

April 11, 2016

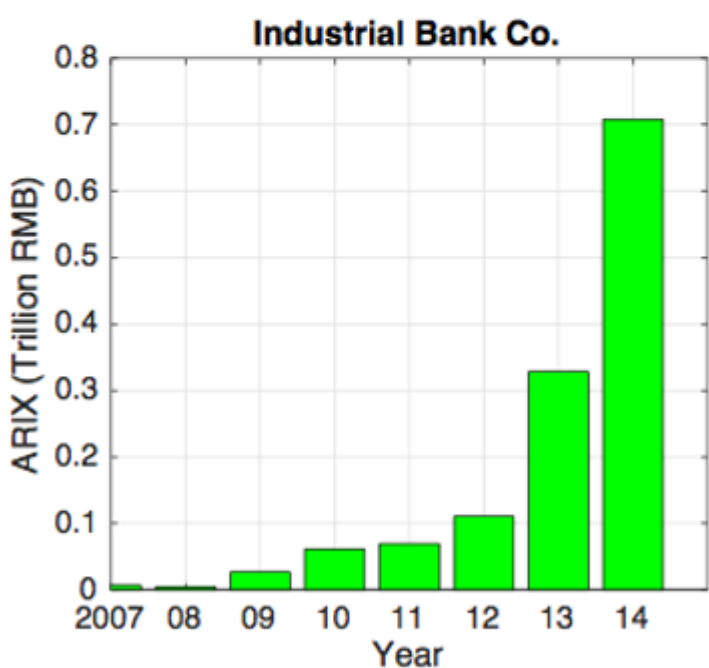
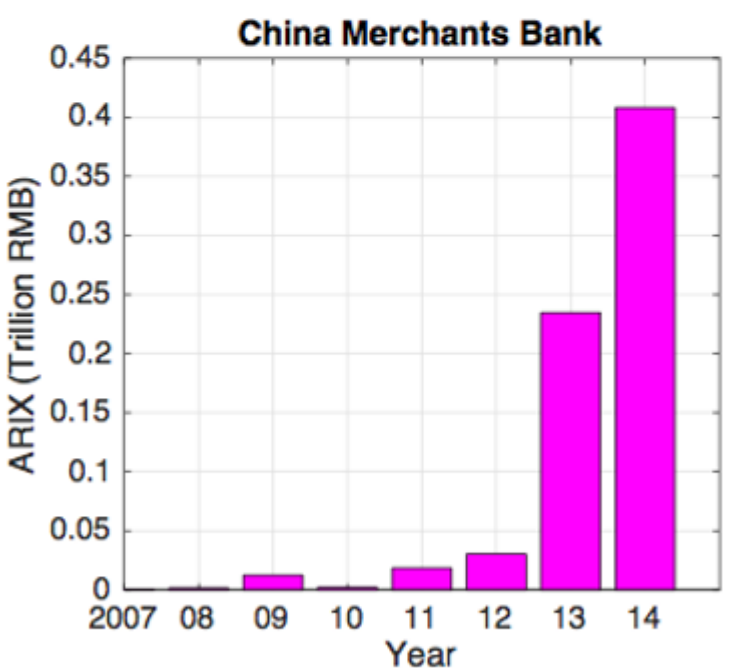
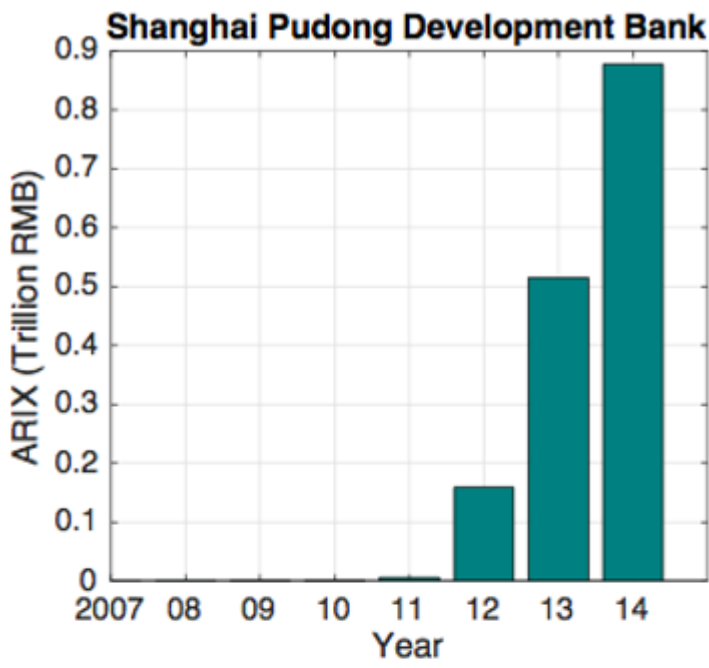
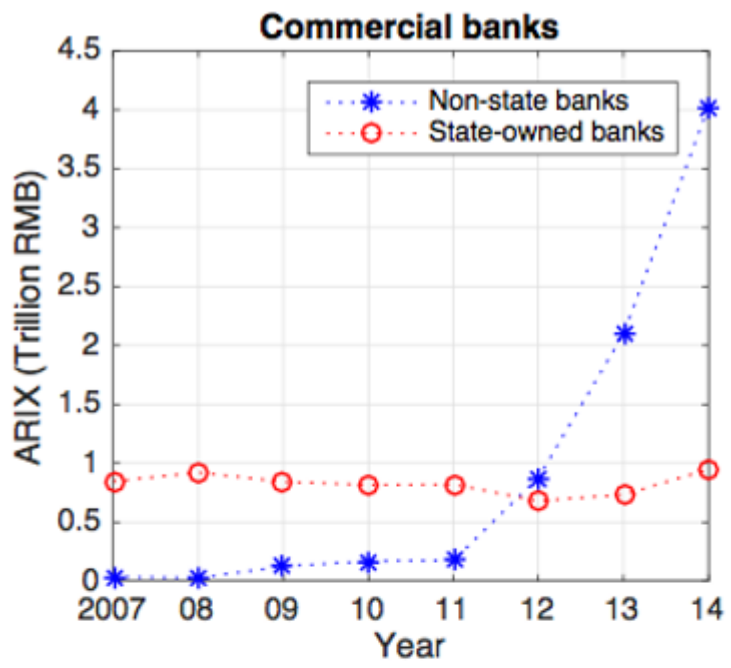
The Rise of Shadow Banking in China

China's banking system has suffered significant losses over the past two years, which has raised concerns about the health of China's financial industry. Such losses are perhaps not all that surprising. Commercial banks have been increasing their risk-taking activities in the form of shadow lending. See, for example, [here](#), [here](#), and [here](#) for some discussion of the evolution of China's shadow banking system.

The increase in risk taking by banks has occurred despite a rapid decline in money growth since 2009 and the People's Bank of China's efforts to limit credit expansions to real estate and other industries that appear to be over capacity.

One area of expanded activity has been investment in asset-backed "securities" by China's large non-state banks. This investment has created potentially significant risks to the balance sheets of these institutions (see the charts below). Using the micro-transaction-based data on shadow entrusted loans, [Chen, Ren, and Zha \(2016\)](#) have provided theoretical and empirical insights into this important issue (see also this [Vox article](#) that summarizes the paper).

Recent regulatory reforms in China have taken a positive step to try to limit such risk-taking behavior, although the success of these efforts [remains to be seen](#). An even more challenging task lies ahead for designing a comprehensive and sustainable macroprudential framework to support the healthy functioning of China's traditional and shadow banking industries.



Note: State-owned banks refer to the big four commercial banks plus the Bank of Communications. Non-state banks include 12 national joint-stock banks and other local commercial banks. "ARIX" is account-receivable investment excluding investment in central bank bills and central government bonds. Shanghai Pudong Development Bank, China Merchants Bank, and Industrial Bank Co. are examples of non-state large banks. Sources: WIND database and the microdata constructed by Chen, Ren, and Zha (2016)

[\(enlarge\)](#)



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