

## Zhou Xiaochuan: Financial services of the central bank and industrial development

Speech by Mr Zhou Xiaochuan, Governor of the People's Bank of China, at the High-level Forum of Industrial Development, Beijing, 12 January 2006.

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Ladies and Gentlemen, dear participants,

Good afternoon. First of all, let me congratulate on the inauguration of the China Industrial Development Promotion Society. Taking this opportunity, I would like to discuss financial services that central bank can provide to promote the development of other industries.

Provided jointly by commercial banks and central banks in most cases, financial services, including deposits, loans, private banking services, transactions of various financial instruments and financial market services, etc. involve many aspects and huge volumes. As these services are delivered to consumers directly by commercial banks and other financial institutions, people are likely to neglect supporting services provided by the central bank.

Many people may only have limited knowledge of the services provided by a central bank. Talking about a central bank, people may link it with macro adjustment policy, like adjusting interest rate and exchange rate, but actually only less than half of the staff in the People's Bank of China involve in macro economic adjustment works, while the others are involved in financial services. As to the financial services of a central bank, most people may directly associate them with printing banknotes, such as issuing banknotes in different series, denominations and currencies, withdrawing worn notes etc. Currently, the outstanding balance of banknotes in circulation totaled some 2.4 trillion yuan, requiring an enormous transportation and storage system by the People's Bank of China to ensure such large amount of banknotes in circulation. However, cash accounts for less than one tenth of the broad money (M2); in most circumstances, money is only numbers on customers' bank accounts. Fund transfer and payment among those accounts are realized through computer network. Accordingly, I would like to introduce five supporting service systems that the central bank provides to protect the safe operation of economy and financial industry.

First is the payment & settlement system. Previously, fund transfer between enterprises or between a holding company and its subsidiaries relied on postal system and took a lot of time, but nowadays, based on computer and electronic network, remote network system and even international multi-currency payment system, fund transfer can be realized through electronic and automatic methods. Commercial banks also have their own fund transfer system. If both the receiver and payer open accounts in the same commercial bank, internal fund transfer system can provide more convenient and faster services. Cross-bank transactions generally can be dealt with in two ways, either through correspondent bank of commercial banks, or the payment system of the central bank to settle payments. China National Advanced Payment System, run by the central bank, includes the large-value payment system that provides large-value and urgent small-value cross-bank real-time settlement services and the retail payment system, a netting payment system, whose customers are many small & medium-sized enterprises and individuals. Due to the huge economic size, the payment & settlement system managed by the central bank involves huge transaction volumes. Launched on June 30, 2005, the large-value payment system can process more than 500 thousand cross-bank transactions on average each day, involving 700 billion yuan. Each transaction can be finished within a minute. Many enterprises feel payment efficiency has improved quite a lot. China National Advanced Payment System is connected with more than 60 thousand commercial bank outlets nationwide on the basis of modern computer and communication network technology and requires both physical maintenance & development as well as application software upgrade. This system will keep on upgrading to maintain safe and high efficient payment and settlement services so as to support economic and industrial development.

Second is a credit registration system. The construction of credit registration system is to smooth information sharing and flow between financial institutions and enterprises. Basic information such as enterprise's organization framework, history and bank account, payments, credits, mortgage information etc. will make commercial banks understand much clearly enterprises reputation and fund safety when offering loans and payment and settlement services, and help business counterparts and commercial banks to make a rational judgment. Even personal information can also be covered in the

system, such as individual home mortgage loans, auto loans, credit limit of individual credit card, and information related to personal credit records. Obviously, the credit registration system is a huge system composed of the enterprise credit registration system and the individual credit registration system. The individual credit registration system was launched in Shanghai first on a pilot basis covering all Shanghai residents. Under the guidance of the State Council, in the beginning of 2003 the PBC started to establish individual credit registration system nationwide which has been put into operation recently. Together with the enterprise credit registration system established in 1997, the national credit registration system run by the PBC now covers all enterprises and individuals who have transactions with banks. Both enterprises and financial institutions are very concerned about the system. Currently, 4.52 million borrowing enterprises are registered in the enterprise credit registration system, and the outstanding balance of RMB loans reached 17.36 trillion yuan, accounting for 90 percent of total outstanding loans of financial institutions, with monthly inquiry averaging at 1.44 million times. 340 million individuals are registered in the individual credit registration system; among whom, 35 million individuals have credit records, with 2.2 trillion yuan of outstanding balance of loans, accounting for 97.5 percent of the outstanding balance of total consumer loans and daily inquiry averaging at 110 thousand times. These two systems have played a crucial role in preventing credit risks. In sum, the credit registration system will help promote the establishment of a good social credit environment. Of course, many tasks remain to be done in this regard, including improving the database, developing both hardware and software, improving relevant laws and deep processing of the information. For example, some problems are caused by the absence of defined laws or regulations on credit registration, such as, what kind of information can be used by the third party? What information cannot be provided due to privacy concern? Whether different information including bank account, payment history, tax payment, mortgage, fake goods production records and black points in the customs can be gathered in a package? In addition, information processing is very complicate due to different demands. If both the central bank and commercial banks cannot meet the needs of information, processing by the third party will require legal approval to be conducted. Currently, credit registration system has been functioning well; both the industrial and financial sectors have paid high attention to it and acknowledged its important role in China's economic and industrial development.

Third is an inter-bank bankcard information exchange system. Bankcards are mainly used by individual consumers, but many enterprises and government agencies also use them in their daily activities. The bankcard market is a competitive one with different brands issued by different companies. Without cross-bank acceptance, a POS machine placed in a shop could only process a particular bankcard, so the payment efficiency will be seriously reduced, and bankcard users will also feel inconveniency in using the cards. Accordingly, an inter-bank bankcard information exchange system must be established to realize cross-bank acceptance. Under the PBC's coordination, the China Unionpay was established by commercial banks to be responsible for the bankcard information exchange among commercial banks. Successful cross-bank transactions done through the China Unionpay in 2005 totaled 2.209 billion, involving a value of 108 million yuan. At present, the Unionpay has been registered as a brand logo that was used by all domestic RMB bankcards and also some bankcards issued by commercial banks in Hong Kong. The Unionpay bankcards are also accepted in 20 countries and regions, including Hong Kong, Macao, Singapore, Malaysia, Thailand, USA, Germany, France and Australia. It has not only facilitated the Chinese consumers to travel and spend abroad, but also exerted great impact on the development of relevant industries.

Fourth is the anti-money laundering system. Needless to say, money-laundering is harmful to sustained social and economic development and the sound performance of financial institutions. Orderly business development needs not only a good AML information monitoring system, but also relevant prevention measures and punishment mechanism. At present, AML legislation is advanced steadily. The PBC has made great efforts in different levels to set up the AML system. The first level is the AML Joint Ministerial Conference led by the PBC under the steering of the State Council. Comprising of 23 government departments including authorities of justice, public security, commerce, taxation, industrial business, customs and financial supervision, the Joint Ministerial Conference is mainly responsible for research, working out AML strategy, guideline and policy and strengthening coordination and cooperation among different government departments in drawing AML regulations and examining irregularities. The second level is the AML management system, i.e. the AML system of the PBC that is also a national system. It includes an AML irregularities inspection system targeted at financial industry, and also an AML information monitoring center, a large data processing system that detects money-laundering activities and other funds transaction clues related to other illegal actions through collecting and analyzing large-value and suspicious transaction reports from commercial

banks. The third level is to participate in international AML cooperation since money-laundering activities always connect with drug traffic and terrorist activities. Currently, China is making great efforts to join the Financial Action Task Force (FATF) and other international organizations, participate in the stipulation of international AML rules and establish bilateral supervision cooperation and information exchange in AML with other countries to create a favorable external environment for financial institutions and business entities to undergo cross-border business operation.

Fifth is a state treasury system. The state treasury system provides financial services for fiscal, taxation and customs agencies and ensures the smooth implementation of government budget as well as safe, efficient use of fiscal funds. The services of state treasury system are relatively indirect to industries and businesses. The central bank is responsible for the fund flow of state treasury system, including collecting tax revenues and allocating budget expenditure. Fiscal funds managed by state treasury belong to the whole nation; therefore, it is the PBC's responsibility to safeguard its timely and full collection and proper use. In China, each government level has its own treasury, even the government at county level, so the treasury system is also a huge one. The state treasury has also established computer network and undergone continuous upgrade to make sure that tax revenue can be timely collected and fiscal funds can be transferred on time.

To properly provide the above-mentioned services, the relevant systems should function safely and soundly without interruption, so a back-up system must be established. When the "9.11" incident in the USA took place, many people worried whether commercial banks in New York and the Stock Exchange and NASDAQ in the Wall Street could maintain its normal operation. Accordingly, how to recover from disasters has attracted much attention of the financial industry because electronic service systems play a very important role in financial market system, not only affecting cross-bank payment & settlement, but also impacting the operation of money market, bond market, stock market and foreign exchange market. The PBC is endeavoring to promote the construction of relevant back-up systems.

The above-mentioned service system provided by the central bank is not a fully competitive system, but the central bank has managed such a system in a business way to provide industrial enterprises with these social services.

In addition, the central bank also provides other important market services by establishing market platforms. The first is a foreign exchange market. People may regard the foreign exchange market as a place where financial institutions continuously trade foreign exchanges, but in fact, most of the foreign exchange trading done by financial institutions on behalf of the enterprises. Since enterprises have demands for currency exchange and risk management to manage their foreign exchange risks by foreign exchange forward or swap transactions, financial institutions first trade risks with enterprises before they go to the foreign exchange market to trade with other financial institutions. At the same time, enterprises can also participate in foreign exchange trading directly. In particular, the foreign exchange market becomes very dynamic with much stronger demands after the reform of RMB exchange rate regime on July 21 of 2005. The PBC as a central bank must establish a market-trading platform to ensure market operation, such as quotation, delivery and clearing, at the same time to maintain a good market order.

The second is an inter-bank bond market. This market now is keeping on growing. In terms of bond transactions, some 3730 enterprises participate in the market apart from the financial institutions. Market participants can manage their own account by investing in bonds or other financial instruments with their short-term idle money. At present, the inter-bank bond market has developed more abundant products to help enterprises manage their funds, especially, enterprises with different revenue time period. For example, some may spend more money in the first half of a year and receive more in the second half, while others are fee-collecting enterprises, like water companies and power plants, which collect money on monthly basis. The inter-bank bond market also provides electronic delivery and settlement services to much more participants than the foreign exchange market does.

The third is a gold market. Gold is a kind of metal as well as a production material. In some industries, particularly in electronic industry, gold is used quite often; in addition, gold is also used in jewelry industry. Accordingly, gold is involved in foreign trade in large volume. To regulate and develop the gold market in China, the PBC established Shanghai Gold Exchange in 2002. Shanghai Gold Exchange now has 128 members, among which, 110 members are involved in industry of gold production, consumption and refinery. Enterprises can conduct gold transactions, invest and hedge risks through the gold market.

Those examples explain how the central bank together with commercial banks and other financial institutions establishes market platforms for industrial enterprises in terms of financial services and

provides good services to satisfy enterprises' demands in market. Of course, the central bank is mainly responsible for stipulating market rules and resolving relevant problems.

Today, I introduced the financial services provided by the PBC in terms of financial support service system and market platforms, which are highly related to economic development and industrial development. Along with economic development, the central bank will meet higher demand for financial services with regard to service level, size and safety and face new challenges in preventing and cracking down money-laundering and banknotes counterfeits activities. Together with other partners in the society, the central bank will utilize modern technology to accelerate service innovation and improve financial services so as to promote the rapid development of financial industry and the whole economy and other industries.

Thank you.