

# Research on Financial Reform and Innovation of Hubei Free Trade Zone

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**Abstract:** The main task of free trade zones is to explore new ways and modes of China's opening to the outside world, to accelerate the transformation of government functions and administrative system reform, to promote the transformation of the mode of economic growth and to optimize economic structure. Hubei area covers an area of about 70 square kilometers, and its economic development has a certain emphasis on the region, as well as a certain degree of selectivity in the content of reform. Although FTA is not a depression of preferential policies, but a highland of opening to the outside world, the opening policy given by the state to FTA is still slightly inadequate, and the pressure test of FTA is insufficient. The construction of the financial regulatory legal framework of the Pilot Free Trade Zone still relies on the "three-party" and the State Administration of Foreign Exchange and other national ministries and commissions to conduct separate research and the introduction of departmental regulations. The financial reform of the Hubei Free Trade Zone will also face the problem of the government system. Since the establishment of the Hubei Free Trade Zone, various laws, regulations, and policy documents have emerged in an endless stream. It takes a long time to really understand the standard of investment in the financial industry. Even the implementation of departmental projects needs to be based on the progress of the central reform.

## 1. Introduction

On September 29, 2013, the Shanghai Free Trade Zone was established. As the first free trade zone in mainland China, its main task is to explore the new path and new model of China's opening up [1]. Promote the transformation of government functions and administrative system reforms, promote the transformation of economic growth mode and optimize the economic structure [2]. As a free trade zone, Hubei should actively respond to the country's economic development strategy and fully abide by the important principles of innovation in the process of financial reform. Goods within the Free Trade Zone are exempt from customs duties, and there are certain support policies in the areas of warehousing, exhibition and processing [3]. China's foreign trade must survive from the cracks, and it is urgent to expand the scope of foreign trade. For example, the 2008 global financial crisis further accelerated the financial cooperation among the three places. The Pearl River Delta Development Plan report proposed to build an emergency mechanism of "Guangdong, Hong Kong and Macao Regional Financial Security Early Warning System" [4]. The establishment of Shanghai FTA conforms to the current trend of global economic development. After its establishment, Hubei FTA is facing a series of problems, such as simplification of government, decentralization of power, opening up of investment field and transformation of trade mode, among which the most critical one is financial reform [5]. The financial reform of Hubei Free Trade Zone shoulders the mission of the times. It should complement and promote the development of Hubei's real economy.

After the Third Plenary Session of the Eighteenth Central Committee of the Communist Party of China, the government began to advocate and implement the policy of open reform in economic development. At the same time, we should guard against all kinds of risks and promote the establishment of free trade pilot zones with international standards [6]. Therefore, there are particularities in the financial structure and system within FTA. Today, with the integration of global economy, China should strengthen the construction of FTA finance to ensure that FTA is supported by financial reform and innovation [7]. For the Hubei Free Trade Zone to develop

smoothly, China needs to make up for the loopholes and shortcomings of today's financial laws, and propose the core legal issues and solutions in the financial field of Hubei Free Trade Zone [8]. To enable China's financial laws to keep up with the trend of financial reforms, to ensure national economic reform and development, and to pave the way for a world-wide financial center.

## 2. The overall goal of financial reform and innovation

The Hubei area covers an area of about 70 square kilometers, and its economic development has a certain focus area, and there is also a certain selectivity in the reform content. Specifically, in the key areas of development, the actual implementation scope mainly includes major development zones, economic open zones and some tourist resorts. From the specific content of development, Hubei wants to rely on the development of some important industries, such as advanced technology, port logistics, shipping services, etc., to form its own strategic plateau for open cooperation. The objectives of financial reform and innovation are mainly the following two aspects.

First, improve the overall quality of bonded work. In the process of this work, the FTA has done a good job in processing, logistics, services and other specific and meticulous work. Other work should focus on reforming the trade and investment system, realizing the transformation of manufacturing industry, enabling financial development to achieve innovation, and at the same time striving to open up the service industry. Secondly, we should change our thinking of reform and carry out innovative reforms. The overall goal of financial reform is to change the mindset and promote the development of advantageous industries and overall economic development in this region based on the actual conditions and characteristics of different regions in Hubei, so that it can set a good example for future local financial reforms. At the same time, the process and methods of financial reform must reflect the characteristics of open reform. Because open reform itself can bring great development vitality to the reform subject, bring better development opportunities for the cooperation places, and promote good cooperation and development between the two sides.

The Hubei Provincial Foreign Exchange Management Bureau issued the first implementation rules for the implementation of the “Golden Reform 30 Articles”. As of 2018, the progress of the “Golden Reform 30” innovation business is shown in Table 1.

Table 1 Progress Table of Financial Reform Business Innovation in Free Trade Zone

Serial number	Innovative projects	Accumulated development (Number of pens, sum of money summary data)
1	Cross-border two-way RMB fund pool business	28, 18.6 billion
2	Transaction of RMB and Foreign Exchange Derivatives for Overseas Institutions	\$950 million
3	There is no need to open an account to be checked for the goods trade income of A-type enterprises in FTA	4258, US\$1.56 billion
4	Direct Investment Foreign Exchange Registration Delegated to Banks	205, 11.2 billion US dollars
5	Foreign Exchange Capital Settlement Willingness of Foreign Investment Enterprises	49, 115.39 million
6	Foreign currency rent collection business for financial leasing	89, 190 million US dollars
7	Domestic Payment of Foreign Currency Equipment Prices under After-Sale Rent-Back	Twelve, US\$250 million

## 3. Problems Existing in the Financial Innovation Process of Hubei Free Trade Zone

### 3.1 The rights and policies conferred by the state are still insufficient

Although FTA is not a depression of preferential policies, but a highland of opening to the outside world, the opening policy given by the state to FTA is still slightly inadequate, and the pressure test of FTA is insufficient. For example, as the core policy of FTA's opening to the outside

world, there are many restrictions on foreign investment access, and there is a big gap compared with the negative list of international practices. In some areas, there is still a phenomenon that “the door is open and the door is not open”. For example, foreign investment enterprises have been allowed to carry out wholesale salt in the current policy, but the Ministry of Industry and Information and the salt authorities have not yet formulated relevant policies and regulations. As a result, the business license of foreign-invested enterprises cannot be processed temporarily, and there is no substantive meaning in terms of access.

### **3.2 Financial innovation lacks system and operational implementation rules**

The construction of the financial regulatory legal framework of the Pilot Free Trade Zone still relies on the “three-party” and the State Administration of Foreign Exchange and other national ministries and commissions to conduct separate research and the introduction of departmental regulations. Reform must touch the distribution of original interests, but there is not a strong agency to take the lead. Lack of system integrity and policy coordination, slow implementation of detailed rules, lack of operability, affecting the development of financial institutions services and business in Hubei Free Trade Zone.

### **3.3 The agglomeration effect of financial institutions is not significant**

In terms of financial institution agglomeration, the agglomeration effect of various non-banking financial institutions is not significant, especially the number of new functional financial institutions including equity investment, asset management and Internet finance is relatively small. In addition, the agglomeration of various financial intermediary service institutions including law, consulting, accounting, auditing, asset evaluation, credit rating, guarantee, and information services will also provide professional service support for the sound development of the cross-strait financial market system.

## **4. Exploration of Financial Reform in Hubei Free Trade Zone**

### **4.1 Hubei Free Trade Zone needs to be risk-controlled**

The financial reform of the Hubei Free Trade Zone needs to be risk-controlled. The financial reform and innovation should focus on the real economy, implement appropriate measures of the real economy and account isolation, and conduct temporary control when necessary. The Chinese banks in the free trade zone should strengthen the reform of the inspection and testing system, risk identification capabilities and risk management and control capabilities, and establish and improve relevant regulatory systems. We should be in line with international standards and establish the highest national credit system. At present, there is still a certain gap between the management of state-owned banks in China and that of international banks, which needs to be taken seriously.

### **4.2 Financial institutions in Hubei Free Trade Zone should expand their business scale step by step**

The upgrading of the original bank branches in FTA is more convenient and faster than that of the new applicant institutions. Futures is because the establishment of subsidiaries is relatively simple in procedure. Securities firms can develop their business in two directions through FTA. Firstly, listed domestic enterprises attract foreign capital equity bond financing to open up new overseas financing for Chinese enterprises. Platform. When the time is ripe, foreign companies will be allowed to list or issue bonds to attract domestic capital investment to form a new “international board”, which will further deepen the exploration of existing customer resources.

### **4.3 Hubei Free Trade Zone System Reform Should Be Progressive**

The financial reform of the Hubei Free Trade Zone also faces the problem of the government system. Since the establishment of the Hubei Free Trade Zone, various laws, regulations, and policy documents have emerged in an endless stream. It takes a long time to really understand the standard of investment in the financial industry. Even the implementation of departmental projects needs to

be based on the progress of the central reform. For the free trade zone, the construction of the legal environment and the construction of the legal system are of utmost importance. The original intention of the free trade zone is to reduce government approval. In the case of reduced government approval efforts, we should establish the corresponding regulatory capacity, otherwise there will be a regulatory vacuum. Because the capital in Hubei FTA can move freely, it is very difficult to control the finance. The reform of the system of Hubei FTA should be gradual.

## 5. Opportunities and Challenges of Financial Reform to the Development of Commercial Banks

The financial business innovation in FTA brings rare opportunities to commercial banks, but also brings new and huge challenges. The following discussion will discuss the positive impact of the free trade zone on commercial banks and some of the problems that financial reforms bring to commercial banks, and analyze the advantages and challenges of commercial banks.

### 5.1 The opportunities that financial reforms bring to commercial banks

The free trade zone is a pilot of financial reform. In the free trade zone environment, commercial banks are welcoming new development opportunities. It is conducive to improving the international operation level of domestic commercial banks, which is conducive to commercial banks' business development and innovation. Facilitation of trade and investment and financing has brought new market demand to commercial banks, and financial reform has injected new vitality into the business transformation of commercial banks.

### 5.2 Challenges of Financial Reform to Commercial Banks

On the one hand, the financial reform measures in the free trade pilot area provide favorable and convenient conditions for the development of commercial banks, on the other hand, they also bring new problems and challenges. The main issues include the following aspects.

The marketization of interest rate has brought more pressure to commercial banks in the region, because the free trade pilot area has taken the lead in the marketization of interest rate. For domestic commercial banks, due to the emergence of various investment products such as funds, trusts and so on, banks must also increase the yield of products to retain funds. The good development of the bond market has also led many well-qualified corporate financiers to turn to the bond market. This has also led to a decline in bank bargaining power. At the same time, due to the openness and inclusiveness of financial markets in the free trade pilot zone, commercial banks have largely reduced the autonomy of interest rate pricing.

From the listing of FTA to 2018, the total cross-border revenue and expenditure of cross-border RMB settlement business is 97.5 billion yuan. In this section, the cross-border income and expenditure settlement of RMB in the free trade zone accounts for 32.9% of the cross-border income and expenditure settlement of the foreign currency, as shown in Figure 1.

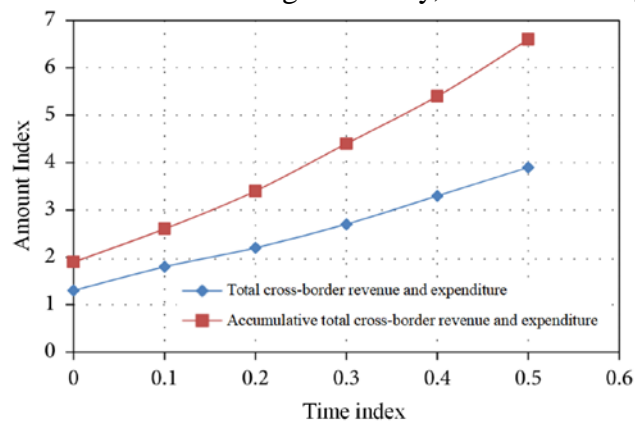


Fig.1. The total cross-border revenue and expenditure of FTA (cross-border RMB settlement business)

Under the relatively relaxed financial environment in the free trade pilot zone, domestic commercial banks in China will be more active in the development of intermediary business on the basis of traditional business, and carry out innovation and improvement of intermediary business. However, in the domestic environment, the intermediate business has the characteristics of strong risk concealment, diversification and poor controllability. Therefore, commercial banks in the Free Trade Zone will also face more complicated operational risks. Controlling risk is not only the primary consideration of the regulatory authorities, but also the basic conditions for commercial banks to achieve their own business objectives. Free Trade Zone is the pioneer of reform and innovation, but due to more innovations in financial products, there will inevitably be some management loopholes. Then it is necessary to identify and evade hidden risks by improving the sound risk supervision mode of commercial banks themselves. For the construction and development of FTA, in order to smoothly and smoothly promote the development of innovative business model, it is necessary to establish a qualified and efficient risk identification and control system.

## **6. The Important Value of Financial Reform and Innovation in FTA**

### **6.1 Financial Reform and Innovation in FTA Helps Financial Transformation**

The financial reform and innovation of FTA have improved the efficiency of international finance, international trade, international logistics and international services. FTA has gathered a large number of well-known overseas companies and auxiliary enterprises. The financial reform and innovation in FTA is conducive to promoting international and domestic financial transformation. Financial reform and innovation in FTA can provide financial settlement facilities for overseas business of trade and logistics enterprises, and provide financial platform and international settlement channels for domestic enterprises to “go out”. The domestic bonded port area will carry out offshore financial business, and a large number of “going out” Chinese-funded enterprises and the headquarters of a large number of foreign-funded institutions will enter the domestic bonded port area. In order to optimize the international trade development environment in the region, it is necessary to establish free trade and transportation policy conditions for trade and logistics enterprises stationed in domestic bonded port areas, and eliminate institutional barriers to the free flow of goods in the region.

### **6.2 Free Trade Zone Financial Reform and Innovation Will Help to Realize Investment Freedom in Transition from Domestic Bonded Port Area to Free Trade Area**

According to international experience, the internationally-run free trade zone requires investment freedom. The development of offshore financial services in domestic bonded port areas and the establishment of offshore financial markets will reduce restrictions on capital flows. Providing more convenient funds for investment enterprises in the region to open accounts, transfer, trade financing, guarantees and mortgages will help to expand the financing channels of enterprises. Provide an efficient and convenient investment and financing environment for enterprise development, further improve investment facilitation and accelerate the free flow of capital in the region.

### **6.3 Financial Reform and Innovation in FTA Can Realize Financial Freedom**

According to international experience, we should start offshore financial business, establish offshore financial market and implement loose foreign exchange management policy. Free convertibility of currencies traded in offshore accounts is allowed. In addition to capital adequacy requirements, deposit reserve is exempted, and liquidity ratio and liquidity requirements are reduced. The liberalization of interest rate fluctuations, the absence of on-site supervision of financial institutions, and only off-site supervision are conducive to the establishment and development of FTAs. Therefore, in the domestically qualified bonded port area, relevant banks and financial institutions are promoted to set up offshore financial services. The establishment of an offshore financial market will create a financial free environment in the transition from a domestic bonded

port to a free trade zone, and form a policy environment for financial liberalization in the free trade zone.

## 7. Conclusion

With the promotion of financial innovation in Hubei Pilot Free Trade Zone, the opening of capital account, and the risk of cross-border capital flows will form a major test for the success of financial reform in the Free Trade Zone. As far as the overall goal is concerned, the Hubei Free Trade Zone should continue to carry out open reforms, strengthen open cooperation with other places, and learn from the development of others. At the same time, we should change the traditional concept of financial supervision in a planned way, establish a principled concept of financial supervision, improve the quality of financial services, and realize the rapid economic development of Hubei Province.

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