
Keynote Speech by Governor of People's Bank of China, Zhou Xiaochuan, at China Global Debt Capital Markets Congress

(November 16, 2010)

Distinguished Guests, Ladies and Gentlemen,

Good morning! I am very glad to attend the China Global Debt Capital Markets Congress co-hosted by the National Association of Financial Market Institutional Investors (NAFMII) and Euromoney, and to discuss the problems of our concern as well as the development of the Chinese debt capital market with you. According to the theme of this congress, I would like to address a few points.

I. The current climate of the Chinese economy is generally favorable.

According to the macroeconomic data in the first three quarters of 2010, the Chinese economy is continuing along the path expected by macro adjustment and control policy, and is further consolidated the momentum of changing for the better. This is principally evidenced in the following aspects including steady and rapid consumption growth, improvement of investment structure, continued recovery of foreign trade, enhanced coordination between consumption, investment and export in driving the economic growth stable development of agricultural production, sustained fast growth of industrial production, better-than-expected employment situation, and stable growth of the residents' income. In the first three quarters, the GDP reached RMB26.9 trillion, which means growing 10.6% year on year in terms of a stable currency, and the growth rate is 2.5 percentage points higher than that of 2009. Overall, the national economy is maintaining a good operating status.

However, we must be aware that the current environment of economic development is still very complicated. Uncertain factors are emerging in the global economic operation from time to time, recovery of the advanced economies is slowing down, the money supply is loose in succession, and some emerging economies are seeing rapid growth, but also facing certain pressure from capital inflow. The foundation for the domestic demand recovery remains imbalanced, private investment and endogenous growth drive need to be reinforced, and the tasks for expanding residents' consumption, improving income distribution and promoting the adjustment and optimization of the economic structure remain challenging. The upward pressure of price requires attention from different parties.

In facing of the aforesaid situation, we will continue to adopt the following measure: firstly, to implement macro adjustment and control policy,

and focus on enhancing the pertinence, flexibility and effectiveness of the policy; secondly, to strengthen liquidity management, and to maintain the moderate growth of money and credit; thirdly, to reinforce the financial support to the transition of economic development pattern and the adjustment of the economic structure; fourthly, to steadily promote the reform of interest rate liberalization, and further improve the exchange rate formation mechanism of Renminbi; and last but not least, to further propel the healthy development of the financial market.

II. The Chinese bond market has made a long stride

In recent years, the CPC Central Committee and the State Council have implemented a series of policy measures to vigorously boost the development of the bond market. In 2004, the State Council published “Some Opinions of the State Council on Promoting the Reform, Opening and Steady Growth of Capital Markets”, elaborating on the positive and prudential development of the bond market, and encouraging qualified enterprises to raise funds through issuing bonds. Developing bond market has been the focus to attention in documents of the prior national working conference on finance and multiple working reports of the government. The recently published “Suggestions of the CPC Central Committee on Formulating the Twelfth Five-year Plan for National Economy and Social Development” clearly specifies that “to accelerate the development of multilevel capital market system, significantly increase the proportion of direct financing, and proactively develop the bond market.”

Since 2005, the People’s Bank of China has worked together with relevant departments and the financial industry to take a series of measures to promote the market-oriented development of the bond market, according to the uniform arrangement of the State Council. These include the following actions: firstly, to reduce administrative examination and approval, and improve the market-oriented mechanism for bond issuance; secondly, to focus on the OTC market which consists of institutional investors only in developing corporate bond market; thirdly, to establish and amplify the market-oriented restricting mechanism, and gradually improve the information disclosure system; fourthly, to establish credit rating system and risk sharing mechanism; fifthly, to improve the mechanism for protecting the legal rights and interests of investors, and strengthening investor education; moreover, to reinforce market self-regulatory management, and establish National Association of Financial Market Institutional Investors (NAFMII) to conduct self-regulatory management of the OTC bond market; furthermore, to make an effort to strengthen the development of settlement, trading, clearing and other market infrastructures; and lastly, to steadily promote the

market opening up process.

Driven by the industry and market participants, the Chinese bond market has taken a long stride since 2005. After five years of development, the market has grown bigger and bigger, and made great progress. Firstly, the market system is increasingly taking shape. It is featured by a market system that is composed mainly by the OTC market, and the exchange market serves as the supplementary part. These two parts coexist, completes each other, and interconnect with each other. Secondly, product varieties are increasingly enriched. Many new products, such as commercial papers, medium-term notes, SME collective notes, local government bond Central Huijin Investment Bond, start to emerge in responding to market demand. Thirdly, the market size has expanded rapidly. In the first ten months of this year, the bond issuance volume had amounted to RMB8.2 trillion, growing 25% year on year. By the end of October 2010, bond under custody hit RMB20.5 trillion, growing 21% year on year. In addition, the market size has catapulted to rank the second in Asia and the sixth in the world. Fourthly, the market entities have kept diversifying. Market issuers have expanded from government, large state-owned enterprises and financial institutions to private enterprises, Chinese-foreign joint ventures and foreign-funded enterprises. The market investors base now have covered banks, securities companies, mutual funds, insurance companies, credit cooperatives, enterprises and other institutions. Fifthly, the market infrastructures have been improved continuously. Laws and administrative regulations as well as relevant market rules and systems complement one another, and provide powerful institutional support to maintain market order and protect the rights and interests of all stakeholders. Finally, market operation mechanism has been continuously improved. Bond issuance administration has been optimized in succession, and some types of bond have already adopted registration system as issuance administration method which is a more market-oriented approach; the degree of market-oriented pricing is gradually increasing, which the market-oriented issuance and pricing mechanism has already taken shape for government bonds and financial bonds, and meanwhile the market-oriented issuance and pricing mode for credit bonds have preliminarily taken shape, and is being improved step by step; the market restriction and incentive mechanism is exerting its function gradually, and the binding force of information disclosure system on relevant stakeholders is continuously strengthening; and the credit risk management instruments are launched to provide market-oriented method to decentralize and transfer the risk.

III. Market self-regulatory organization has started playing an active role

In order to fulfill the requirement of shifting the market administration pattern and the practical need of the market development, market members initiated and founded NAFMII in September 2007. Since the foundation, the NAFMII, always upholding the principal of “self-regulation, innovation and service”, organized market members to tap the enthusiasm and creativity, and played an active role in accelerating the development of China’s debt capital market.

Based on the actual condition for market self-regulatory management, NAFMII established registration system for non-financial corporate debt financing vehicles in accordance with the principle of market orientation and professionalism. The practice and development of registration system have dramatically increased the efficiency of the direct debt financing of Chinese non-financial enterprises, and thus have expanded the market size at a fast pace. The NAFMII has fully stimulated the enthusiasm, initiative and creativity of market members, preliminarily fulfilled the transition from supervision dominance-oriented innovation to market dominance-oriented innovation, and made universal breakthroughs in product innovation, system innovation and organization innovation. In addition, the NAFMII has organized the market members to research and launch the SME collective notes, after launching medium-term notes and its rapid development. Moreover, in order to build the credit risk sharing mechanism, the NAFMII has convened the market participants to research and launch the credit risk mitigation agreement, after fully referring to the international experience. Furthermore, in order to strengthen the development of market infrastructures, the NAFMII has sponsored the establishment of a professional credit enhancement institution and a credit rating agency, after conducting thorough survey of the market demand. Last but not least, the NAFMII has started playing an effective and important role by actively carrying out self-regulatory management and facilitating its members.

IV. The Chinese bond market still has many gaps to fill

The Chinese bond market has realized the fruitful development in recent years. However, compared to the developed ones, the bond market has failed to play its fundamental role in resource allocation to a satisfactory extent, and remained unable to satisfy the need created by sustainable development of the Chinese economy. This is mainly evidenced by: (1) the lack of risk management instruments, the unsound market mechanism for risk sharing and the underdeveloped financial derivatives market; (2) market liquidity still need to be improved, market price still fails to reflect the true market supply and demand, and yield curve still need further perfection; (3) institutional investor types are concentrated, and serious homogeneity still exists; (4) the

public creditability of credit rating agency still needs to be enhanced; (5) legal and policy issues that hinder the market development still need solution, and adjustment in accounting standards, taxation and other associated systems are needed in order to meet the need of product innovation. In one word, compared to the matured financial markets, underdevelopment is still the biggest problem faced by the Chinese bond market.

V. Learn from the past experience and continue to develop the Chinese bonds market

It is imperative to build a Chinese bond market that is commensurate with the national economic development, adaptive to the market demand and competitive in the international arena.

First, continue to adhere to the direction of market-oriented reform, and strive to reduce unnecessary administrative control. At present, the major problem that hinders the rapid development of the Chinese debt capital market is the excess administrative involvement. Not only the bonds issuance is subject to administrative control, but also bonds investments of financial institutions are also regulated by various restrictive measures. The experience of many countries in developing the debt capital market shows that balancing the relationship between effective supervision and market-oriented development is the precondition to effectively promote the development of the financial market and prevent market risk.

Second, continue to uphold the development mode that is oriented to institutional investors oriented and OTC market oriented. The default risk of credit bonds is an objective reality. It can't be eliminated through administrative examination and approval or other means, but should be identified and borne in a market-oriented manner. Institutional investors possess professional teams, and have the ability to identify, bear and dispose of risks, which individual investors usually do not have and thus cannot identify risks due to their professional ability. Therefore, complex financial products are not suitable for individual investors, and what happened in other markets are worth careful study and research. As bond products are different in terms of credit risk and product structure, and involve large-scale single trade and diversified demand for trading, making them difficult to be standardized. As such, bonds trading are suitable for institutional investors only and to close the deal in the OTC market through quote-driven mode. Throughout bonds markets around the globe that the OTC market takes a remarkable proportion, and exceeds 90% in most cases.

Third, continue to strengthening market infrastructures. After the

outbreak of the international financial crisis, countries have rethought the cause of the crisis. The United States passed new financial supervision reform act this July. Different from inadequate financial infrastructures in the States, China's OTC debt capital market has had uniform central custodian system and centralized trading platform since its establishment. These infrastructures guarantee the transparent operation and risk controllability of China's OTC debt capital market. However, it is still necessitated to comb the management system for market custodians, and realize the integration and "seamless linkage" of trading, clearing and custodian systems. In addition, it is still needed to enhance the practice standards for underwriters, credit rating agencies, accountants, lawyers and other intermediaries, and materialize the convergence with the international standards.

Fourth, let market self-regulation play a bigger role. The experience of the international markets shows that strengthening self-regulatory management helps improve market supervision system. The functions of market self-regulatory organization are reflected in three dimensions: first of all, self-regulatory organization is closer to market demand, and can promote innovation continuously and effectively, which can avoid the disadvantages of the government's involvement in innovation – without sustainability and tendency to be distorted; secondly, self-regulatory organization can promote effective communication between government regulators and market participants; and third, self-regulatory organization can identify market risks at a very early stage as it is closer to the market and have close contact with market participants.

Fifth, continue to adhere to the principal of opening up to foreign investors. In recent years, the Chinese debt capital market has made great progress in the process of "inviting in" and "going out". China has successively allowed domestic institutions to issue USD-denominated bonds, permitted international development organizations to issue Renminbi bonds within the Chinese territory, empowered Asian Bond funds, qualified foreign institutional investors (QFIIs) and overseas Renminbi clearing banks to invest in the domestic bond market, and given the green light to the issuance of Renminbi bond by domestic enterprises and financial institutions in Hong Kong. The practice proves that the opening up of the debt capital market has played a positive role in accelerating market development, and created a bigger space.

Ladies and gentlemen, the development of Chinese debt capital market has been remarkable in the past. In future, it will embrace a vast prospect, shoulder a heavy mission and have a long way to go. We will join relevant authorities to continue driving financial reform, and actively support and

encourage market self-regulatory organization and market members to engage in exploration and innovation, striving to learn from international experience, gathering collective wisdom and keeping progressive to drive the sustainable and healthy development of the Chinese debt capital market.

Finally, I wish the Congress a great success! Thank you!

NOTE: This is the translation of the speech made by Governor Zhou Xiaochuan. Should there are any discrepancies between the Chinese and English versions, the Chinese version shall prevail.