

TONG Bing (仝冰)

# Dual-Track Reform of Interest Rates: China's Path

## 利率双轨制改革：中国的路径

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It is generally believed China's financial reform lags behind its economic development. The market-oriented reform of interest rates began in the late 1990s, twenty years after 1978, when the policy of reform and opening up was initially put forward. During that time, the financial system was dominated by the banking sector, a subsidized credit system which channeled household savings at low interest rates into state-guided borrowing for investment (this situation hasn't changed much until today, unfortunately). Non-banking financial sector was negligible; state-owned enterprises have the priority to cheap credit supplied by banks, which are crucial for their survival. The People's Bank of China (PBoC) set the same retail interest rates for all

在就任美国总统这一年多时间里，特朗普古怪的行为模式一直困扰着政治家、记者甚至科学家。他正在运用这种方式建立一个新的世界秩序，那些曾经被习以为常的世界准则正面临突如其来地挑战。

中国的利率市场化改革起始于1990年代末期，在此以前，商业银行执行由人民银行规定的统一的存贷款利率。国有企业享有优先得到低息贷款的权力。由于中国的银行业在金融



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commercial banks and set different lending quotas for each bank. The government took a cautious attitude toward the reform of interest rate liberalization, at least partly because in the absence of deposit insurance, intense competition among banks may lead to instability of the banking system, and hence negative impacts on the real economy.

Financial reform accelerated during the past few years. In July 2013, the PBoC abolished the control of lending rates, and in October 2015, removed the ceiling of deposit rates. However, these measures do not indicate that interest rates are fully market-determined, as acclaimed by the media at that time. Official restrictions were cancelled, but only to be replaced by hidden controls. An industry self-disciplinary mechanism of market interest rate pricing, established in September 2013 and intended to avoid disorderly competition among commercial banks, imposed de facto restrictions on nominal interest rates. Commercial banks did not get full pricing power for their funds; the central bank continues to intervene in credit allocation and issue benchmark interest rates. And the financial market is still divided, characterized as a dual-track interest-rate system: on the one hand, retail interest rates of saving deposits and loans are administratively controlled; on the other hand, most asset prices in currency, bond and stock markets—including the interest rates of interbank markets—have been liberalized. This is why the dual-track interest rate reform was launched in 2018, a new round of market-oriented reform of interest rates which aims to integrate the two tracks of interest rates: regulated and market-determined interest rates.

The dual-track reform is a successful experience of China's reform. China chooses a path of reforming in small incremental steps, instead of a radical transformation as practiced in Russia and Eastern

部门中长期占据主导地位，获得低息资金对于企业的发展至关重要。而且银行间的竞争可能会引起银行业的不稳定。因此中央政府对于利率市场化改革一直采取谨慎态度。从1998年开始，人民银行按照“先外币、后本币；先贷款、后存款，先长期、后短期”的思路推进利率市场化改革。

最近几年，改革的进程明显加速。2013年7月中国人民银行取消了贷款利率管制，2015年10月取消存款利率上限。但是，这些措施并不表明利率市场化的胜利完成。2013年9月成立的银行业内的市场利率定价自律机制，在约束商业银行恶性竞争的同时，也形成了事实上的存款利率上限。商业银行还没有完全的资金定价权；央行仍然发布存贷款基准利率作为重要参考。金融市场仍然处于分割的状态：一方面，存贷款零售利率仍然受到行政管制；另一方面，货币和债券市场等金融同业市场利率主要由市场决定。在2018年开始的新一轮利率市场化改革，主要目的是实现货币市场利率与信贷市场利率的两轨并一轨。

双轨制改革是中国改革的成功经验。以商品市场的价格改革为例：中央政府的改革策略是对于存量商品的

Europe. Take the price reform as an example: the government introduced market prices at the margin of the pre-existing state-controlled prices, gradually nibbled up the planned economy with the market, and finally realized a unified market economy. The price reform began in 1978 in rural areas. By 1985, market prices of agricultural products were basically the same as administrative prices. After 1986, the two systems of prices were integrated as a single one. Then the main battlefield of reform shifted from rural to urban areas. The government gradually removed price control of consumer and capital goods in most cities. By the end of 1993, prices of more than 97% of iron and steel products and the majority of electromechanical products had been liberalized. After 1994, prices of nearly all industrial products were determined by the market. This marks that China has basically completed the dual-track reform of its price system.

The reform of China's financial market follows roughly the same path. In recent years, the traditional business scope of the banking industry was constantly penetrated by trust, insurance, asset management and securities, which leads to substantial changes in the financial structure. The change is reflected in a new statistical indicator put forward by the PBoC in 2010: "aggregate financing to the real economy (AFRE)", i.e. total volume of financing provided by the financial system to the real sector, which is a broad measure of credit and liquidity in the economy. This statistic shows that the proportion of bank loans in AFRE (flow) declines from 92% in 2002 to about 50% in 2013, and then returns to about 90% in 2018 due to the internalizing of "off-balance-sheet" financing. The AFRE (stock), an indicator more comparable internationally, shows that the share of bank loans reaches 70% by July 2019, dropping 20 percentage points from that in 2002. Meanwhile, other items in the AFRE, such as off-balance-sheet financing (i.e. shadow banking)

价格保持计划管制，放开增量的价格，从边际上引入市场，然后再逐步用市场蚕食计划，最后实现单一市场。1978 开始的改革从农村起步，到 1985 年农产品的市场价格与官方价格基本一致，到 1986 年以后完全由市场决定。1984 年以后，改革的主战场从农村转向城市，逐步放开了大多数城市耐用消费品、生产资料的价格管制。到 1993 年底，97 %以上的钢铁产品和绝大多数机电产品价格已放开，绝大部分工业生产资料市场和消费品市场已完全放开由市场调节。这标志着我国基本上完成了从双轨价格向市场价格的并轨。

我国金融市场的改革也大致遵循了同样的路径。信托、保险、资管、证券不断的渗透银行业务范围。央行发布的（流量）社会融资规模统计数据显示，银行贷款占社会融资的比例在 2002 达到 92%，随后逐年下降至 2013 年的 50%左右。到 2019 年 7 月底，（存量）社会融资规模达到 214.1 万亿，其中银行表内贷款 147.7 万亿，占比为 70%。而在 2002 年，这一数值接近 90%。社会融资规模中的其他项——包括金融机构通过表外提供的融资（即影子银行）和直接融资——占比增加。另外，互联网金融、民间借贷也蓬勃发展。这些都使

and direct financing, display quick expansion. In addition, online and informal financing are booming. All of these make the impact of official controls over deposit and lending rates decrease. Nevertheless, the banking industry still dominates the financial system. By the end of the second quarter of 2019, the assets of the banking industry account for 91.1% in those of the financial sector and the liabilities account for 91.9%.

Financial markets are far more complex than goods markets, and the deregulation of capital prices is more challenging. Due to the lack of financial instruments, the PBoC has to intervene directly by setting loan quotas and retail interest rates of all maturities, an operation too drastic for a smoothly functioning market economy. The market-oriented reform would imply that the central bank abandons the price control over credit and broader monetary aggregates, as well as quantitative constraints such as loan quotas, and chooses instead the price of monetary base as the main policy tool. During the process, missing links in the transmission channel—from the short-term interest rates affected directly by monetary policy to the broad range of market interest rates that affect investment and consumption spending—have to be established. The ultimate goal of interest rate reform is to achieve a competitive financial market with ample instruments—to set the price of and hence allocate capital based on market forces, and to channel funds efficiently into where money is most needed—and an effective monetary policy transmission mechanism. And the efficacy of monetary policy is measured by the speed of changes in the policy rate spreading across the markets of bonds, stocks and credit, the degree of their pass-through to the bank retail rates and the predictability of their impact on the real economy.

得存贷款利率管制的影响逐步下降。尽管如此，银行业在整个金融体系中仍然占据主体地位，截至 2019 年 2 季度末，银行业资产占金融业总资产的 91.1%，负债占比 91.9%。

金融市场远比商品市场更加复杂，资产价格的并轨也更加有挑战性。利率并轨的终极目标是形成一个有效竞争的金融市场和顺畅的货币政策传导机制。传统的直接调控存贷款利率的货币政策过于猛烈，利率市场化意味着央行放弃对信用价格的管控，而通过影响基础货币的价格——从货币市场的短期政策利率传导到其他金融市场利率，尤其是银行零售利率——从而影响实体经济的运行。2019 年 8 月，人民银行宣布各银行应在新发放的贷款中主要参考贷款市场报价利率（LPR）定价，这意味着 LPR 将替代此前的贷款基准利率，成为贷款利率的新基准。新一轮的利率市场化改革迈出了重要一步。而利率市场化改革本身，是中国金融改革的一部分。未来的改革还包括汇率市场化和资本账户可自由兑换，这些将是更为重大的挑战。

仝冰现为河南大学金融发展与风险评估实验室副教授，毕业于北京大学国家发展研究院

In August 2019, the PBoC announced that commercial banks should price new loans with reference to the loan prime rate (LPR), a new tool to implement policy objectives and to replace the previous benchmark lending rates. The new LPR contributes to a smoother policy transmission mechanism by constituting a missing link between banks' retail lending rates and the PBoC's medium-term lending facility (MLF), which itself was created in September 2014 to provide selected banks with funds to maintain liquidity by allowing them to use securities as collateral. It is an important step of the dual-track reform to liberalize the country's rigid interest rate policy, but there is still a long way to go. The PBoC has yet to loosen the ceiling on commercial bank deposit rates as currently mandated by industry self-disciplinary mechanisms. De facto interest rate liberalization requires the elimination of structural distortions in financial markets and the real economy, which is part of broader market reforms—the transition from a planned to a market system is not a big bang, but a continual process. And other items on the agenda of financial reform, including liberalization of exchange rates and convertibility of capital accounts, are still tougher challenges.

*TONG Bing is associate professor at the school of economics at Henan University and member of the CFDS. He graduated from the National School of Development at Peking University.*