Discussion of “What We Learn from China’s Rising Shadow Banking” by Chen, Ren, and Zha

Kinda Hachem
Chicago Booth

Pacific Basin Research Conference
November 18, 2016
Summary

- Monetary tightening between 2010 and 2013

- Saw ↓ bank loan growth but ↑ entrusted loans
  - Entrusted loans = firm-to-firm loans facilitated by trustee
  - Small banks facilitated more entrusted loans to “risky” industries than did large banks or non-bank trustees

- Rise of entrusted loans coincides with higher ARI on asset side of bank balance sheets
  - Based on this, authors conclude risks from entrusted lending were brought on balance sheet
Questions About Model

• Banks choose between:
  – Cash
  – Safe Loans
  – ARI on Risky Loans

• To disentangle LDR from safe-loan regulation, should allow another possibility:
  – ARI on Safe Loans

• Use model to see whether this prevails in equilibrium. If yes, need to reconcile with data.
Questions About Model

• Also need to defend assumption that ARI on risky loans has same maturity as deposits

• Regression (1) from paper:

\[ s_s = \alpha + \alpha_t + \alpha_m m_s + \alpha_r I (\text{Risky}_i) + \varepsilon_s, \]

• Find \( \alpha_m < 0 \) and \( \alpha_r > 0 \). How to get from this that loans to risky industries are short-term?

• Maybe \( \alpha_m < 0 \) because longer-term loans made when partial liquidation is possible
Questions About Timing

- Biggest jump in entrusted lending is in 2013, well into the “contractionary” phase

- From Figure 2 of the paper:
Questions About Timing

• Same for ARI. No ARI time series in paper but from Figure 4 of authors’ VoxEU column (March 2016):
What Happens In 2013?

• CBRC crackdown on bank-trust cooperation in WMP issuance. Led to rise of TBRs which are a type of ARI. From Hachem and Song (January 2016 V):

---

**Diagram Description**

- **WMP Buyers**
  - **Bank A (or its SPV)**
  - **Bank B (or its SPV)**
  - **Trust Company**

**Business b/w counterparts**
- Bridge company can stand between to further obfuscate
- Bank B (or its SPV) books reverse repo or investment receivable
- Compliant since funds did not come directly from WMP
What Happens In 2013?

- CBRC crackdown on bank-trust cooperation in WMP issuance. Led to rise of TBRs which are a type of ARI. From Hachem and Song (January 2016 V):
Shadow Banking More Generally

• Authors’ main data source is entrusted loan announcements by listed firms

• According to Allen et al (2015), announcements by listed firms accounted for 10% of all entrusted lending reported by PBOC in 2013

• Big remainder could be trust lending in disguise
Shadow Banking More Generally

**Breakdown of China's Debt-to-GDP**

- Shadow Finance
- Corporate Bonds
- Bank Loans

**Breakdown of Shadow-to-GDP**

- Undiscounted Bankers' Acceptances
- Other Credit
- Trust Company AUM
- WMPs Outstanding

Notes: The right panel divides “Shadow Finance” from the left panel into undiscounted bankers’ acceptances and other credit. The AUM and WMP series are then superimposed on other credit.

Sources: NBSC, PBOC, CBRC, IMF, China Trustee Association, KPMG Trust Surveys