

BEN 24 – China Credit Crunch

Discussion Questions

1. What do you think is the biggest problem with the banking system in your country?
2. How has your country's banking or financial situation been affected since the beginning of the economic crisis?
3. What changes do you think should be made to the global banking system?

Transcript

The global financial **spotlight** is **focused squarely on** China with its economy and banking system beginning to show signs of weakness. Interest rates **hit all-time highs**, while the **central bank stood by** and watched, as Reuters reports.

The People's Bank of China has **engineered** a tightening of cash in **money markets** after seeing interest rates **spike** to 25 percent or higher for some deals. This was done in order to try to **rein in** excessive credit growth, especially in the **lightly-regulated "shadow banking"** sector.

So what caused the People's Bank of China, or **PBOC**, to do this? During the first 10 days of June, Chinese banks increased lending by a **staggering** 1 Trillion Yuan - an amount the central bank said, "had never been seen in history." As Business Insider notes:

The PBOC evidently took the **lending spike** as a sign that banks expected easy credit policies to continue, so their response was to do the **hard opposite**: They allowed interest rates to spike, and basically gave the banks the **back of the hand**, letting them know that their **risky behavior** would not be **rewarded**.

A week later, the PBOC relented and injected cash into the system through open market operations with the goal of restarting interbank lending. After rates returned to normal, the central bank had some tough words for the financial system. From the New York Times:

The People's Bank of China let the world know that it was **putting** the nation's banks **on notice**: the **easy money** and the **speculation** it fed had to stop. The banks must **step up risk controls** and improve **cash management**.

The easy money in question comes from a shadow banking system **dominated** by lending to high-risk borrowers such as **entrepreneurs** and property developers. The biggest concern isn't the volume, but the *quality* of the loans and the banking system's ability to **absorb** potential losses, as the International Business Times explains:

Shadow banking can take many forms, including **loan sharks**, investment companies known as **trusts**, and **off-balance-sheet** lending by regular banks. The most important of the **latter** are "**wealth-management products**," which are considered potentially dangerous.

But the problem is not just limited to China's shadow banks, the big state-owned banks have also got their **fingers in the pie**. As the Economist points out, the central bank is losing patience with the **sleight of hand** that's become common practice:

No doubt the PBOC is also **frustrated** by the banks' balance-sheet **shenanigans**. Many banks sell **wealth-management products** to investors that **mature** just before the end of the **quarter**. The repayments are paid into the bank in time for **regulatory inspections**, only to disappear into a new product immediately afterwards.

The new Chinese government has called for a more **conservative approach** to financial markets. But as the People's Daily explains, so far the money hasn't always been going in the right direction:

Cutting down on shadow banking will also **resonate** with **Premier Li's** call for the financial sector to support the **real economy**. China's **total social financing surged** 50.2 percent to 9 trillion Yuan during the first five months, but much of the money **flowed** to property developers and **local governments** via the shadow banking system, leaving SMEs **starved** for cash.

With these kinds of effects on China's financial system, what lies ahead in the days to come? As Bloomberg suggests, it could be a **catch-22 situation**:

Any attempt to **bring** the credit boom **to heel** is going to slow investment growth and lead to **defaults**. Are they willing to accept businesses, or investment vehicles, or banks **failing**? We are soon going to find out.

The general **consensus** is that although this may be a **bitter pill to swallow** initially, **in the long run** everyone should be **better off**. As City Wire concludes:

They'll get it done, say investors. It is just a question of how quickly. 'This is a long-term **structural trend** they have **to see through**; it's both **in their interests** and the interests of the rest of the world'.

Vocabulary

Spotlight: Focus or point of attention; "The difficulty with being a celebrity is always being in the spotlight."

To be focused squarely on something: To look directly or exclusively at something; "The conversation during the meeting was focused squarely on how to cut costs."

To hit an all-time high: To reach a maximum point or record high; "Temperatures in California's Death Valley hit an all-time high of 134 °F (56.7 °C) on July 10, 1913"

Central bank: The entity responsible for overseeing the monetary system for a nation or group of nations.

To stand by: To remain uninvolved or refrain from acting; "After the explosion in Lac-Megantic, Quebec, the townspeople could do nothing but stand by and wait for the fire to be put out."

To engineer: Organized and implemented; "Samuel is engineering a new training program for more than 200 employees at the bank."

Money markets: A segment of the financial market in which financial instruments with high liquidity and very short maturities are traded. Participants use the money market as a means for borrowing and lending in the short term, from several days to just under a year.

To spike: a sudden, short-term change in the price of a stock that quickly returns to its previous price; "News of the ongoing conflict in the middle East caused oil prices to spike on Thursday."

To rein in: To reduce or bring under control; "We need to rein in our labor costs if we're to have any chance of making a profit this quarter."

Lightly-regulated: Few or no regulations; to allow to function without a strict adherence to the rules or regulations.

Shadow banks/shadow banking system: A network of financial institutions comprised of non-depository banks, e.g. private or unregulated banks, structured investment vehicles (SIVs), hedge funds, non-bank financial institutions and money market funds.

PBOC: The People's Bank of China; The Chinese central bank.

Staggering: Causing great astonishment, amazement, or dismay; "The tax rate in Italy is absolutely staggering; middle-class workers pay more than 50%!"

Hard opposite: Exact or direct opposite of something

To give someone the back of the hand: To reprimand, scold, or lecture.

Risky behavior: Investment and activities that contain a high level of potential loss.

To be rewarded: To receive compensation or praise for an action or result; "Tam was rewarded for her hard work with a new position and a big increase in her salary."

To relent: to change one's mind about a decided course, in particular a harsh/severe one; "After asking repeatedly for the new toys, Benjamin's father relented and bought them for him."

To inject: To put in, add, or inset; "Greg always tries to inject some humor into sensitive situations."

Open market operations: The buying and selling of government securities in the open market in order to expand or contract the amount of money in the banking system.

Interbank lending: A loan between banks to help finance operations.

Tough words: Difficult, yet very honest or true, feedback and advice; "After everyone failed the last math exam, our teacher had some very tough words for the whole class."

To put someone on notice: To be formally warned, cautioned, or advised; "We're have put foreign governments on notice that we want a change of trade policy."

Easy money: Money made with little effort, sometimes dishonestly, or money that can be borrowed at a low interest rate.

Speculation: Investment decisions based on the hope and expectation there will be a profit, but no firm evidence that this will be the case; "Speculation in the real estate market was one of the causes of the financial crisis."

To step up: Increase, improve, or enhance; "Before the Olympics, the local and national governments stepped up security in order to avoid any potential problems."

Risk control: The method by which firms evaluate potential losses and take action to reduce or eliminate such threats.

Cash management: The process of collecting, managing, and investing cash.

To dominate: To be the major factor or influence; "The lives of professional athletes are dominated by training, competition, and the desire to win."

Entrepreneur: A person who organizes and manages any enterprise, especially a business, usually with considerable initiative and risk.

To absorb: To take in, receive, or accept; "The shoes were designed to absorb the shock of hitting hard ground."

Loan shark: A person or group that offers loans at extremely high interest rates, often for illegal purposes such as gambling.

Trust: A relationship in which one party (trustor/agent), gives to a person or organization (trustee), the right to hold and invest assets or property on behalf of a third party (beneficiary).

Off-balance-sheet lending (OBS) : A form of financing in which large expenditures are kept off a company's balance sheet in order to help improve appearance of the overall financial state of the company.

Latter: The second of two persons or things mentioned; "Between a manager and a CEO, the latter is more senior."

Wealth management products: Investment opportunities, generally for very rich people, provided by financial institutions.

To have your fingers in the pie: To have a role or be involved in something; "Valentina wants to have a finger in the pie; she doesn't think we can do it by ourselves."

Sleight of hand: A way of deceiving people, also used during magic tricks; "Some mathematical sleight of hand was required to make the figures add up."

To be frustrated by: disappointed, discouraged, or upset; "Mario was frustrated by the lack of response to his request for a transfer."

Shenanigans: Secret or dishonest activity or maneuvering.

To mature: To become due for payment.

Quarter: 3 months of the year, often abbreviated "Q"; "Our Q3 numbers are 20% higher than last year!"

Regulatory inspection: An inspection performed by a regulatory body or group to ensure the bank is in compliance with guidelines and regulations.

Conservative approach: The tendency to be moderate or cautious.

To cut down: To stop, limit, or reduce; "By cutting down on air conditioning during the summer, we saved nearly \$500."

To resonate with: Appreciate or enjoy, cause or start an emotional reaction; "It was a movie that resonated with all different types of people; everyone absolutely loved it."

Premier: Political title, similar to Prime Minister or President (depending on the country and political structure).

Real economy: The part of a country's economy that produces goods and services, rather than financial services; "Some senior economists see deregulation and globalization as a threat to the nation's real economy."

Total social financing: Financial activities including loans of local and foreign currencies, trust loans, corporate bonds, equity financing, foreign direct investment and foreign debt.

To surge: A sudden large increase; "There has been a surge in housing prices recently."

To flow: To move continuously and unobstructed towards a destination in a manner similar to a liquid; "Orders for the new mobile phone flowed in to the office."

Local government: Government of the affairs of counties, towns, etc., by locally elected political bodies.

To be starved for: To have a strong desire or need for someone or something; "After being on vacation for a week, my cat was starved for attention."

Catch-22 situation: A frustrating situation in which one is trapped by contradictory regulations or conditions or where there are two equally undesirable alternatives.

To bring to heel: To force someone to obey you; "He decided that threatening to sue the publishers was the easiest way of bringing them to heel."

Default: The failure to live up to the terms of a contract. Generally used to indicate the inability of a borrower to pay the interest or principal on a debt when it is due.

To fail: To be unsuccessful or perform inadequately/poorly; "Despite their hard work, the sales team failed to reach their annual targets."

Consensus: An opinion or position reached by a group as a whole; "The consensus of the group was that the committee should meet twice a month."

Bitter pill to swallow: An unpleasant fact that has to be accepted.

In the long run: In the long-term.

To be better off: In a more satisfactory condition or situation; "I think you'd be better off if you bought a new car and didn't try to repair your old one."

Structural trend: Relating to the structure or organization of something.

To see something through: To continue doing something until it is finished, especially something unpleasant or difficult; "Having come this far, she was determined to see things through."

To be in someone's (best) interest: To someone's advantage or benefit; "It was in their best interest to move to a cheaper apartment outside of the city center."

Language Review

A. Collocations

Match the words in each column to make collocations from today's lesson.

1. Put	A. To heel	
2. In the	B. Regulated	
3. Cash	C. High	
4. Lightly	D. Approach	
5. General	E. On Notice	
6. Bring	F. Interests	
7. All-time	G. Consensus	
8. Conservative	H. Injection	

B. Review Quiz

1. According to the article, what is a cause of the credit crunch in China?
 - a. The banks are lending too much money to each other.
 - b. Off-balance sheet lending.
 - c. The central bank did not act to increase available funds.
 - d. The volume of shadow banking loans.
2. According to the article, why is the PBOC frustrated?
 - a. 1 Trillion Yuan increase in lending
 - b. Not enough speculation
 - c. Shadow banking is being cut down
 - d. Balance-sheet activities
3. In the sentence, "If offered a burger or a pizza, I'd choose the former." which one would be chosen?
 - a. Pizza
 - b. Burger
4. "You may be surprised to know that Bing Crosby's 'White Christmas' is the _____ best selling song."
 - a. Easy
 - b. Most
 - c. All-time
 - d. Catch-22

5. The _____ of wine and cheese can have a big influence on both the quality and the price.
- Mature
 - Maturing
 - Matured
 - Maturity
6. "Greg has really needs to _____ his performance if he wants to finish the project on time."
- Rein in
 - Stand by
 - Step up
 - Focus in
7. The CEO's _____ to move the bank in a new direction is what led to him being replaced.
- Reward
 - Failure
 - Frustration
 - Domination
8. Despite their difficulties in the labor market, Italy is one of the most _____ countries in the world.
- Entrepreneur
 - Entrepreneuring
 - Entrepreneurial
 - Entrepreneurship
9. "My boss will be _____ everything before the meeting, so let's make sure it's perfect."
- Inspecting
 - Inspected
 - Inspection
 - Inspector
10. "They're no _____ now than they were after he lost his job."
- Worst off
 - Best off
 - Worse off
 - Bad off

Answers

A. Collocations

1. Put	A. To heel	Put On notice
2. In the	B. Regulated	In the Interests
3. Cash	C. High	Cash Injection
4. Lightly	D. Approach	Lightly Regulated
5. General	E. On notice	General Consensus
6. Bring	F. Interests	Bring To heel
7. All-time	G. Consensus	All-time High
8. Conservative	H. Injection	Conservative Approach

B. Review Quiz

1. C; 2. D; 3. B; 4. C; 5. D; 6. C; 7. B; 8. C; 9. A; 10. C

Online Practice

Click the "Launch" button to open the **online practice:**

Launch Quiz