

## **Labyrinth of Chinese financial system**

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《Abstract》

This paper intends to clarify issues in Chinese financial system and its dilemma. It has been managed under the “Financial Restraint” rule while its side effects have become apparent in these days due to the rapid economic development. Hence, gradual liberalization is now going on through introducing the market mechanism. Even though, structural problems in Chinese economy force them to continue to rely on discretionary administrative measures to manage it. For example, widening income gaps prompt them to adopt nation-wide accommodative monetary policy, despite of the asset price inflation in the advanced area.

Such complicated policy stances cause the malfunction of the banking system and impede the efficient resource allocation. My analysis, using enhanced “Credit Rationing” model, suggests that combination of minimum lending rate regulation and strict credit risk controls have resulted to fragment bank lending market. Premium borrowers avoid it due to higher interest rates while weaker ones, like SMEs, face difficulties for getting loans irrelevant of the rate level. Such malfunction necessarily nurtures “Underground” finance while less developed capital markets fail to offer alternatives.

To adjust them, they need more de-regulation with institutional arrangements to diversify the financial system, so as to establish the efficient resource allocation mechanism.