

Annette Kleinbrod

# **The Chinese Capital Market**

Performance, Parameters for  
Further Evolution, and Implications for  
Development

Deutscher Universitäts-Verlag

# Table of Contents

List of Figures .....	XIII
List of Tables .....	XVII
List of Abbreviations .....	XIX
General Notes .....	XXI
<b>1 Introduction .....</b>	<b>1</b>
<b>2 The Significance of Effective Development in China .....</b>	<b>5</b>
2.1 Stability and Welfare as Governance Maxims throughout the Millennia .....	6
2.1.1 Momentous Historical Occurrences .....	6
2.1.2 From Sophisticated Power to Stunted Performance .....	10
2.2 China's Development Since 1978 .....	14
2.2.1 Stability and Welfare Throughout the Course of the Reform Period .....	15
2.2.2 A Note on Conduct to Imminent Instability .....	17
2.2.3 Unequalled Achievements in Regaining Momentum .....	20
2.3 Considerations for the Future Path of Development .....	26
2.3.1 A Broad Array of Challenges .....	27
2.3.2 The Paramount Importance of the Financial System .....	29
<b>3 The Connection Between the Capital Market and Development .....</b>	<b>33</b>
3.1 General Aspects of Financial System Design .....	34
3.1.1 Resuming the Bank-based Versus Market-based Debate .....	35
3.1.2 Limited Applicability of an Overall Concept of Efficiency .....	37
3.1.3 Principle of Dynamism and Evolutionary Capability .....	39
3.2 The Finance-Growth and Finance-Development Link in Theory and Empiricism .....	41
3.2.1 Theoretical Concepts .....	42
3.2.2 Empirical Studies .....	43
3.3 Resulting Research Method .....	47
3.3.1 Fundamental Features of the Development Structure .....	48

3.3.2 Overview of the Role of the Capital Market in Effective Development.....	54
3.3.3 A Functional Perspective as a Starting Point .....	56
3.3.3.1 The Functional Perspective Concept.....	57
3.3.3.2 Functions of the Capital Market.....	58
3.3.3.3 Essential Details of Stock and Bond Markets .....	64
3.3.4 Evaluating the State of the Capital Market .....	70
3.3.4.1 General Statistical Data on Capital Market Capacity.....	70
3.3.4.2 Capital Market Development Indicators .....	70
3.3.5 Parameters Influencing the Capital Market.....	72
3.3.5.1 Basic Considerations.....	73
3.3.5.2 Eight Significant Parameters Depicted as Spheres .....	74
<b>4 The Current Performance of the Chinese Capital Market.....</b>	<b>78</b>
4.1 Rationale for the Stock and Bond Markets' Re-emergence Since the 1980s.....	79
4.2 The Stock Market Segment.....	81
4.2.1 Relevance of the Stock Market in Raising Capital .....	82
4.2.2 Particularities as to the Differentiation into Diverse Share Categories.....	84
4.2.2.1 Shares of Companies Incorporated in China.....	85
4.2.2.2 Shares of China-related Companies Incorporated Outside China.....	91
4.2.2.3 Market Segmentation in Transition.....	93
4.2.3 Companies Quoted on Domestic Stock Exchanges .....	99
4.2.3.1 Number of Listed Companies .....	100
4.2.3.2 Industrial Distribution .....	103
4.2.3.3 Regional Distribution .....	107
4.2.3.4 Selected Financial Indicators and Overall Performance .....	109
4.2.4 Investors in Domestic Stock Exchanges .....	116
4.2.4.1 Number of Investors.....	116
4.2.4.2 Composition of Investors .....	120
4.2.4.3 Regional Distribution of Investor Accounts.....	126
4.2.5 Data on Stock Market Performance .....	131
4.2.5.1 Total and Tradable Market Capitalisation.....	131

4.2.5.2	Trading Volume .....	134
4.2.5.3	Turnover .....	137
4.2.5.4	Average Turnover Rate .....	138
4.2.5.5	Price to Earnings Ratio .....	140
4.2.5.6	Stock Exchange Composite Indices .....	143
4.2.5.7	Essential Periods Causing a Shift in Performance Direction .....	145
4.3	The Bond Market Segment .....	149
4.3.1	Relevance of the Bond markets in Raising Capital .....	151
4.3.2	Features of Existing Bond Categories .....	156
4.3.2.1	Treasury Bonds .....	157
4.3.2.2	Financial Bonds .....	162
4.3.2.3	Enterprise Bonds .....	164
4.3.3	Secondary Market Options .....	167
4.3.3.1	Interbank Market .....	168
4.3.3.2	Stock Exchanges .....	169
4.3.3.3	Bank Over-the-Counter Market .....	170
4.3.3.4	Towards Higher Secondary Market Efficiency .....	171
4.3.4	Data on Bond Market Trading .....	172
4.3.4.1	Weight of Bond Trading on the Interbank Market .....	172
4.3.4.2	Trends of Bond Trading on Stock Exchanges .....	175
4.3.4.3	Initial Phase of the Bank Over-the-Counter Market .....	183
4.3.4.4	Overriding Requirements for Bond Trading .....	184
4.4	A China-International Comparison of Capital Market Development .....	185
4.4.1	China's Stock and Bond Market Development as a Basis for Comparison .....	186
4.4.2	State of Affairs in Selected International Countries .....	193
4.4.2.1	United States and Germany .....	193
4.4.2.2	Japan and India .....	195
4.4.2.3	Asian Tiger Economies .....	197
4.4.2.4	Asian Panther Economies .....	201
4.4.3	A Concluding Remark on the Use of China-International Comparisons .....	205

4.5 Recapitulatory Notes on the Performance of Capital Market Functions .....	207
<b>5 Significant Parameters for the Chinese Capital Market .....</b>	<b>211</b>
5.1 Institutional Framework .....	212
5.1.1 The Potential Impact of the Institutional Framework on the Capital Market ...	212
5.1.2 An Evolving Institutional Framework in China .....	214
5.1.2.1 Formal Rules .....	214
5.1.2.2 Enforcement of Formal Rules .....	215
5.1.2.3 <i>Guanxi</i> as the Basis of Informal Rules.....	216
5.1.2.4 The Danger of Disregarding Rules.....	217
5.1.2.5 Concluding View on the Impact of the Institutional Framework.....	219
5.2 Corporate Governance.....	220
5.2.1 The Potential Impact of Corporate Governance on the Capital Market.....	221
5.2.2 Pivotal Features of Corporate Governance in China.....	223
5.2.2.1 Diversification of Ownership Forms.....	224
5.2.2.2 Relationship Between Companies and Shareholders .....	226
5.2.2.3 Scope of External Incentives and Directives.....	230
5.2.2.4 Potential for Incentives Based on Agreements .....	232
5.2.2.5 Concluding View on the Impact of Corporate Governance.....	234
5.3 Reputational Agents .....	235
5.3.1 The Potential Impact of Reputational Agents on the Capital Market .....	235
5.3.2 The Role of Reputational Agents in China .....	236
5.3.2.1 The Media as a Case in Point for the Realm of Possibility.....	236
5.3.2.2 Rating Agencies as an Illustration of the Long Road Ahead .....	238
5.3.2.3 Concluding View on the Impact of Reputational Agents .....	239
5.4 Key Stakeholders Acting For Society .....	240
5.4.1 The Potential Impact of Stakeholders Acting for Society on the Capital Market .....	241
5.4.2 Key Stakeholders Acting For Society in China .....	242
5.4.2.1 Social Organisations.....	243
5.4.2.2 Research Entities and Individual Personages.....	248

5.4.2.3 Ethnic and Spiritual Groupings .....	251
5.4.2.4 Cyberspace Connectability.....	251
5.4.2.5 Concluding View on the Impact of Stakeholders Acting for Society ...	253
5.5 The General Political and Economic Situation .....	253
5.5.1 The Potential Impact of Policy and the Economy on the Capital Market.....	254
5.5.2 Policy and Economy in the Course of the Reform Measures Started in 1978 ..	254
5.5.2.1 Political Actions Under the Fourth Leadership Generation .....	255
5.5.2.2 Towards Higher Economic Efficiency .....	255
5.5.2.3 Concluding View on the Impact of Policy and the Economy .....	256
5.6 Societal and Demographic Affairs .....	257
5.6.1 The Potential Impact of Societal and Demographic Affairs on the Capital Market .....	257
5.6.2 Fundamental Changes in Society and Demography in China.....	259
5.6.2.1 Changes in Income Levels and Distribution .....	260
5.6.2.2 Population and the Ageing Society .....	261
5.6.2.3 Concluding View on the Impact of Societal and Demographic Affairs.....	265
5.7 The State of Technology and Infrastructure.....	265
5.7.1 The Potential Impact of Technology and Infrastructure on the Capital Market .....	266
5.7.2 Trends of Technology and Infrastructure in China .....	266
5.7.2.1 The Role of Information and Networking Technologies .....	267
5.7.2.2 Overcoming the Infrastructure Bottleneck .....	268
5.7.2.3 Concluding View on the Impact of Technology and Infrastructure.....	269
5.8 Regional and Global Integration .....	269
5.8.1 The Potential Impact of Regional and Global Integration on the Capital Market .....	270
5.8.2 The State of China's Regional and Global Integration .....	270
5.8.2.1 The Level of Regional Integration .....	271
5.8.2.2 The Significance of the Accession to the World Trade Organization...	271

5.8.2.3 Tendencies of Interest .....	272
5.8.2.4 Concluding View on the Effect of Regional and Global Integration ...	273
5.9 Closing Notes on Significant Parameters.....	273
<b>6 Opinions on Capital Market Performance and Its Potential .....</b>	<b>276</b>
6.1 Method of Data Acquisition.....	276
6.2 Survey Results.....	277
6.2.1 Contribution to Financing Effective Development .....	278
6.2.2 Accomplishment of Capital Market Functions .....	283
6.2.3 Influence Exerted by Significant Parameters .....	291
6.2.4 Reciprocal Influence of the Significant Parameters .....	305
6.2.5 Greatest Obstacles to Further Capital Market Evolution .....	314
<b>7 Prospects of the Capital Market and China's Development .....</b>	<b>317</b>
<b>Appendix .....</b>	<b>325</b>
A Side Note on General Facets of the Notion of Corporate Governance .....	326
A.1 Diversity in Corporate Governance Perceptions.....	326
A.2 Mechanisms Giving Direction to the State of Corporate Governance.....	331
A.2.1 Primary Participants and Internal Mechanisms.....	331
A.2.2 External Incentives and Directives.....	332
A.2.3 Stimuli Based on Agreements .....	334
B Side Note on the Civil Society Approach.....	336
B.1 From a Philosophical and Political Concept to a Buzzword.....	336
B.2 Re-examination of this Concept's Applicability to Today's China.....	338
C Glossary.....	342
<b>Literature and References .....</b>	<b>353</b>
<b>Data Sources .....</b>	<b>431</b>
<b>Major Regulations, Rules, and Measures Mentioned in the Text.....</b>	<b>434</b>