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Survey Structure

- ▶ **Survey of nine bankers:**
 - ▶ 5 Loan officers
 - ▶ 3 shadow bankers
 - ▶ 1 manager of interbank lending
- ▶ **Bank types and regions:**
 - ▶ 3 mid-tier banks, Zhengzhou, Beijing, and Shanghai
 - ▶ 1 Big Four bank, Beijing
 - ▶ 2 commercial banks, Zhengzhou and Shanghai
 - ▶ Online finance business: Hefei
 - ▶ Financial services company: Beijing
 - ▶ Small loans company: Nanjing
- ▶ **Interviews conducted September 14-21, 2016**

Objectives

- ▶ Generally to understand whether distress in the banking system is growing. Specifically, whether loan demand is rising or falling, why M1 is unusually high, and why interbank transactions are so large.

Finance: Out of Options

Bankers Wait for a Crisis

- ▶ Banks are increasingly cautious about extending loans, so pressure to push out money means they lend preferentially to governments.
- ▶ They seemed flabbergasted by housing prices. One said the majority of buyers are financial institutions.
- ▶ Bankers said the government would not implement planned new restrictions on WMPs because institutions cannot afford to forego the liquidity WMPs provide.
- ▶ Loan officers reported layoffs and drastically reduced pay packets, but shadow bankers said their pay was up.

Our Q3 banking survey gives a sense of a system stilled and unwilling to make any changes that could cause a crisis. “The current real economy is generally not good,” said a shadow banker in Nanjing. “Especially for private enterprises.” If new draft regulations tightening rules around the issues of wealth management products are implemented, he said, “capital will flow out of bank channels.” Others agreed. The PBOC will not seek implementation this year or most of next, they said, because banks need cash.

The bankers said they find it harder to extend loans, since borrowers have worse repayment prospects. “Banks are more cautious about lending,” said a banker in Chengdu. A Beijing banker said, “There is no real increase in corporate loan demand, but we expect a pick-up in nationally supported projects such as shantytown development, highways, railways and PPP [public-private partnerships].” All the bank officers were seeking more lending to local government financing vehicles, because these are viewed as good credit risks.

The three shadow banks in our sample, unlike the formal banks, were increasing their loans. One commented that they were doing this to fill a gap where the formal banking system had retreated.

Banks are making more loans to property developers.

How can banks become better allocators of capital? “The best way is to let the banks collapse as soon as possible and let the market decide,” said a loan officer with a commercial bank.

Despite a white-hot housing market, the banks said their mortgages were not increasing. They were making more loans to property developers. One loan officer said that mortgages are an unattractive category because properties are flipped so quickly that the loans are assumed by other banks shortly after issuance.

Responses suggested that the banking system is tight on cash. Commercial banks and smaller financial institutions are issuing more WMPs into the interbank market than to their retail clients, because they need funding, said an interbank manager. “Generally, small and medium banks buy products issued by the Big Five and the joint stock banks.”

Notable Quotes

Layoffs and Falling Compensation at Banks

“The Big Four in Chengdu have lost staff, but layoffs are not the main reason. It’s because everyone in Chengdu banks, especially sales staff, are earning less. People are finding jobs not just in banking but in funds and trusts. The most attrition is in the business department (corporate loans, marketing, individual finance, etc.). Income for people in those departments has dropped dramatically for everyone, so they quit.” —Chengdu mid-tier bank

“No layoffs, but since H2 2015, more staff have been leaving, mostly from the front office marketing department. Among those who leave, 60% go to other joint-stock banks and many more go to trusts or financial leasing companies or other areas.” —Big Four bank, Beijing

“We have no layoffs and I have not heard of any. There is an overall pay cut or about 20% to senior management.” —Mid-tier bank, Zhengzhou

Housing Sales

“The Zhengzhou market is currently in panic-purchase mode. Land auction prices are soaring, and people have a firm expectation that housing prices will grow. . . The purchasing is mainly done by financial institutions, and financial risk is rising sharply, but it seems to still be within the tolerance range of the central government. So I don’t understand it anymore.” —Zhengzhou mid-tier bank

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Bank Lending

“Banks are more cautious about lending. The access threshold is higher, and it’s more difficult for corporations to finance, so the demand for loans in the market is bigger. However, with the regional economy deteriorating and NPLs rising, the information asymmetry has given rise to more caution in the bank industry.” —Chengdu mid-tier bank

Restrictions on WMPs

“The new rules on WMPs will not be implemented this year, and implementation in the first half of next year is unlikely. The current real economy is generally not good, especially for private enterprises. Financial returns will decline if it is implemented, and capital will flow out of bank channels.” —Nanjing small loans company

Unusual Levels of M1

“As the deposit interest rates continue to decline, the corporate sector is switching to fixed-term financial products in the pursuit of relatively stable and higher income. 2) As the economy enters a downturn, commercial banks are reducing their medium and long term loans to enterprises, leading to a slowdown in the growth of corporate sector time deposits. 3) As house prices rise, WMPs are expected to yield more than time deposits, resulting in reductions in personal deposits.” —Beijing mid-tier bank

NPLs

“In this quarter at my bank NPLs increased, and the NPL rate regionally was generally high, especially at Merchant's bank, Pingan, Minsheng, and the Big Four. Pudong Development Bank NPL pressure also increased significantly. “ Mid-tier bank, Chengdu

Why Interbank Volumes Are High

“Due to higher returns in the bond market, banks are using their own capital and capital from WMPs to invest in interest-bearing bonds and corporate paper.” —Mid-tier bank, Beijing

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