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## A PLACE AT THE TABLE

Giving private capital a slice of the action



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## Financial Reform Seeks Breakthrough

Policymakers hope new reforms will revitalize the slowing Chinese economy. The country's highly monopolized financial sector has become the first target of reform.

The major deficiency of China's current financial system is that the capital market is still monopolized by state-owned banks, but these banks are not able or willing to support small and medium-sized enterprises (SMEs) and emerging industries.

However, SMEs are one of the main forces in resolving employment problems, and also an important power in China's economic development. Emerging industries are the key industries to be developed in China's current economic transition.

To reform the financial sector, private investment potential should be fully utilized.

Today there is up to 4 trillion yuan (\$634.9 billion) worth of private capital in the market, with most of it in the real estate sector, private lending, art and wine. If private lending is legalized and the capital is properly transferred into the real economy, speculative practices will be changed to investment practices, which will make it much easier for China's capital-hungry SMEs to get access to financial resources.

The financial reform will also deliver a message: the Central Government will no longer depend on monetary policies as much as it did in the past when dealing with problems in the real economy. It will try to resolve problems through financial reform, taxation reform and economic system reform.

It's not easy to push forward the reform. It must be based on a stable financial sector as well as stable and sound economic development. It's also necessary for decision-makers and reform participants to properly judge various problems emerging in the process of the financial reform and manage to solve the problems in a timely and flexible way.

Currently, two things should be taken into consideration. First, it's important to legalize private lending. While promoting private investments, it's necessary to first work out "game rules" for private investments. Second, China's financial sector not only needs to open private finance, but also needs a diversified financial market and interest rate liberalization.

Due to the consideration of economic security and stability, the financial reform that stems from Wenzhou in east China's Zhejiang Province, could be seen as a trial. Wenzhou is expected to set up a diversified financial system so as to greatly improve financial services and strengthen the ability to prevent and tackle financial risks. The region is supposed to provide experience to the rest of the country.

It's a pity that the liberalization of the interest rate and the establishment of private or joint-stock banks are not included in this round of reform. We hope that China's financial reform will be further pushed forward to ensure a successful transition of the Chinese economy. ■

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## Travel Craze

Zhanqiao, a scenic spot in Qingdao, east China's Shandong Province, is over-crowded with tourists during the three-day holiday of International Workers' Day.

The attractive scenery and the comfortable weather of Qingdao make the coastal city a well-known seashore resort. Many waterfront scenic spots in the city received 500,000 visitors daily on average during the holiday from April 29 to May 1.

<http://www.bjreview.com>

**“What the U.S. side should do now is not to continue confusing public opinion or evading or covering up by all means its responsibility for the incident, nor should it continue its interference in China’s internal affairs. Rather, it should draw a lesson from this incident seriously with a responsible attitude, truly reflect upon its policies and actions, take necessary measures to prevent similar incidents, and maintain the larger interests of China-U.S. relations with concrete actions.”**

Foreign Ministry spokesman Liu Weimin, on May 2, in response to U.S. Secretary of State Hillary Clinton’s public statement on Chen Guangcheng’s entering and leaving the U.S. Embassy in China

**“China has maintained that the international community should take an objective, impartial and balanced position on Sudan and South Sudan, avoid taking sides or imposing unbalanced pressure on the parties, and refrain from interfering in the mediation efforts of the African Union and other regional organizations and countries.”**

Chinese UN Ambassador Li Baodong, at a UN Security Council meeting where a resolution on Sudan and South Sudan was unanimously adopted on May 2

**“My work in the government, all through these years, is really a difficult job, and it is a special test of strength for me and a special period of learning. The next government will be leaning on the people as well.”**

Russian Prime Minister and President-elect Vladimir Putin, at a government meeting on May 2





SHI JIANWEI

**COMIC WORLD** A visitor looks at a painting at the Exhibition of Comic Artists & Auction, which kicked off in Hangzhou, east China's Zhejiang Province, on May 1

adding that annual growth of the migrant population will be around 10 million in the 2011-15 period.

## Social Security Plan

China has approved a five-year plan to speed up the establishment of a social security network that covers both urban and rural citizens by 2015, the State Council, China's cabinet, said on April 27.

The government will strive to build an essentially complete social security system and a relatively sound management service system by the end of China's 12th Five-Year Plan period (2011-15), according to a statement released after a State Council executive meeting presided over by Premier Wen Jiabao.

The statement said that the country's social security development is unbalanced, as the system in rural areas obviously lags behind, and the coverage rate of some basic social security systems is still low.

It said the government will speed up the construction of the system, which includes extending its old-age pension scheme to cover all residents, improving insurance systems for healthcare, employment injury, unemployment and maternity, as well as adopting measures to cope with an aging population.

## Embracing Buddhism

**Bainqen Erdini Qoigiyajabu**, the 11th Panchen Lama and top ranking figure of Tibetan Buddhism currently in China, attended the third World Buddhist Forum (WBF) held in Hong Kong on April 25-27. This was the first time the 11th Panchen Lama attended activities outside the Chinese mainland.

Born in February 1990 at Lhari County in northern Tibet, he was confirmed and approved by the State Council, China's cabinet, as the reincarnation of the 10th Panchen Lama in November 1995, after the lot drawing from a sacred golden urn in strict compliance with religious rituals and conventions.

The 22-year-old Panchen Lama is also vice president of the Buddhist Association of China. He attended the first and second WBF held in Zhejiang Province in 2006 and in Jiangsu Province in 2009, respectively.



## Population Urbanization

China's population urbanization rate, which reached 51 percent last year, will further climb to 60 percent by 2020, bringing the country's urban population to around 850 million, according to a demographic study released on May 3.

The China Population and Development Research Center said in a report that in the next 20 years, China's urbanization will maintain a fast speed, with around 300 million people moving from rural to urban areas.

China's urbanization will enter a stable stage by the middle of the 21st century, with the peak between 70-75 percent, it said.

In 2011, the number of migrant workers in China reached 230 million, the report said,

## Oil Spill Compensation

U.S. energy giant ConocoPhillips China will pay 1.09 billion yuan (\$172.79 million) in compensation for oil spills that occurred in north China's Bohai Bay starting in June 2011, the State Oceanic Administration said on April 27.

Moreover, China National Offshore Oil Corp. (CNOOC) and the Chinese unit of ConocoPhillips will pay 480 million yuan (\$76.09 million) and 113 million yuan (\$17.91 million), respectively, for environmental protection efforts in the Bohai Sea, according to the administration.

The money will be spent, according to

**STAY SMALL** A guest stays in a capsule-shaped single room at a newly-opened mini hotel in Xi'an, northwest China's Shaanxi Province, on May 2



ORIKANT

China's laws and rules, on the ecological construction in, and environmental protection of, the Bohai Sea, cleaning up petroleum pollutants in the sea, fixing damage to the marine ecological environment as well as monitoring and research on the impacts of oil spills to the ecosystem, according to the administration.

The severe oil spills in the Penglai 19-3 Oilfield in the Bohai Bay polluted more than 6,200 square km of water, an area about nine times the size of Singapore, and caused huge losses in the tourism and aquatic farming industries of Liaoning and Hebei provinces.

The Penglai 19-3 Oilfield is one of China's largest offshore oilfields, with daily production of about 160,000 barrels. ConocoPhillips China operates the Penglai 19-3 Oilfield, in which CNOOC, China's largest offshore oil producer, holds a 51-percent stake, while ConocoPhillips holds 49 percent.

## Work Hours

Chinese employees work 8.66 hours daily on average and spend 0.96 hours in transit, according to a newly released survey.

The survey jointly conducted by Peking University and zhaopin.com, one of China's leading recruitment website, covered more than 30,000 respondents in 28 cities.

The survey shows that on average Chinese workers spend 7.33 hours sleeping, 8.66 hours at work, 0.96 hours on the road and 7.05 hours on other activities.

Guangzhou in southern Guangdong Province tops the list in daily working time, with 9.02 hours. Hangzhou in eastern Zhejiang Province, Shanghai and Shenzhen in Guangdong follow with above 8.8 hours. Beijing workers average 8.68 hours.

## Nano Technology

China will further industrialize the use of a new material developed with the help of nanotechnology to ensure the safety of its power grids, according to a statement from the National Center for Nanoscience and Technology (NCNT) on May 2.

The NCNT said the material has undergone strict testing and technical evaluations and will be used to solve the problem of flashover, a phenomenon in which energized conductors inadvertently come into contact with other conductors or a grounded surface. Flashover has been a persistent safety problem in China's power grids.

Other projects based on the use of the new material are in the research phase and will eventually be applied to China's power grids on a large scale, the NCNT said.

The material was created in 2009 after three years of research by the NCNT, the



**SETTING OFF** Chinese research vessel *Dayang Yihao* departs from Sanya in south China's Hainan Province on April 28, kicking off the country's 26th oceanic expedition mission



**HOBBY FOR FUN** A man operates a helicopter model at the Hobby Expo 2012, which kicked off in Beijing on April 30

Institute of Process Engineering under the Chinese Academy of Sciences and the China Electric Power Research Institute.

## Back to Nature

A nature reserve in east China's Anhui Province will release six captive-bred alligators into the wild as part of an experimental program to boost the population of the endangered animal.

The Anhui Yangtze Alligator Nature Reserve is preparing to put the alligators in a

natural environment later this month, marking the center's eighth attempt to do so since the program started in 2002.

So far, the nature reserve has succeeded in releasing 45 Chinese alligators into the wild.

Anhui is home to the majority of the country's Chinese alligators, which are widely known as the Yangtze alligators because they live along the lower reaches of the Yangtze River.

The breeding center now has more than 1,000 captive alligators.



## Regulating Stock Market

The China Securities Regulatory Commission (CSRC) issued new rules for the initial public offering (IPO) system.

The rules issued on April 28 are aimed at improving the accuracy of information disclosures and making initial pricing more reasonable, said the CSRC.

The new IPO rules detail separate responsibilities for issuers, intermediary institutions, law offices, accounting firms and rating agencies, as well as dictate strict punishments for infringement and illegal practices.

The CSRC promised to introduce independent third parties to carry out risk evaluations regarding information disclosures by companies in order to give references to medium- and small-sized investors.

When price earning ratios go 25 percent higher than their listed industry peers, issuers should further analyze possible risks in order to disclose more information to investors.

The CSRC said the new rule gives market participants time to consider whether their pricing is reasonable or not.

## Cheaper Transactions

China's stock exchanges in Shanghai and Shenzhen on April 30 both said they will cut brokerage fees for A-share transactions by over 25 percent starting June 1 in a bid to alleviate investor burdens.

The brokerage fee at the Shanghai bourse will be lowered from 0.011 percent to 0.0087 percent of the trading volume. The Shenzhen bourse will lower the fee from 0.0122 percent to 0.0087 percent.

China Securities Depository and Clearing Corp. will also lower the registration fee for A-share transactions in the Shanghai bourse from 0.05 percent to 0.0375 percent of the trading volume.

It's estimated that the cuts in transaction fees will save investors about 3 billion yuan



ZHANG JIANHENG

**CULTURE EXPO** A client shows interest in the products displayed at the 7th China Yiwu Cultural Products Trade Fair that opens on April 29 in Yiwu of Zhejiang Province

(\$477.81 million) annually.

The cuts will markedly lower the transaction cost and investor burden, and thus contribute to the healthy development of the country's capital market.

## Manufacturing Up

China's purchasing managers index (PMI), a preliminary readout of manufacturing activities, rose in April for the fifth consecutive month.

The PMI climbed to 53.3 percent in April 2012, 0.2 percentage points higher than that of March, according to figures from the China Federation of Logistics and Purchasing (CFLP). A reading of 50 percent demarcates

expansion from contraction.

"The continuous rebound of PMI shows that China's economic growth is stable," said Cai Jin, Vice Chairman of the CFLP.

## Free Trade Talk

China and South Korea on May 2 announced the beginning of negotiations for setting up a free trade area (FTA), according to a press conference attended by Chen Deming, Minister of Commerce, and Park Tae Ho, South Korean Trade Minister.

Chen said the first round of negotiations will be held in May, adding that he hopes the negotiations will be concluded within two years.

## Numbers

# 776 billion yuan

China's online payments hit 776 billion yuan (\$123.38 billion) in the first quarter, said the Beijing-based IT consulting firm iResearch.

# 11.4%

Tibet's economy grew by 11.4 percent year on year to reach 13.3 billion yuan (\$2.1 billion) in the first quarter of this year, said the Statistics Bureau of Tibet Autonomous Region.



Park Tae Ho said the two countries will start by finalizing modalities for trade in goods, services, investment and other areas, which will be an integral part of the agreement.

Both ministers agreed that the level of liberalization for trade in goods and services should go beyond each country's commitment to the WTO.

Bilateral trade between the two countries has witnessed strong growth during the past two decades, with bilateral trade volume rising 18.6 percent year-on-year to \$245.6 billion last year.

China has become South Korea's largest trading partner, while South Korea ranks as China's third largest trading partner.

## Rubber Acquisition

Sinopec Group, China's top oil refiner, said it will buy a 25-percent stake in a nitrile butadiene rubber plant belonging to leading Russian petrochemical company Sibur.

Sinopec signed an agreement with Sibur on April 29 to expand the annual output capacity of the rubber plant in Krasnoyarsk to 56,000 tons from the current 42,000 tons.

It said the two firms plan to establish a joint venture at the end of this year.

An oil-resistant synthetic rubber, nitrile butadiene rubber is widely used in aeronautics and astronautics, as well as in the oil, petrochemical and textile industries.

## People.cn's Debut

On April 27, the first trading day of *People's Daily's* website, People.cn, on the Shanghai bourse, its shares surged 73.6 percent to 34.72 yuan (\$5.51) per share.

The company started trading at 31.01 yuan (\$4.92) per share on the Shanghai Stock Exchange, 55.05 percent higher than its initial public offering (IPO) price of 20 yuan (\$3.17).

## Education Reformer

**Zhu Qingshi**, President of South University of Science and Technology of China (SUSTC), has attracted attention of the public again as the university received approval from the Chinese Ministry of Education in April to recruit students.

Zhu, 66, former President of the University of Science and Technology of China (USTC), was appointed president of SUSTC in 2009.

A graduate from USTC in 1968, Zhu started research work at the Chinese Academy of Sciences (CAS) in 1974 and was sent to study abroad in 1979. He returned to China in 1982 and became an academician of the CAS in 1991. In 1994, Zhu started teaching and researching at USTC and became its president in June 1998. After retiring from the post in September 2008, Zhu was chosen as the president of SUSTC because of his efforts and spirit in reforming higher education in China, which is in line with the spirit of the new university.

Zhu holds that universities should recruit students and issue diplomas independently, which could be a direction of the education reform in China.



The IPO, which has attracted a great deal of market attention as it marks the first-ever listing of a state-owned media website, is expected to raise up to 1.38 billion yuan (\$219.4 million) through the sale of 69.11 million shares on the Shanghai market.

The company's IPO prospectus showed the major source of the company's profits come from advertisements, and information and wireless services.

The company said it plans to use 527 million yuan (\$83.65 million) from the IPO proceeds to improve its wireless services, make tech upgrades and bolster its editorial team.

**INTO SPACE** A Long March-3B rocket carrying two satellites for China's global navigation and positioning network known as *Beidou*, or *Compass* system, blasts off from the Xichang Satellite Launch Center in southwest China's Sichuan Province on April 30



# 61.34 billion yuan

Industrial and Commercial Bank of China said its net profit rose 14 percent year on year to 61.34 billion yuan (\$9.77 billion) in the first quarter.

# 51.6 billion yuan

China Construction Bank said its net profit for the first quarter of the year rose 9.26 percent year on year to 51.6 billion yuan (\$8.23 billion).

## THE UNITED STATES

Visitors board a Boeing 747-8 Intercontinental airliner delivered to Lufthansa at the Paine Field airport on May 1 in Everett, Washington. The German carrier is the first commercial airline to deploy the Boeing 747-8 Intercontinental, the largest 747 model



## FRANCE

The Great Roman Games show on April 28 in the amphitheater in Nîmes, southern France. The event is a historical evocation of the games as they could have taken place in A.D. 122



## IRAQ



A boy holds an Iraqi flag during a march in Baghdad celebrating International Workers' Day on May 1



Participants get their hot air balloons ready during the Torres Ballooning Festival in Torres, Rio Grande do Sul, on April 28. More than 50 teams from eight countries participated in the annual festival

## AUSTRALIA

Two koalas displaced from their habitat by flood waters at the Lone Pine Koala Sanctuary in Brisbane. Australia moved on April 30 to protect its most vulnerable koalas, listing the much-loved furry tree-dwellers as a threatened species in parts of the country



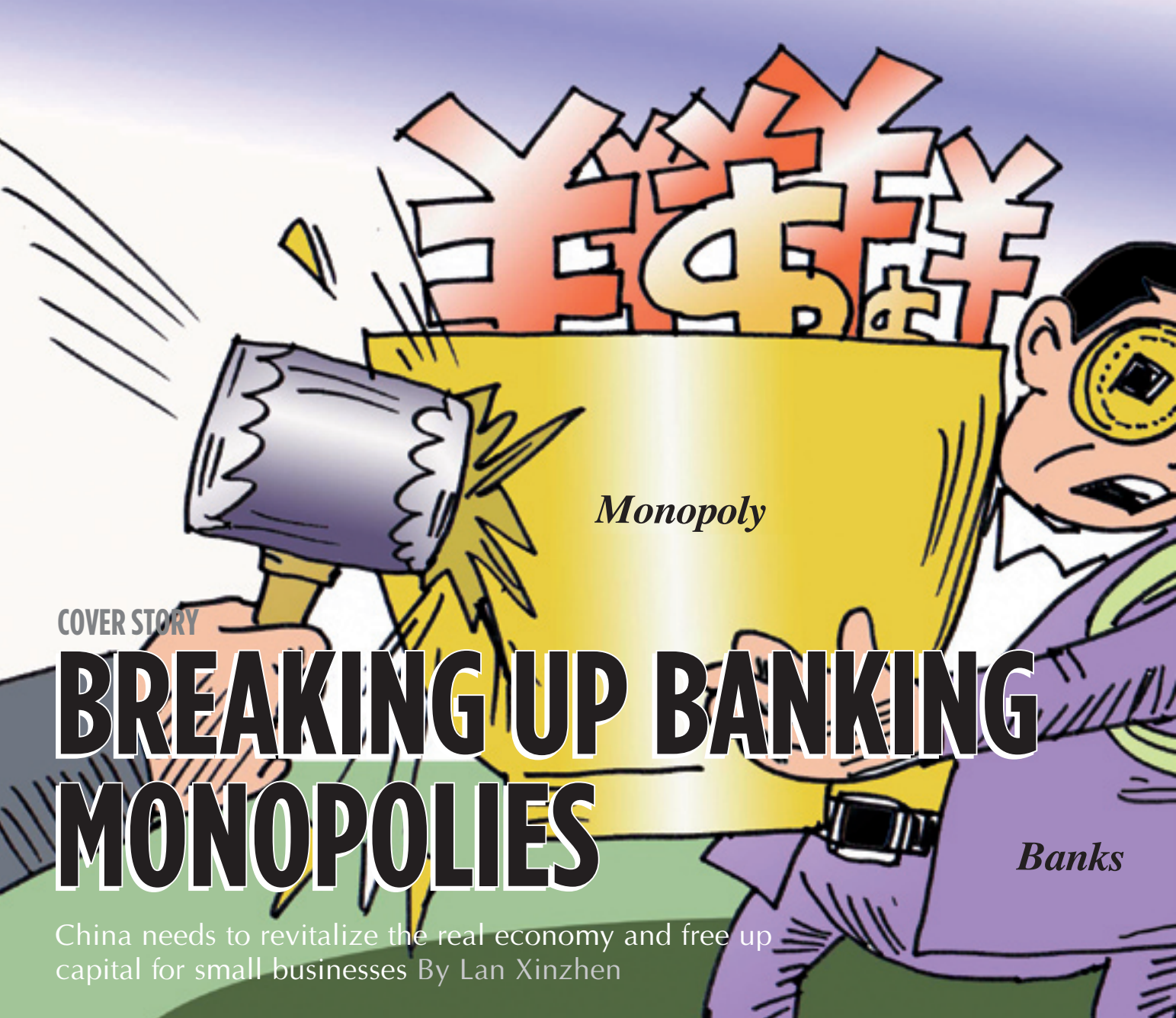
## BRAZIL



Policemen escort a minivan carrying the family members of slain Al Qaeda chief Osama Bin Laden in Islamabad on April 26, as they leave for the airport before their departure to Saudi Arabia. Pakistan deported Bin Laden's family, nearly a year after he was killed in a U.S. raid

## PAKISTAN





COVER STORY

# BREAKING UP BANKING MONOPOLIES

China needs to revitalize the real economy and free up capital for small businesses By Lan Xinzhen

China is in the initial phase of a state-led financial reform, starting with its private economy powerhouse of Wenzhou in Zhejiang Province, in an effort to better support the development of the real economy.

On March 28, the State Council gave the word to establish a pilot zone for comprehensive financial reform in Wenzhou. The plan requires the city government set up a financial mechanism facilitating the locality's social and economic development. It also outlines 12 tasks for Wenzhou to focus on during the reform process, such as "encouraging and supporting participation of private capital in the reform of local financial institutions."

In April, Shenzhen, the original base of China's economic reform in the late 1970s, followed suit with a guideline for financial

reform. The focus of Shenzhen's financial reform will be to serve the development of the real economy, including the introduction of pilot two-way trans-border loans between the mainland and Hong Kong, the establishment of the Shenzhen Qianhai Equity Exchange before the end of this year, and the development of the innovation bond market.

Up to now, 16 pilot zones have been set up to connect technology and finance in cities like Tianjin and Chengdu, and they are seeking further financial innovation to offer financial support to scientific and technological enterprises.

Guo Yanhong, researcher at the Research Institute of Huachuang Securities Co. Ltd., said economic readjustment is generally accompanied with opportunities for institutional improvement. In China, the recent slowdown

of economic growth and the intermittent breakout and intensification of liquidity risks all substantiate the need for financial reform.

According to Guo, the old economic mechanism will face a series of challenges. To avoid economic recession, it is necessary to adopt measures to prevent the economy from shrinking. Historically, after economic crises, corresponding institutional innovations have typically followed.

"Through analysis of U.S. financial reforms, we can find that the reforms actually represented a process of financial liberalization," said Guo.

The pilot financial reforms in Wenzhou and Shenzhen also aim at pushing forward the Chinese financial mechanism. Wenzhou's reform will regulate private capital, while reform in Shenzhen will serve economic



transformation and focus on incorporating capital from diversified channels into the process.

### Ending state monopoly

Days after the State Council executive meeting on March 28, Premier Wen Jiabao announced that the Central Government was determined to break the monopoly in the banking sector during a visit to Fujian Province.

“I think it has been too easy for our banks to make profits,” he said. “The reason is that a small number of large banks hold a monopoly in the sector. This is why we’ve now come to make way for private capital to enter the financial service sector, which ultimately requires breaking monopolies.”

The Central Government is obviously

discontent with the state monopoly in the financial sector. It has already issued several documents supporting the non-public economy’s entry into the financial sector, encouraging private capital to establish banks in the country’s vast rural areas. However, because of various “glass doors,” it is difficult for private capital to enter the financial system. To date, none of the government’s measures has been effective at weakening the state banks’ monopoly. The biggest ill for state monopolies in the financial sector is that bank credit is typically given to large state-owned enterprises, leaving small and medium-sized enterprises (SMEs), especially private businesses, to fend for themselves.

Most Chinese media think among the 12 tasks for the comprehensive financial reform set by the State Council for Wenzhou, the most important is to encourage and support private capital’s participation in reforming local financial institutions and establishing village banks, loan companies, rural financial cooperatives and other new-type financial organizations in accordance with the law.

This means that private capital can establish real “privately owned banks,” with their management personnel selected by shareholders, instead of being appointed by the government.

Pan Zhengyan, Deputy Director of the Financial Research Center of the Shanghai Academy of Social Sciences, said breaking the state’s monopoly on banks has been society’s wish for some time, and bigger strategic reform of the banking sector is unavoidable. But only financial reform processed with market-oriented measures will be able to break the state monopoly.

Pan said the first thing that needs to be done is to enhance competition in the financial market by extending market access to the financial sector. An important goal of the pilot project is to set up a reasonable and multiple financial system instead of one dominated by state-owned financial institutions. This calls for the practice of allowing private capital to fully integrate into the financial system. Incorporating private capital into the financial sector will not only enhance market forces, but also expand the sector’s market capacity.

According to Pan, to thoroughly break the state monopoly in the financial sector, the government should also change the rules of market competition. Non-market formation of interest rates is a special mechanism in the Chinese banking sector. That is to say, prices of bank capital (interest rates) are decided by the “authority,” instead of the market. The price mechanism does not play a decisive role to either the suppliers (banks) or the buyers (enterprises). It is difficult for privately owned SMEs to get loans at reasonable prices.

### Chinese Structure of Banking Sector

Banks in China are divided into state-owned banks, foreign-funded banks, joint-stock banks and private financial institutions. Among the total assets of domestic banks, state-owned banks account for 90 percent, joint-stock banks 7 percent, foreign-funded banks 2 percent and private financial institutions less than 1 percent.

(Source: *China Banking Regulatory Commission*)

Hence there is conflict in the Chinese financial industry: On the one hand, SMEs, particularly privately owned ones, can only depend on financing means with high interest rates and high risk such as usurious loans or illegal financing, with interest rates higher than the social average. On the other hand, under the protection of a special pricing mechanism, banks of various sizes are enjoying bonus from policies and gaining profits from actual “negative interest rates” caused by inflation. Such a price formation mechanism for bank capital is beneficial to the banking sector and directly leads to monopoly profits in the banking sector and actual monopoly in the financial industry.

“The key point to change the unreasonable allocation of social resources is to change the present market rules. Otherwise, it is hard to realize justice and rationality in competition of the financial industry and to really break the monopoly in the banking sector,” Pan said.

### Legalizing private lending

Liu Yuanchun, Deputy Director of the School of Economics of Renmin University of China, said an important part of the financial reform scheme in Wenzhou is to regulate private lending and facilitate private capital entry into the financial sector.

Private lending, especially in large sums, is illegal in China. In Zhejiang Province, where the private economy is more developed than in other regions, many people have already been sued for private lending. Figures showed that in 2008 there were nearly 200 cases involving illegal deposits and more than 40 cases involving fundraising fraud. The recent Wu Ying case has aroused wide public condemnation against ruling private lending as illegal.

Wu Ying, 31, former legal representative of Zhejiang Bense Holding Group, was detained by the public security bureau for her



## Highlights of Financial Reform in Wenzhou

- Regulate development of private financing and set up filing and monitoring mechanisms for private financing;
- Support private capital to participate in local financial reforms and launch or participate in the establishment of village banks, credit companies and rural cooperatives;
- Develop special asset management institutions, and guide private capital to set up venture capital, equity investment companies and related investment management institutions;
- Research to carry out pilot projects on individual direct investment and explore to establish convenient direct investment channels;
- Encourage state-owned banks and joint stock banks to set up special institutions of credit to small enterprises, support financial leasing companies and other non-bank financial institutions to develop business, and promote joint stock transformation of rural cooperative financial institutions;
- Innovate the development of financial products and services offered to micro and small enterprises, agriculture, the countryside and farmers, and strengthen credit support and comprehensive services to them;
- Carry out stock transfer and property

right transactions of technologies and culture by non-listed companies;

- Actively develop bond products of various types, and promote more enterprises, especially micro and small ones, to establish and improve the re-guarantee system;
- Expand insurance services, develop insurance products serving special markets and industrial clusters, and support commercial insurance to participate in the construction of the social security system;
- Enhance construction of the social credit system, promote construction of the credit system of micro and small enterprises and the rural credit system, and strengthen supervision of the credit market;
- Encourage state-owned banks and joint stock banks to set up special institutions of credit to small enterprises, support financial leasing companies and other non-bank financial institutions to develop business, and promote joint stock transformation of rural cooperative financial institutions;
- Establish a comprehensive statistical system for the financial industry and strengthen supervision and pre-warning;
- Establish risk-control mechanisms for the comprehensive financial reform.

(Source: *Wenzhou government financial reform plan*)

involvement in illegal fundraising on March 16, 2007. Jinhua Intermediate People's Court of Zhejiang Province sentenced Wu to death for fraud on December 18, 2009. Zhejiang Higher People's Court affirmed the death sentence on January 18, 2012.

This death sentence aroused public debate on whether the businesswoman should be executed for her crime. Online, most people sympathize with Wu and think her crime doesn't warrant a death sentence. Others believed Wu and other cases are institutional tragedies.

Probably due to public pressure, the Supreme People's Court decided on April 20 to reject the death sentence for Wu and sent the case back to Zhejiang Higher People's Court for retrial. The death sentence will probably be reversed.

"The financial reform experiment in Wenzhou will open a window for private finance to enter the banking sector," said Yi Xianrong, a researcher at the Institute of Finance and Banking

of the Chinese Academy of Social Sciences. "Its significance should not be underestimated in pushing forward China's reform of the financial market, particularly the reform of the complete financial system."

According to Yi, where private lending is active, local economies are usually more developed. Most of the funds from private lending have gone to the real estate market, and most of the funds used for private lending ultimately come from the banking sector. If private lending collapses, it will not only damage the economy in China's most prosperous east coastal areas, but also seriously affect China's real estate market and the banking system as a whole. At present, the scale of private lending in China totals 4 trillion yuan (\$634.92 billion), and the amount of capital lent "under" Wenzhou has surpassed 120 billion yuan (\$19.05 billion).

"Problems of Chinese private lending are the result of strict control over the legal financial system. The most important thing for the experiment to be carried out in Wenzhou should be to

## Highlights of Financial Reform in Shenzhen

- Push forward pilot of trans-border renminbi loans between Shenzhen and Hong Kong;
- Establish Qianhai Equity Exchange;
- Set up national-level venture capital mother fund for emerging strategic industries;
- Establish a uniform management institution for capital of multinational corporations;
- Construct an innovative bond market.

(Source: *Shenzhen government financial reform plan*)

LENDING TO YOU: Huaфон Small-Sum Loan Co. Ltd. is the first micro-credit company in Wenzhou, Zhejiang Province, where micro-credit companies are being supported by the ongoing financial reform





legalize present private lending and then regulate private lending in China. It is important for China's financial reform," Yi said.

In the detailed plan for financial reform, Wenzhou proposes to establish micro-credit companies based on private capital and make them cover all the townships. This year, the city is to set up 30 micro-credit companies with net assets of 20 billion yuan (\$3.17 billion). By the end of 2013 the number of micro-credit companies in Wenzhou will reach 100, with net assets totaling 40 billion yuan (\$6.35 billion).

Zhou Dewen, Vice Chairman of the China Association of Small and Medium-Sized Enterprises, said encouraging private investment through financial reform not only can consolidate the development of the Chinese private economy, but also further promote the private economy to make bigger contributions to China's economic development.

He also said to regulate private lending and promote private investment, the government should formulate game rules on private investment. Now the most important thing is, when

legalizing private lending, China needs to make laws on private investment and financing to regulate and protect these activities.

## Benefiting SMEs

Cao Fengqi, Director of the Research Center of Finance and Securities of Peking University, said financial reform will significantly influence the financing for SMEs. "To legalize private lending will be beneficial to SMEs and can solve their financing difficulties to some extent," he said.

Today, SMEs make up more than 90 percent of all enterprises in China. SMEs also contribute more than 60 percent of the GDP, 80 percent for urban job opportunities and 50 percent of the country's tax revenues. Furthermore, 65 percent of the country's invention patents and 80 percent of the research and development of new products are from SMEs.

Development of SMEs needs financial support, but financing difficulties have long been an unsolved problem. According to a report on the development of Chinese SMEs released by the All-China Federation of Industry and Commerce in 2011, more than 90 percent of the surveyed owners of privately owned SMEs said they could not get loans from banks.

According to the report, the real reason is that monopolies by the four biggest state-owned commercial banks have gradually reduced the financial resources that small and medium-sized banks can get, restricting their capability to serve SMEs. To seek profits and avoid risk, the four biggest state-owned commercial banks are reluctant to offer loans to SMEs.

Difficulty in acquiring loans from legal financial institutions has led SMEs to turn to private lending, which has no legal status in the financial legal system. Due to unsound financial laws, legal private lending activities are not clearly defined against crimes of illegal fundraising or fundraising fraud. Many enterprises don't dare to borrow private capital and are forced into bankruptcy.

The financial reform this time will legalize private lending, which could rescue these SMEs.

The financial reform in Shenzhen proposes two impor-

tant policies in supporting SMEs: offering favorable loans to emerging strategic industries as well as micro and small enterprises, and nurturing a multi-market and multi-level financial system.

## Grassroots appeals

The 12 tasks for the financial reform in Wenzhou were designed by the China Banking Regulatory Commission and the Central Government. The Wenzhou government and market participants such as private lenders and borrowers were excluded from the process, leading to doubt on the thoroughness of the reform.

A report of the Guangzhou-based *Southern Weekend* said, "An anonymous investor in Wenzhou has found the intention from the 12 tasks that 'no one in the decision-making level really wants to break monopolies.' He said only if real privately owned banks are created 'can the financial monopoly be broken by setting up some micro-credit companies in Wenzhou.'"

Hence Zhou thought there are arguments on whether the financial reform should be designed by the Central Government or local governments.

The financial reform Zhou wants should be designed from the ground up because this will better cater to the wants and needs of market participants.

Ma Guangyuan, researcher at the Institute of Risk Investment of Peking University, also expressed discontent with the financial reform designed by the top level. He said in his blog that the scheme of Wenzhou's financial reform is still far behind market expectations.

Ma said there are many problems in China's financial sector that need to be solved, such as breaking the financial monopoly, introducing market-oriented reform of interest rates and legalizing private lending. These are all urgent, particularly the market-oriented reform of interest rate. But regrettably, the financial reform scheme approved this time gives no response to the most urgent topics in the reform.

Ma warned that in terms of the timing of reform, now is the best window of opportunity to push for significant financial reform. Conditions are ready to legalize private lending, allow private capital to enter state-owned financial institutions and adopt market-oriented formation of interest rate. If this chance is allowed to pass by without change, it will be more and more difficult for future reforms. ■



WANG YONGSHAN



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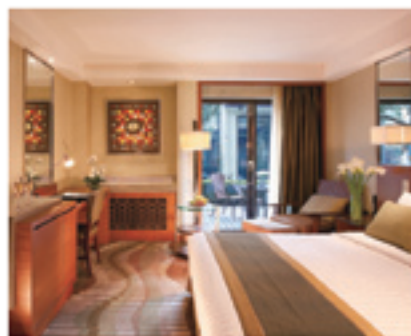
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