

FINANCIAL SECTOR IN CHINA AND IN NORWAY

The Norwegian Experience

- **1970s:** Inflation and negative real interest rates
Credit budget to reduce volatility
Based on credit rationing
Grey market is growing (Banks also participate)
- **1980-1988:** Inflation continues and difficult to sustain the system
Private sector quite innovative
Credit budget is done away with
Competing on market shares



- **1988-1992:** Gorbachev meets Deng (May 1989)
Berlin Wall crumbles (November 1989)
Full convertibility of NOK (July 1990)
German economic reunification (July 1990)
 - Need for a real appreciation. France declines a nominal one. Inflation follows. And Bundesbank starts raising interest rates. Which spreads to the rest of the world.
NOK cannot maintain fixed exchange rate, and floats (December 1992)

*Combination of domestic decisions and external events
And a banking community not understanding its trade*

- **1992-2001:** Restoration rule to stabilize the external of the NOK (1994)
Inflation coming down
State oil Funds starts filling up (1996)



- **2001-2007:** Inflation targeting (March 2001)
Rough ride for the NOK – at 7,25 to the euro in January 2003
Labor market learns to live with inflation targeting

Parallels to China

- Private Sector is quite innovative.
- Over time difficult to have interest rates lower than what the markets dictate.
- Grey market important in China. Makes for more efficient distribution of capital.
- Will not borrow in State Banks because of tax evasion.



- Developing assets markets takes time
 - Stock market – finally flying – after learning process
 - Bond market – in the making?
 - Real estate market since late 1990s
 - Law on property in March 2007
- With well developed markets, diversification is easier, and the effects on the real economy of one market going bananas is dampened.
- Difficult to introduce the market mechanism in financial markets.
- Recapitalization of Norwegian banks early 1990s: 3,5% of GDP



- Recapitalization of Chinese banks a decade later: 10,4% of GDP
 - And the job is yet not done. Keep producing NPLs
 - ABC has not yet found a Strategic Partner
 - To learn the trade of banking from SPs seems like a good strategy
- July 1990, full convertibility of NOK and managing the exchange rate becomes difficult.
- China makes her RMB/USD remarkably well. For how long?
 - Allow outflow, e.g., buy stocks etc in Hong Kong.
 - External events may make the money flowing back.
 - And a solid appreciation of the RMB may be hard to avoid.



- Well known – can only have two of the three:
 - Independent interest rate policy
 - Free capital movements
 - Managed exchange rate
- From export- and investment- driven growth to consumption led, and the time may be ripe for full convertibility of RMB. But I am not quite convinced. At any rate, start with floating, having the business community learn to live with that.

