

## **Analysis of China's Banking Industry Organizations during the Tenth Five-Year Plan Period**

**Luo Liyong**

School of Economics, Sichuan University, Chengdu, China

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**Abstract:** Improving market openness degree and continuing from market access to price opening will promote industry diversification and enhance the effective competitiveness of China's banking industry. It is the goal of China's banking industry organization policy during the 10<sup>th</sup> Five-Year Plan period. Nowadays, the imperfections of China's banking industry organization are as below: monopoly structure does not produce monopoly profits, market concentration and asymmetry of profits and assets, resulting in huge social welfare losses, which seriously affected the rapid development of the banking industry. To this end, we will continue to relax restrictions on industry access, promote competition in the money market, deepen the reform of the shareholding system of state-owned commercial banks, relax price controls, promote interest rate liberalization, etc., optimize the banking industry organizations in China, and reform our banks. It is very important to organize the system to meet the insatiable desire for loan funds in China's economic reforms.

### **1. Introduction**

After years of financial reforms, the Chinese banking industry has made remarkable achievements in terms of asset size and profitability. However, there are still a lot of problems in Chinese banking market compared with that in developed countries. Based on the relevant industrial organization theory, this paper focuses on the investigation and analysis of the status quo of China's banking industry, and explores ways to optimize the industrial organization of China's banking industry.

### **2. The goal of China’s Banking Industry Organization Policy during the 10<sup>th</sup> five-year Plan period.**

The core of a national financial industry is the banking industry, which has a direct impact on the stability and healthy development of the economy. [1] During the 10th five-year Plan, China’s banking industry, facing important development opportunities and severe challenges, will greatly enhance the position and role of the banking industry in the operation of the whole national economy through unprecedented opportunities-the deepening of marketization. Since the Reform in 1978, in order to improve competitiveness, improve the quality of banking service and operational efficiency, China’s banking industry has taken to break the monopoly, improve the modern multi-bank organization system, increase the number of employees from the perspective of policy guidance and specific measures to achieve phased success, the success of the Reform mainly lies in loosening control. However, from the domestic and international point of view, the Reform is far from achieving the desired goal: from the point of view of domestic development and international comparison, the monopoly degree in the construction of banking organization system in China banking industry is still very high, the degree of openness is limited, the market access and operation are still very high, the lack of fair competition environment, the low capital adequacy ratio and the operation of the four state-owned commercial banks with high proportion of non-performing assets are not optimistic. The overall efficiency of the development of China banking industry needs to be improved, and there is a lack of strong super-multinational banks with international competitiveness. In the face of such a banking situation and reform task, in order to finally establish an efficient modern banking system with strong international competitiveness and

constantly promote economic development, only further reform of the regulatory system to promote the healthy and coordinated development of the banking industry.

Combined with the development trend of the world banking industry, the future reform trend of China banking industry has a general trend: to reduce government intervention in the whole industry, to strengthen the deregulation reform of the independence of the banking industry, to establish branches in line with the economic region to promote the commercialization process, to implement reasonable and strict supervision, to break through business restrictions, to continue to open up the market from market access to price, and to improve the degree of market openness. It will promote the emergence of diversification and effective competitiveness of the industry in order to maintain the safe development of the banking industry and improve the efficiency of the industry; And continue to expand business and high-level development through overseas mergers and acquisitions, promote the effective concentration of the industry, and improve the international competitiveness of the banking organization system.

### **3. The defects of China banking industry organization**

(1) The monopoly structure does not produce monopoly profit, there is no monopoly advantage effect, and the market concentration of profit and assets is asymmetrical. But there is a huge difference between the 1/3 absolute monopoly of state-owned commercial banks with only 1/3 profit and those with close to 2/3 profits and less than 1/3 assets. This shows that the state-owned commercial banks, which maintain the monopoly structure of asset scale, do not rule out the uncertain risk and do not obtain the income of economies of scale, that is, there is no corresponding monopoly advantage effect.<sup>[2]</sup>

(2) There is a huge loss of social welfare. The losses caused by state-owned commercial banks with monopoly structure include state-owned commercial banks that store a large number of non-performing assets, state-owned commercial banks with huge idle costs and state-owned commercial banks whose loans are not given to non-state-owned economic departments in time, resulting in a net loss of social wealth. The bad loan losses of state-owned commercial banks are about 1.25 trillion yuan based on the conservative non-performing loan ratio of 25 per cent of state-owned commercial banks. Since 1991, China state-owned commercial banks have not yet formed huge deposits of actual investment, resulting in social welfare losses of about 300 billion yuan. Since the 1990s, the average investment efficiency of the non-state-owned economy is 9.5 times higher than that of the state-owned commercial banks, which has been very high, but the credit gap of the state-owned commercial banks is that of the non-state-owned economy, which is as high as 775 billion yuan. The total loss of these three items is about 2.325 trillion yuan. The banking industry of China with monopoly structure caused by excessive financial system and administrative intervention since the founding of the people's Republic of China is not formed spontaneously under the influence of market competition, but under the background of planned economy, and there is no monopoly advantage effect. This monopoly mode has caused the net loss of social welfare. The four professional banks with obvious characteristics of "path dependence" have good actual effect of institutional change, so the transformation to state-owned commercial banks in the absence of a complete market environment has a strong guidance. [3]because it will take some time, the maturity of the competitive financial system can meet the demand for loans in China's economic reform, and if it can't be met immediately, the Reform will be hindered. Therefore, the organizational structure and governance mechanism of the state monopoly financial system can blindly expand the scale of deposits and loans under the national credit guarantee, and the old system of state-owned commercial banks formed in this way is certainly more effective than the competitive financial system. However, the soft budget of state-owned commercial banks eager to monopolize funds-the capital occupied does not represent expenditure and cost, but the source of income-is also limited because it is state-owned. Therefore, under the environment of gradual integration of Chinese economy into the world economy, in order to meet the needs of the rapid development of the banking industry and enhance international competition, it is necessary for the monopoly organization structure of China's banking industry to form in the result of market

competition under the background of the increasingly perfect market mechanism of our country.

#### **4. The assumption of optimizing the industrial organization of China's banking industry.**

##### **4.1. Continue to relax the restrictions on industry access and promote the competition in the money market.**

A number of consecutive joint-stock banks and local private banks (such as Minsheng Bank of China) are the representatives and symbols of the opening up of the financial industry, but they still account for about 66% of the assets and deposits of the four state-owned commercial banks. The absolute shareholding status of state-owned shares of other joint-stock banks and the restrictions on the establishment of branches by emerging joint-stock banks and private banks illustrate the highly nationalized characteristics of China's banking industry. Monopoly characteristics are still obvious, private commercial banks are subject to special restrictions. The competitiveness of Chinese banking industry needs a truly mature market competition environment, which can be improved among different property rights subjects. The lack of private sector will lead to high degree of convergence and nationalization of market property rights. Therefore, it is the key to optimize the banking industry organization of our country to encourage the establishment and development of new joint-stock and private banks and to continue to relax the restrictions on industry access.

##### **4.2. Deepening the shareholding system reform of state-owned commercial banks.**

The shareholding system reform of state-owned commercial banks has become an effective way to solve the problem that financial holding companies rely on capital market mergers and acquisitions for the establishment and development of financial holding companies.<sup>[4]</sup> This joint-stock reform model, which is conducive to desalting the "ownership discrimination" against private lending enterprises, can strengthen internal management, enrich the source of funds, and help to alleviate the "financing bottleneck" faced by small and medium-sized enterprises. In the process of joint-stock reform of state-owned commercial banks, which is necessary to maintain the state-controlled position, the key question is not whether the state holds shares or not, in order to form an effective governance structure that improves the efficiency of state-owned commercial banks, and to introduce foreign strategic institutional investors with economic strength and standardized operation. On the one hand, it can improve the bank governance structure under the single property right structure, on the other hand, it can ensure the state-owned holding position of the state-owned commercial banks after the diversification of property rights.

##### **4.3. Relax price control and promote interest rate marketization.**

Ronald McKinnon and Edwards Shaw's theory of financial deepening tells us that the importance of interest rate marketization should be attached importance to, and interest rate liberalization, which has five effects: technological innovation, investment, savings, employment and income, is the core part of financial reform in developing countries. In addition, price competition is also very important to the reform and development of the banking industry itself, and it is the most important and core means of competition for international or domestic banks. The risk of bank operation and waste of resources can be paid for controlling interest rate policies and distorting bank competition. Only when the interest rate is marketized and the price control is liberalized, compared with the foreign banks, the financing cost of the domestic banks can really realize the effective competition of the banking industry, and the development level of the banking industry in China is not at a disadvantage. At present, the deregulation of loan interest rate has become one of the reform directions of the efficient operation of banking industry organization in our country.

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