What are the Sources of Financing of the Chinese Firms?

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Summary

One big puzzle in China's rapid economic growth in the past three decades relates to the financial sector. On the one hand, the Chinese economy has experienced one of the fastest growth rates in the world continuously since the late 1970s, partly driven by the rapid development of the private sector, which outpaced the growth rate of the state sector. On the other hand, the vast majority of researchers believe that the formal financial sector in China lacks efficiency by many standards.

It appears to be common knowledge that external financing in China is mostly limited to state-owned firms and is hard to obtain for smaller private firms. In this paper we take a closer look at internal and external, formal and informal, financing sources of Chinese firms during the period of rapid economic reform in 1997-2006. To this end we analyze balance-sheet data from Chinese Industrial Surveys of Medium-sized and Large Firms for 2000-2006 and survey data from the Large-Scale Survey of Private Enterprises in China that was conducted in 1997, 2000, 2002, 2004, and 2006.

The following stylized facts emerge from our analysis: (1) State-owned firms continue to enjoy significantly more generous external finances than other types of Chinese firms; (2) Chinese private firms have resorted to various ways to overcome financial constraints, including increasingly more mature informal financial markets, cost-saving through lower inventory and other working capital requirements, and greater reliance on retained earnings; (3) There are substantial variations in financial access among private firms: While the small private firms face more financial constraints, the more established large private firms seem to have access to finances that are more equal to their SOE counterparts; and, (4) There is some evidence that financial access of small private firms, especially to formal bank loans, has improved moderately in the past decade.