly targets small and medium-sized enterprises. Up until this May, our amount of outstanding loans for small and medium-sized enterprises was 76.7 billion yuan, among which 50.5 billion yuan was to rural residents or agriculture-related businesses and 9 billion yuan was for technological startups.

This is made possible by a number of initiatives we took in the past few years. In 2006, we created a research center to study the needs of small enterprises and provide services to them accordingly. In 2009, we established yet another center under the requirement of China Banking Regulatory Commission to explore financial services for technological enterprises. Last year we created a department that specifically deals with the financing needs of small enterprises.

FAN Yongjin

SHI Meiliang

Christopher DALO

Christopher DALO
Global Head of Sales Management and Customer Offerings, SME Banking, Standard Chartered Bank

The SME banking business for Standard Chartered includes operation in 30 countries across Asia, Africa, and the Middle East. We are currently in 21 cities in China. On the financing side, we've been able to build robust credit models to predict repayment. This has been very effective for us especially in the small business segment when we're approaching customers who don't have collateral we can use these models to get comfortable about lending to them. In 2008 after the financial crisis we partnered with many governments to ensure the flow of credit continued to SMEs. This was primarily through a lot of the government guarantee schemes.

The other thing is education. SMEs don't have access to a lot of the networking and resourcing that larger companies do. A few years ago in Pakistan we partnered with IFC doing a lot of financial training for SMEs. 50 percent of the attendees actually thought their accounting and cash flow forecasting had improved. Financing is important but equipping small business owners with the skills to run their businesses is also very important. The infrastructure the government in Singapore provides to small businesses, especially startups, is great. They have tax incentives for angel investors. They have co-investing with angel investors. They are working with local universities to raise the profile of small businesses. Even if a company has financing a lot of times it still might not succeed because it lacks a foundation built on a skill set.

YU Xiaodong
Chairman, Shanghai Huijin Financing Guaranty Company

Loan companies need to understand the characteristics of small and families businesses in order to provide customized services for them. While serving SMEs, loan guarantee companies need to create a risk management system that suits small businesses. Therefore, their focus when accessing a firm's qualifications should be on the growth potential of the firm rather than underlying collaterals of the loan.

Moreover, loan guarantee firms, as non-bank financial institution, must resolve the issue of innovation. In today's rapid development of technology and among the fierce competition, there is a never ending stream of new businesses and financial models. We need to dig into the core value of small and medium sized enterprises both today and in the future. We should use the thinking of investment banks and actively cooperate with companies for the long term; strengthen technology and encourage up and coming industries as well as the research of modern businesses. In terms of developing innovative business growth point, loan guarantee firms can learn from the experience of small loan companies and work with non-financial institutions.

LI Yinghui
General Manager, Shanghai Purang Financial Services

We do not lack policies or capital or infrastructure for small and medium sized companies. Why are there still problems financing these

YU Xiaodong

LI Yinghui

ZHANG Yufeng

companies? The first reason is our monetary policies change too frequently. In the last two years the loosening and tightening of monetary policy doesn't really affect large companies but is harmful to small and medium sized companies.

Secondly, in terms of financing, there is still no platform for short term lending.

I have a few suggestions. First is to not only allow these companies to enter capital markets but also allow them to enter money markets. This allows them to get short term financing as well as make short-term investment. Second, we need to energetically support rural banks, loan guarantee companies, and small and medium sized banks at the same time. We should also support some privately run financial institutions.. Third, the government should have preferential tax policy to encourage the marketization of financial services companies.

ZHANG Yufeng
President, Shanghai Songjiang JUNHE Micro-credit

Unlike banks, small loan companies should have a large risk tolerance. Our accumulative loans have reached 50 billion yuan, with the non performing rate at around 0.67 percent. Therefore, there is still some room for more risk. Innovation in financing needs capital leverage. Private small loan companies should not shy away from this.

The leverage rates of banks are significantly higher than small loan companies. It would be great if the regulator allows us to have higher leverage rates, even if this means we need to shoulder more risks. Entrepreneurs like us have the spirit to play it risky and start all over again when we fail.

Night Chat by the Huangpu VII

Financial Information Service and Capital Market Growth

Moderator: LU Guangjin/ Director-General, Foreign Institutions' Information Service Bureau State Council Information Office, The People's Bank of China

ZHANG Changhong
Chairman and General Manager Shanghai Great Wisdom

Globalization is profoundly linked to the growth of China's economy during the last thirty years. With economic growth, China's capital market has become a network of nerves that connect the resource allocation of enterprises. China is a manufacturing powerhouse, but its financial services industry does not yet have the same clout.

Chinese enterprises have developed fast during the last decade taking advantage of the overall economic growth and the perfection of the Internet. In retrospect, we were so busy catching up with the rapid expansion of our user base that we missed some details.

Now we have several tasks. We need to enlarge the size and improve the accuracy of the data we provide. We need to upgrade our technological system to process a massive amount of information at the same time and better analyze and integrate them for clients' use.

Information service companies have to prevail in the ability to provide accurate and valuable information fast, because in the era of information age, data itself can be easily found elsewhere.

On the other hand, the explosion of information has made it hard for many people to find useful information among all of the noise, thus providing another opportunity for companies like us to succeed. Our job is to screen out just the type of information a person needs to help him make informed decisions. I also believe that in future we need to provide information with a point of view, which tells users how we interpret the information, such as a change in national policies.

Douglas TAYLOR
Founder and Managing Partner, Burton-Taylor International Consulting

The financial information industry is a US$25 billion industry globally. In China it's about US$750 million. That US$750 million has grown 10-fold in the last seven years. The growth in China far exceeds the growth in other developed countries. The key here though is transparency. Outside investment must be able to measure risk and the people sitting in these chairs are the people who provide the tools that allow outside investors to understand the risk. They are providing the foundations of this market capitalization that draws investment. This creates transaction volumes, and becomes the very foundation upon which financial markets are built.

What we have in China now is perhaps the fastest growing financial information market in the world. We have an unusual market because in most other countries international players have the largest share of market revenue. In China domestic players are the majority. 76 percent of the revenue generated by financial information sales in China comes from local players.

I would expect over time that will change. I don't necessarily expect that the international players will become the majority, but they will carve out more than their 24 percent as transparency increases and more dollars begin to flow from outside into China. The dynamics we can expect are continued growth but probably a change in the mix of the way the financial information revenue is generated, more skewing towards international players.

David SCHLESINGER
Chairman, Thomson Reuters China

The definition of cutting edge technology, however, has changed a lot over the years. Reuters was founded on carrier pigeons and the telegraph. In more than a century and a half you can trace a direct line from carrying stock prices in a tube on a carrier pigeon's leg or carrying news on a brand new telegraph line to today's millisecond transmission of financial data.

But let's be very clear: technology is never more than an enabler, a means to an end. Behind the technology there needs to be all the building blocks of a true, healthy financial market: smart people, ethical rules, laws, fair enforcement, a level playing field for all, and a sense of professionalism. The past decade has showed us too many examples of the disaster that can ensure if any one of those building blocks is missing. As technology improves the need for a solid underpinning becomes ever more acute. The increasing speed, complexity, and sophistication require it.

When trading was done face to face, the participants could gain a measure of the man in front of him. There was a relationship and a trust. My company made its fortune by standardizing electronic trading and foreign exchange creating an electronic intimacy. Still the actual trading had to be the result of smart people with shared ethics, a shared legal underpinning, and a faith that the trades would in fact be delivered.

ZHANG Changhong

Douglas TAYLOR

David SCHLESINGER

LU Feng
Founder and Chairman
Shanghai Wind Information

Today's financial industry has a new dimension. We need to teach students studying finance from the very start the importance of analyzing financial data and navigating vast amounts of information.

What is the relationship between the internet and financial information? The internet has enabled a substantial amount of information to be delivered almost instantly to end users. It also means higher demands on financial information providers, because most information is already freely available to the public on the Internet. The challenge becomes how we can differentiate our services from the data floating on line. The only solution should be to customize our services to suit differing needs.

Domestic financial information providers still have a long way to go compared with their western counterparts. We need to learn from advanced experiences and then develop our own strengths.

QI Shi
President & CEO, Eastmoney Information

Eastmoney was established in 2005 and went public in 2010. This would have been impossible without the Internet. Internet enables people and companies to access information with ease and at low cost. The ability of the internet to lower the costs of retrieving information will change the landscape of the market. Internet has enabled me to build a large user base in a relatively short time.

The common way to grow an Internet business is to accumulate a large user base first and then develop value-added services accordingly. This is also how I develop my businesses. My responsibility now is to attract users to my website. When they pay for our paid services, I make money. This business model is borne out of the characteristics of the Internet and is probably different than those in traditional fields. Regarding contents on the website, I believe quality is the most important element. Whether you want to develop original content or indexing articles from other websites is a matter of personal preference.

Another thing I think is important is the increasing use of mobile phones. This year, more people use their mobile phone to surf on line than a computer. With smart phones becoming more popular, we can expect mobile-end financial information services to develop quickly.


LU Feng


QI Shi


Ee Chuan NG

Ee Chuan NG
CEO & General Manager, Bloomberg China

It's the same for Bloomberg, Reuters, and other local companies in the industry. Our analysts have to be highly logical and have the ability to resolve issues. Collecting data isn't just reporting numbers, it's being able to standardize these numbers so that they can be compared and the meaning of the data can become apparent. Anybody can get on the Internet and look up information. But what information is reliable? How do you compare numbers?

Supplying financial news is not a straightforward business. The state of the world's financial markets is extremely complex, it's no longer two-dimensional. If you're a fund manager, and you're working in the U.S. on the stock market, then Greece's credit crisis has an impact on your investment decisions. With the globalization of China and its reform and opening, the situation has become three-dimensional. It's like figuring out a Rubik's Cube. At Bloomberg, we have connections with many markets. We have seen the development and transformation, even globalization, of many markets. From that we've gained some insight. Financial numbers are a window into these markets.

How do we go about providing financial information? First and foremost we listen attentively to the needs of our users. This is one of Bloomberg's key values. Everything we do is for our users, because ultimately it is our user's needs that influence the market. Keeping track of the pulse of the market is extremely important for our users. Another insight we've gained is that we're able to contribute to the development of financial markets, to deliver some innovation, some certainty. For innovation and certainty, the accuracy of financial information is extremely important. But obtaining innovation and using new technologies well isn't just a matter of delivering information. What matters is pinpointing the importance of the information.

Thirty years ago the biggest securities firm in the U.S. did their own financial analysis. All we did was provide some standardization, some systemization. Today, we still do that work, but having a search function for information has become important. It's also important for Bloomberg to have an international perspective especially with so many international companies. For example, when off-shore markets of RMB started to develop, it became important for us to run numbers on these new markets. We developed new tools and communicated with our users, with Chinese banks. We ended up developing the RMB CNH code which has already been launched in the Hong Kong market.

Night Chat by the Huangpu VIII

Financial Cooperation among the Mainland, Taiwan and Hong Kong

Moderator: YUAN Man/ Senior Editor, CAIJING Magazine

HE Jianxiong
Director General, International Department,
The People's Bank of China

There are two phases of cooperation between Hong Kong/Macao and China. In the first phase, Hong Kong and Macao acted as China's port for the flow of funds, people, and goods. These flows also had a spillover effect: technology, talent, and experience all entered China through them. The second phase technically has not ended yet, but covers about 10 years of experimentation from the start of Closer Economic Partnership Arrangement (CEPA). During this stage, China was developing its economy and opening up to the world. China gained access to markets through Hong Kong and Macao. All the results of these two phases of cooperation have yet to be seen, but right now we need to deeply reflect on the strategy for the future.

In terms of the scale of China's economic market, the first thought is always that it is big. Hong Kong, Macao, and Taiwan can use China's market as a source of goods and production services. With its liberalization and integration into the world economy, China has created the longest and most complete supply chain in the world. No other country has had such a large-scale, complete supply chain.

The pace of cooperation between China and the other three regions is related to the pace of China's reform. As China fine tunes its structure, the level of cooperation will increase in finance, in the opening up of capital accounts, and in the use of the yuan for cross-border businesses.

Risk will probably increase, but how much risk you have is not an issue of how much openness there is, but rather a result of the accumulation of structural problems. If you move one step at a time, you can slowly expose those problems and encourage the regulatory authorities to resolve them.

The introduction of the yuan into Hong Kong, Macao and Taiwan will not be disruptive. Instead, the entrance of the yuan would provide one more option. I think it will be a stabilizing factor rather than a destabilizing one in these regions.

TENG Lin Seng
Chairman, the Monetary Authority of Macao

Macao is a Special Administrative Region with a population of 560,000. We have always pursued a free market without a foreign exchange control regime. Macao's economic structure is extremely open. Our banking system includes 29 local and foreign banks.

Macao's per capita GDP last year was US$ 66,000, ahead of many other economies. Macao's tax system is very simple and transparent, making it easy to build a regional commercial platform. Macao's government has tried really hard to develop industry. We are constantly improving the business environment and the legal structure to the best of our ability. Examples include establishing service centers, lowering taxes, providing subsidies. In 2009, Macao signed the CEPA with China and we are about to sign Supplementary Agreement 9.

In order to implement the Pearl River Delta development plan, the governments of Guangzhou and

Macao have already signed an agreement. The cooperation between the two governments is comprehensive and systemized. Macao also has a relatively unique advantage. We aim to build Macao as a market for mainland China, Brazil, Angola and many other countries.

Macao started yuan business in 2004 with a clear blueprint. The People's Bank of China and the Macao's regulatory authorities have signed an agreement with long-term plans regarding operational details. It also has an agreement with Macao's clearing center. Operations have run smoothly since 2004. We have a supervisory structure that closely monitors irregular situations. Communication is very important in this area. We need to create a relatively stable environment for expanding yuan businesses, which will benefit not only Macao and the mainland but also Hong Kong and Taiwan.

HE Jianxiong

TENG Lin Seng

Samuel J.S. HSU

Samuel J.S. HSU
President, Taiwan Stock Exchange

The development of direct financing can increase the efficiency of indirect banking. According to McKinsey's statistics in 2011, direct financing has amounted to more than 400 percent of GDP in developed countries. On the other hand, the value of Shanghai and Shenzhen stock exchanges combined is about half that of the mainland's GDP. Obviously, there is a lot of room for improvement. The cost of direct financing is low. To finance from higher-interest bank loans, companies have to keep their costs low.

Data shows that the bilateral trade between mainland China and Taiwan reached US$ 160 billion in 2011. In the past decade, Taiwan has invested more than US$ 100 billion in the mainland. Financial governance should be built on the development of the real economy.

How should we implement financial cooperation between Taiwan and China? The Bank of China opened a branch in Taipei on June 22. This is a start. We hope there can be more opening and communication in the fields of securities and insurance. Taiwan has 1.2 million small and medium-sized enterprises and 67 banks. These banks have extensive experiences with lending to large Taiwanese companies. If they could be allowed to operate in the mainland market, they can share experiences with mainland banks and the two can complement each other.

HUANG Hongyuan
Executive Vice President, Shanghai Stock Exchange

Shanghai and Shenzhen stock exchanges signed an agreement earlier with Hong Kong's stock exchange's operator to found a joint-venture company. This is the most recent progress in the financial cooperation between mainland China, Hong Kong and Macao. In its early growth stage, I think the new firm would develop some cross-market securities index products and some correspondent financial derivatives that can be traded in stock exchanges in all three areas. This is an ongoing process-- during this time we have been maintaining a solid exchange of personnel, information, innovation ideas, and regulatory experiences. We would continue expanding cooperation, by introducing, for example, cross-market exchange-traded funds. We have been working closely with Hong Kong authorities to speech up launching this product.

Generally, I think the financial cooperation between mainland

China and Taiwan would continue to expand, for two main reasons: first, you have the rapid growth of mainland China's economy. As long as annual GDP growth remains high, cross-strait financial cooperation will continue to improve. The second reason is that each of the markets occupies separate stages of development. The Taiwan, Hong Kong and Mainland Chinese stock exchanges each have their own characteristics, and have room to accommodate mainland China's growth.

In the mainland, the Shanghai and Shenzhen Stock exchanges have relatively rigorous management and products that lack diversification. But they can improve fast as the overall economy grows. On the other hand, Taiwan Stock Exchange is a highly market-oriented securities platform, and so is the stock exchange in Hong Kong.

JIN Yu
President & Deputy Chairman of the Board, Bank of Shanghai

One of the highlights of the past three years of financial cooperation between mainland China and Hong Kong/Macao has been the internationalization of the yuan. When our bank first embarked on the journey in 2009, we did not expect that we can make such progress in only three years. The amount of yuan settlement has reached more than 2 trillion yuan. The amount of yuan deposits account for 9 to 10 percent of all deposits in Hong Kong and about 12 percent in Macao.

The internationalization of the yuan is a step by step process that will promote the openness of China's capital account and the convertibility of Chinese yuan.

Hong Kong has established an offshore yuan market. The arbitrage room resulted from the difference in yuan exchange rates between the Hong Kong market and the mainland market will inevitably promote the reforms of yuan exchange rates to be more market-oriented.

HUANG Hongyuan

JIN Yu

Paola SUBACCHI

With a broader vision of developing a Chinese global financial center, we need to look beyond the complementary cooperation between Shanghai and Hong Kong. Following the signing of ECFA, there will be more cross-strait investments, personnel exchanges and other business interactions. With improvements to the clearing system and other financial services, cross-strait cooperation will grow significantly.

Paola SUBACCHI
Research Director, International Economist, Chatham House

One of the questions that people ask us is why an institution based in London is interested in financial centers in greater China. The answer is that what is happening here is of vital importance for the world economy. We were very interested to see what China was doing to reform its financial sector and the impacts of the reform on the four financial centers: Shanghai, Hong Kong, Shenzhen, and Taipei.

All of these centers are changing because of China's financial reform including the internationalization of the RMB. We try to take a long term view and predict how these centers will look like in 10 years' time after the reforms occur. Our conclusion is that we will have a fully convertible RMB in 10 or 15 years, and the RMB will be a key currency in the international monetary system. We see a strengthening of China's financial influence in the region and in particular a larger exposure to its financial periphery.

中国外汇交易中心
全国银行间同业拆借中心

中国外汇交易中心暨全国银行间同业拆借中心（简称交易中心）为中国人民银行直属事业单位。自1994年成立以来，交易中心按照中国人民银行、国家外汇管理局发展银行间市场的战略部署，在上海市委、市府的大力支持下，依靠广大市场成员，以“人民币相关产品的交易主平台和定价中心”为建设目标，坚持“多种技术手段、多种交易方式，满足不同层次市场需要”的业务方针，利用先进的电子信息技术，依托专线网和互联网，建成了为银行间外汇、货币、债券三个市场的现货及衍生品交易、信息和监管等提供服务的基础平台，每日生成人民币汇率中间价、上海银行间同业拆放利率Shibor、债券指数、收益率曲线等系列市场基准，服务对象包括2000多家法人机构、4000多家交易帐户、18000多家信息和监管用户，2011年交易总量达到235万亿元人民币。

The China Foreign Exchange Trade System (CFETS), also known as the National Interbank Funding Center (the Center), is a sub-institution of the People's Bank of China (PBC). Since its founding in 1994, CFETS, aiming at building the "main trading platform and pricing center for RMB-related products", under the guidelines of "multiple technological means and trading patterns to meet market demands of various levels", with advanced electronic information technology, by virtue of dedicated network and internet, has set up the basic platform with trading, information and surveillance services for interbank FX market, money market, bond market and derivatives market. Every day, CFETS calculates and publishes a series of market benchmarks including CNY central parity rates, Shanghai Interbank Offered Rate(SHIBOR), bond indices and yield curves. CFETS provides services for over 2,000 corporate institutions, more than 4,000 trading accounts and over 18,000 information and surveillance users. In 2011, the total trading volume attained 235 trillion RMB.

Luncheon Keynote Speech

Actively and Steadily Promoting China's Financial Internationalization

XIAO Gang/ Chairman, Bank of China

It is my great honor to participate in the 2012 Lujiazui Forum, discussing economic and financial hot topics with experts of the fields. The world economic setup is currently experiencing fundamental changes. In order to implement an open strategy that is more active and mutually-beneficial and foster new competitive edges in faster paces, China must steadily promote financial internationalization.

What I mean by financial internationalization is to facilitate international financial businesses utilizing global elements, to optimize resource allocation, and to share developmental opportunities. This mainly involves three components: firstly, moderate opening-up of the financial market; secondly, active expansion of overseas use of the Renminbi; and thirdly, steady promotion of international operation of financial institutions. Financial internationalization is not only an important component of China's Opening-Up strategy. It is at the same time a necessary condition for such strategy to be implemented.

The internationalization of the financial market, of the currency and

of financial institutions - all three are closely linked together, complementing each other, and hence must be simultaneously promoted. The purpose is to serve the real economy. The internationalization of the financial market is fundamental for the internationalization of the currency, and the internationalization of the financial institutions can lend support to that of the financial market and of the currency. Financial institutions are the main participating entity of the financial market, and they are the main channel for currency circulation. They act upon the market, and serve the enterprises.

In recent years, more and more businesses are starting to 'go out', and have attained significant progress. Till the end of 2011, up to 18,000 Chinese businesses have engaged in direct non-financial investments overseas which are worth a combined US$ 377.3 billion.

As China's Opening-Up policy embarks on a new stage, we will gradually realize the transition from commodity export to capital export and from the status of a major trading country to that of a major investment country. In 2009, direct Chinese investment abroad for the first time surpassed direct foreign investment in China. According to predictions made by institutions concerned, in the next few years direct Chinese investment abroad will continue to expand rapidly. These new characteristics demand that financial institutions, especially large commercial banks, operate internationally; and provide financial services which will support the international operations of Chinese enterprises.

China's financial internationalization have achieved significant progress. In 2011, cross-border Renminbi settlement had surpassed 2 trillion. Till the end of 2011, the five largest state-owned commercial banks operated up to 915 branches abroad, totaling US$ 707.7 billion in overseas assets. But on the whole, the level of financial internationalization is still rather low. Financial services are lagging behind the development of the real economy. It is falling behind the pace of international operation of Chinese businesses. In terms of trade, China has become one of the world's most important trading countries. Yet the vast majority of trade has to be settled via US dollars or the Euro. In terms of investment, Chinese investment abroad covers 178 countries and regions, but overseas presence of Chinese banks cover only 35. This hardly satisfies the financial need of those enterprises that are 'going out'.

In the coming period, we must focus on the expansion of Renminbi use abroad, promote moderate opening-up of the financial market, moderately expand the extent to which foreign institutions can issue Renminbi-denominated bonds in China, allow eligible international financial organizations, overseas currency authorities and financial institutions to invest their Renminbi holdings in our financial market.

We must progressively develop our large multinational financial institutions, enhance our abilities of global financial operations, elevate our standards of international business management, encourage Chinese enterprises to 'go out' and expand their space for development. Looking at the history of overseas. All multinational companies have strong financial support, and have benefitted from legislations and series of supporting government policies. Many countries also encourage commercial banks to 'go out', to accelerate international operations, and to provide diverse financial services to multinational companies.

Since the 1990s, developing countries have become important regions for expansion by multinational banks. In particular, Latin American and South-East Asian countries that were once hit by economic crises and countries undergoing economic transition have provided historical opportunity for the expansion of multinational banks. Since the dawn of the new century, especially after the international financial crisis, multinational companies from emerging markets have grown rapidly. Capital no longer flows in one direction from developed countries to developing ones. Developed countries and emerging markets are now both capital exporters. Innovation is no longer the 'monopoly' of developed countries, more and more enterprises of emerging markets are becoming new sources for innovation.

In the current international financial crisis, multinational banks of some developed countries have been hit hard. This has provided banks of developing countries with the opportunity for international operation. For the Chinese banking sector, due to slowing domestic growth and undergoing financial reforms, profit growth might decrease as compared to the past couple of years. Speeding up international operation is conducive to risk-spreading, and to boosting diverse sources of income.

Currently, attention must be paid to several points in the acceleration of the banking sector's international operation:

First, financial institutions need to position themselves scientifically. They need to define main geographic regions, clientele and products for international operation and develop differentiated services and products that suit the need of China's real economic development.

Second, banks need to optimize their global distribution network , strengthen cooperation with foreign financial institutions while improving their own strengthes.

Third, precautions must be taken against risks in international operations. Having a strong risk-management capacity is the key to success in international operation. Cultivating human resources is important, so is communication and a conducive corporate culture.

In recent years, the status of Shanghai as an international financial center has been significantly rising amongst all global financial centers. According to the 2012 Global Financial Centers Index, Shanghai ranks No. 8. In the newest Xinhua-Dow Jones International Financial Centers Development Index, Shanghai stands at the top of the list. The growth of Shanghai as an international financial center has attracted more and more financial institutions to conduct business here.

I believe, in the future, Shanghai will surely make greater contributions towards China's Opening-Up strategy and its financial internationalization.


金融治理改革与实体经济发展
REFORMING GLOBAL FINANCIAL GOVERNANCE FOR REAL ECONOMIC GROWTH

LUJIAZUI FORUM

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