Promoting Innovation and Cooperation to Create a Better Future for Asian Financial Markets in a Big Asset Management Age

Address at the workshop on the future of Asian financial markets focused on NPL markets

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Honorable Dr. Lohani, Distinguished guests, Ladies and Gentlemen,

Good morning!

It's a great honor to be invited by the ADB to participate in today's workshop on strengthening the future of Asian financial markets focused on NPL markets. I'd like to take this opportunity to discuss with you the operation and management of NPLs as well as the future of the financial markets in Asia. As the largest public AMC in China and the third chair of the International Public AMCs Forum (IPAF), China Huarong Asset Management Co., Ltd. is honored to co-organize today's workshop with the ADB. Here I'd like to extend my warm welcome to our guests and my sincere gratitude to the colleagues from the Economic Research and Regional Cooperation Department and the Finance Sector Group for their hard work in preparing for today's workshop. Meanwhile, on behalf of the 9,800 employees of China Huarong, I'd like to thank you for your support and help to our company over a long period of time.

My topic today is promoting innovation and cooperation to create a better future for Asian financial markets in a "Big Asset Management Age".

I. The outlook of economic and financial development and NPL markets in Asia

As a result of the economic globalization and international industrial transfer, Asia has become one of the most dynamic regions with great potential to grow. In recent years, more than 50% of the world economic growth has been generated by Asia, which has played an important role in the recovery of the global economy in a post-crisis world.

The recovery of the global economy is not without challenges and great divergences are being seen among different countries. The US economy has shown positive signs of stabilization and recovery. In 2014, the Fed quit the QE program and the US GDP increased by 2.4%, a rate that was higher than those of other developed countries. However, the Eurozone was still mired in stagnation with only 0.9% increase in its GDP. The recently-started QE program by the European Central Bank (ECB) was a measure by this region to stimulate its economy. The GDP growth rate of China in 2014 was 7.4%, slightly lower than the target rate of 7.5%. The People's Bank of China has recently loosened policies by cutting interest rates and required reserve ratios to ensure steady and healthy growth in 2015. Japan's economic growth is weak and the real GDP growth in 2014 is estimated to be negative, the first time since 2009. The estimated growth rate of India is more than 6% while the Philippines have already achieved such rate. And the growth rates of Indonesia, South Korea and Thailand are 5%, 3.3% and 1% respectively. So generally speaking, as a result of the uncertainty of the global economic development, the growth momentum of Asian countries is weakening and they are generally faced with downward pressure. And some Asian economies have been witnessing an increasing amount of debts since the Asian financial crisis.

According to Mckinsey & Company, the global amount of debts has increased from $ 57 trillion to nearly $ 200 trillion since 2007 while half of that increase has been generated by developing countries. Statistics by Morgan Stanley have also shown that the debts-to-GDP ratio of Asia increased from 144% to 205% from 2007 to 2014, a rise of more than 60%. On one hand, the Fed's exit from QE has created new expectation for higher interest rates, which results in the tightening of liquidity and higher borrowing cost for Asian countries. On the other hand, the depreciation of currencies in Asian countries because of a strong US dollar will create more pressure as these countries repay their debts. In fact, since the fourth quarter of 2014, currencies of China, Japan, Thailand, Indonesia, Malaysia and India have all depreciated against the US dollar.

In 2015, the total amount of NPLs in the Asian financial system will gradually increase because of the downward pressure, capital outflows, economic restructuring and risk exposure in some sectors that are going through industrial upgrading and transformation. Let’s take China’s NPL market as an example. In recent years, the accumulated risks are increasingly reflected on the quality of bank credits, resulting in a rising balance and ratio of NPLs. In the end of last year, the balance of NPLs in commercial banks (incorporated businesses) was RMB 842.6 billion and the NPL ratio was 1.25%, which had been rising for 13 consecutive quarters.

So it is appropriate to say that the rising amount of NPLs in Asia will create more opportunities for AMCs to provide assiting and counter-cyclical financial services to help enterprises in trouble. While on the other hand, a downward economy will definitely bring more pressure and challenges to the operation and innovation of AMCs.

II. Promoting innovation to drive transformation so that a policy-directed institute that focuses on NPL disposition can be transformed to a modern financial holding group that covers pro-cyclical and counter-cyclical market-based operations—taking China Huarong as an example

In the end of last century, Asian countries began to establish

AMCs to address the Asian financial crisis that started in 1997. In this context, the Chinese government established four public AMCs including China Huarong, China Cinda, China Orient and China Great Wall in 1999. From 1999 to 2006 (policy phase), the four public AMCs were responsible for disposing NPLs that amounted to RMB 1.4 trillion from the four major commercial banks in China (Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China and China Construction Bank). During this period, the four public AMCs were concentrating on professional disposition of NPLs, helping release the burden of SOEs, successfully managing problematic enterprises, addressing systemic financial risks, serving as economic stabilizers, “firewalls” against financial risks and “firefighters” for the financial crisis and making important contribution to China’s financial reform, economic security and social stability. Starting from 2006 (commercial transition phase), public AMCs in China began to do commercial acquisitions and equity investments and to provide entrusted services and financial consulting services by establishing subsidiaries focusing on securities, trust, financial leasing and other mandates.

Public AMCs in China have accelerated their commercial transition since 2009 and realized differentiated development following the principle of “one company, one strategy” proposed by the central government. China Huarong regards itself as a professional asset manager and first-class comprehensive financial service provider and develops a strategy of “three steps in five years”: first, fully adopting a market-based approach and implementing the “large client strategy”; second, promoting the strategic transformation toward a modern financial holding group that is market-based, diversified, comprehensive and internationalized; Third, achieving leap-forward development through the reform of sharing-holding system, introduction of strategic investors and IPO. Four transformative goals are also set: transformation from a policy-directed institute toward a market-based enterprise; transformation from a pure NPA manager toward a modern and comprehensive financial service provider; transformation from a non-listed company to a listed company; transformation from domestic mandates only to also including international mandates. With the strategy and goals, China Huarong is able to achieve rapid growth for six consecutive years and transform itself from a policy-directed NPA manager with limited resources, difficult operation and money-losing branches toward a large financial holding group with profits doubling year after year and the value of the state-owned assets constantly appreciating. China Huarong completed the reform of share-holding system in October 2012. In August 2014, the company successfully introduced seven more strategic investors including Warburg Pincus, CITIC Securities International, Khazanah Nasional Berhad, CICC, China National Cereals, Fosun and Goldman Sachs. Meanwhile, the Ministry of Finance, as one of the two initiators, maintained its controlling interest in China Huarong while China Life Insurance, as the other initiator, also increased its holdings. Currently we've started the preparation work for the IPO and will do all we can to become listed in Hong Kong this year.

At the end of 2014, China Huarong's assets exceeded RMB 600 billion and its net assets exceeded RMB 80 billion, making the company the largest AMC in China. The Fitch, Standard & Poor and Moody rated China Huarong as A, A- and A3 respectively with a stable outlook. Currently we've formed a strategic framework of "one body and two wings" that consists of the headquarters as the "body" and 31 branches and 14 subsidiaries that have licenses for financial and non-financial mandates (including Huarong Xiangjiang Bank, Huarong Securities, Huarong Trust, Huarong Leasing, Huarong Futures, Huarong Rongde AMC, Huarong Yufu Capital, Huarong Huitong AMC, Huarong Real Estate, Huarong Zhiyuan, Huarong Hong Kong, Huarong Qianhai Wealth Management, Huarong West Development and Investment and Huarong Tianze Investment) as the “wings” to provide comprehensive financial services that cover asset management, bank, securities, trust, leasing, PE, futures, investment and real estate to enterprises, governments and other clients in the market. And now China Huarong becomes a public AMC with the largest amount of assets, profits and return for shareholders, the most complete set of financial licenses, the highest degree of marketization, the strongest innovative ability and the greatest potential to grow.

So the four public AMCs in China including China Huarong have been actively promoting the construction of NPL market and self-transformation toward market-based institutes since their establishment in 1999. They have become a major force in cultivating China’s NPL market, exploring ways to cover a wide range of mandates and providing diversified financial services to adapt to pro- and counter-cyclical conditions. Currently the other three public AMCs in China are also transforming themselves to become financial holding groups.

III. "Five Thoughts" on Deepening the Regional Cooperation among Asian Public AMCs

As the amount of NPLs increases in the financial markets, the best solution, in our opinion, is "using time to create opportunities, investing more in distressed assets that are in stock and bringing those distressed assets back to life". In other words, our responsibility lies in providing assisting and counter-cyclical financial services to the society. As how Asian public AMCs deal with the fluctuation in the economic cycle and promote the adjustments and upgrading through addressing financial risks, I'd like to share five suggestions:

First, establishing an alliance mechanism among Asian public AMCs to strengthen their cooperation in the industry. As the Asia-Pacific integration progresses with the establishment of APEC, countries in the region are deepening the economic and financial cooperation as they effectively implement their regional interconnectivity plans. I propose that we establish an alliance mechanism among Asian public AMCs under the guidance of IPAF and the principle of “resource sharing, advantage complementation, mutual communication and cooperative development” to strengthen the exchange of industrial experience, to improve companies’ capacities and techniques in disposing NPLs and abilities of identifying, addressing, operating, preventing and controlling risks, to promote the competition and cooperation among Asian public AMCs and to establish an Asian NPL Disposition Fund as a way to explore the practice of cross-border NPL acquisition and restructuring and as a vehicle to effectively integrate financial resources, support the development of real economy, promote the industrial upgrading and prevent and address financial risks in Asia.

Second, grasping the opportunities in an increasingly larger Asian NPL markets to promote innovation in operating and management models and to provide assisting and counter-cyclical financial services. The operation and management of NPLs is where the strength of AMCs lies. Asian public AMCs should firmly grasp the opportunities created by increasingly larger NPL markets in Asia and utilize and innovate NPL operating models such as “stocks plus additions”, “acquisition plus disposition”, “acquisition plus restructuring” and “finance plus industry”, which combine traditional NPL disposition methods with debt and asset restructuring, mergers and acquisition, asset securitization and other measures. By establishing an NPA acquisition fund and utilizing innovative mandates such as NPA securitization involving private equity fund, AMCs are able to follow the path of “asset management – value appreciation – disposition and exit – profit realization”. Based on the features of NPA management in a counter-cyclical period, AMCs should adopt a strategy of acquiring NPLs in a downward economy, selecting those with growth potential as “stocks” and planning to sell them when the economy recovers. This is how AMCs can “use time to create opportunities” and obtain profits by operating risks.

Third, promoting the structural adjustment of industries and Asian economic transformation and upgrading by using NPA operation as a starting point. Currently Asian countries are under the pressure of economic restructuring: China has such an urgent need because industries with high level of energy consumption and pollution such as the mining industry and the manufacturing industry are now faced with problems caused by excessive production capacity. In addition, a turning point of the real estate market has also occurred and the industry may begin a long process of adjustment. Japan is promoting its structural reform by issuing bonds to increase governmental investment. South Korea is under greater pressure of adjusting its strategic and emerging industries. The economic growth of the Philippines and Indonesia mainly relies on exporting resources and is greatly impacted by the commodity prices. While in India, there is a great need for infrastructures and its industrial system also needs to be improved because of the imbalanced industrial structure. In such context, Asian public AMCs should address the assets, projects, enterprises and institutes that are in trouble by utilizing asset management methods such as debt acquisition and asset and equity restructuring. Asian public AMCs should also activate the social value of production factors and help idle and bad assets to generate profits again as a way for Asian public AMCs to offer solutions for the government, enterprises and creditors and to promote the industrial restructuring and economic transformation across the region.

Fourth, grasping the opportunities in a "Big Asset Management Age" to optimize measures of providing comprehensive financial services to Asian enterprises. With the emergence of financial innovation such as Internet and mobile finance, the financial industry is deviating from traditional mediums and moving toward a “Big Asset Management Age” in which the financial cake is being shared by entities such as bank, securities company, insurance company, trust company, PE firm, AMC and new financial medium. It is important for Asian public AMCs to grasp the opportunities in the accelerating integration of entities in the financial industry to better serve clients’ needs by offering financial products with underlying strategies such as “stocks plus additions”, “debt plus equity”, “acquisition plus operation”, “actual investment plus credit enhancement” and “own capital plus structural financing”. It is also important for AMCs to provide financial services that cover the life cycle of Asian enterprises and the whole financial industrial chain with a focus on NPA management as their main mandate.

Fifth, strengthening the exchanges and training of professionals is a guarantee for intellectual support to the sustainable development of Asian public AMCs. Talent lies at the core of global competition. Asian public AMCs should strengthen their communication and cooperation and establish mutual-visit programs to promote the exchanges among IPAF members. It is particularly important to strengthen the exchanges of professionals among IPAF members and improve the IPAF training system that may offer sessions on the legal framework, pricing and evaluation techniques and investment and M&A measures of NPA. It is also important to share information about techniques, product development and risk control measures of NPA operation and management among IPAF members. Today's workshop is a very good example of strengthening the communication among Asian public AMCs. In April, the IPAF will organize a training seminar on the operating model of asset management in Thailand. I think it is valuable and meaningful and China Huarong will actively participate in it.

Ladies and Gentlemen, Dear Friends!

Cooperation brings multiple wins. China Huarong is willing to cooperate with all stakeholders to achieve win-win situations in Asian NPL markets and make contribution to the region's financial stability and the welfare of Asian people!

Lastly, I'd like to invite the leaders, experts and our friends at the ADB to the third IPAF summit that will be held in Beijing in late October. As the current chair of IPAF, China Huarong will learn from the previous two chairs and devote every effort to ensure the success of the summit. Thank you very much!