UNH research recommends new regulatory structure to mitigate financial risk in China

January 26 2011

New research from the University of New Hampshire suggests that China should establish a unified supervisory agency, similar to what is used in Singapore, to oversee its complex financial sector.

The new research by Honggeng Zhou, associate professor of decision sciences, and Wenjuan Xie, assistant professor of finance, both at UNH, is presented in the working paper "Challenges for the Unified Financial Supervision in the Post-crisis Era: Singaporean Experience and Chinese Practice." The paper is co-authored by Jing Geng of Harvard University and GuiBin Zhang of Monash Asia Institute.

"The United States is a good example of a country that encountered significant financial repercussions because of the lack of integrated financial supervision. Because China has not allowed free exchange of its currency in the financial market, China was not hurt as much as the United States in the financial crisis. However, as China allows more flexibility in its currency market and its economy is more globalized, China could face serious financial consequences if China does not move toward a more unified supervisory agency model," Zhou says.

A unified supervisory agency oversees a number of financial entities that have increasingly complex relationships, such as banks, investment banks, finance companies, asset managers, securities brokers, and insurance companies. An advantage of unified financial supervisory agency is that it monitors financial products as well as financial institutions.

The discussion of unified financial supervisory agencies has been a hot topic worldwide following the financial crisis. In the United States, the most recent financial reform bill signed by President Barack Obama in July 2010 includes the creation of the Financial Stability Oversight Council, which is a move toward integrated financial supervision.

Worldwide countries such as Australia, Canada, Denmark, Japan, Korea, Norway, Singapore, Sweden, and the UK formed an informal club of "integrated supervisors" right after the 1997 financial crisis. These countries have reformed their supervisory functions in response to the emerging international trends of blurring of boundaries between financial industries of banking, insurance and capital markets, as well as financial conglomeration.

The world's second-largest and fastest-growing economy, China currently has separate entities that supervise and regulate different parts of its enormous financial system. The researchers recommend China take a gradual approach to creating an integrated mega-functioning supervision body.

"The world financial markets are experiencing a special revolution. The emergence of new products -- new risk management techniques and cross-border financing -- has changed the traditional financial structures. The phenomenon of financial conglomerates, cross industry financial products and its impact on traditional supervision model have not only attracted theoretical researchers' attention but also financial regulators into considering how they can supervise financial institutions, products and markets better. How to view the phenomenon of universal banking and financial holding business -- how to evaluate its influence and make reasonable response -- are questions that need study using multi-dimensional and comprehensive analysis based on modem economic theories," Xie says.

Provided by University of New Hampshire