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‘To Get Rich is Glorious!’

China’s Stock Markets in the ’80s and ’90s

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To
Our families and friends

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Preface

Much is written about the various efforts aimed at reforming China's state-owned enterprises. But in all this literature the Chinese government's determined effort to use the equity capital markets as a tool of enterprise reform has been virtually ignored. The fact is that during the past decade this has been, and will continue to be, the principal thrust with regard to the reform of state-owned enterprises. On-again, off-again noises about bankruptcy, M&A solutions, and asset management companies are only side shows in the process.

China's companies have been offering securities to investors, both domestic and foreign, since 1984 and have listed their shares on international stock exchanges since 1992. By late 1999 there were over 1000 companies which had successfully listed shares. All of this amounts to a Big Deal in the international (and domestic) financial community where most market knowledge resides. Even so, little of China's experience has been explored systematically in English (and not much more in Chinese). This book is aimed at filling the gap by approaching China's securities reforms from both historical and technical angles and tracking their development through the end of 1999.

We do not intend this to be a handbook and believe that even those with a casual interest in the country will learn much about how China operates. Seeing where China and its companies have come from and what problems they face now should provide the reader a feeling of where things are going in the longer run. The securities markets everywhere produce colorful characters and outrageous scandals and China has been no exception to this. Although one of us has been involved in China's securities industry since 1992 and has seen plenty of 'color', our intent here is to provide a systematic record of events, showing how things happen and drawing a few conclusions. The colorful book will have to come later. This book is also not about privatization in China since this is not what is happening. It is about what happened to the policy of state enterprise reform through corporatization. By corporatizing state enterprises, the government began with the simple aim of increasing their operating efficiency. But some of these enterprises proceeded to sell shares to the public raising badly needed funds in the process. This transformed the entire reform.

It is a bit difficult not to be jaded about all this given the official spin put on the reforms. As a senior official in the now defunct, but once all powerful, State Committee for Restructuring of the Economic Systems put it in 1989, 'The purpose of the share system is the share system and not to issue shares to the public.' This official was an idealist or was, perhaps, protesting too much. If people were willing to pay money for pieces of paper evidencing minority ownership in an overall minority ownership of an enterprise notionally owned by the 'State', why shouldn't the actual owners of the enterprise, the management, satisfy their demands? Of course, this is what happened with great rapidity and the genie of the market was out of the bottle.

But that is not all that has happened. It seems that international investors were equally, if not more, interested in participating in what by 1992 was becoming a China boom. Over the ensuing eight years Chinese companies, the government and, indeed, the entire economy have become dependent for capital on the whims of the international investor community. As the recent market craze for 'New Economy' hi-tech companies clearly illustrates, what is hot in the West suddenly becomes hot in China, driving the government and its policy process before it. And equally so, if the global markets are cold, no Chinese company will succeed in selling its shares, no matter how 'good' the government may think the deal is. Markets do not fit well inside of plans. The global securities markets are visibly setting the government's domestic agenda to a degree that is no less significant for having gone unremarked. Money knows no language barriers.

The international impact is not just a matter of money, it is also a matter of values. As major Chinese companies seek the support of international investors, they have been, at times, forcibly reminded that there may be strings attached. The huge international money managers have their own constituency, the groups and organizations which have entrusted funds for them to manage. And as, for example, the surprising riots in Seattle against the vision of the World Trade Organization suggest, the Chinese government, its companies and their Western sponsors can likewise ill afford to disregard the ideologies and ideals found in Western democracies. China may strive to continue as the Middle Kingdom, but what it is in the 'middle' of has changed and is continuing to change with a speed and a far reaching influence never seen before in world history. If, as the Chinese say 'History is a mirror', it is important to understand the origins and the subsequent development of this new force in China's economy. Doing

so, we believe, provides a clear insight into where China is going in the years ahead and provides the basis for a strengthened optimism.

Through the assistance of one of our colleagues, Mr Yang Changpo, we were given reason to satisfy our curiosity by developing a report on China's securities markets for the Asian Development Bank. Unfortunately, the report while only partially completed proved to be so interesting and information outside of China so completely lacking that we decided a full-blown overview might be welcomed. An on-line search for English materials on the Chinese stock markets revealed numerous statistical studies of Chinese stock volatilities and only a handful of patchwork commentaries. These we believed were either too sophisticated or too journalistic, lacking the basic overview that might be of more general interest. There was only one book, Yao Chengxi's excellent *Stock Market and Futures Market in the PRC*, which looks at these markets in 1995 from a lawyer's viewpoint. We felt that our view as market participants might also be of interest. Since one of us had been an investment banker in China since 1992 and had direct personal experience and the other an equity trader in Hong Kong, it seemed to us we had the right skill set to tackle the problem.

We apologize in advance if the chapters on Chinese shares are rather arcane, but then the variety of Chinese equities is exceedingly arcane to begin with, but important, nonetheless, to appreciate. These ingenious shares types are the means the government used to ring fence the market and inhibit outright privatization which seems to have been proceeding helter-skelter in Guangdong during the 1980s. The book is also not particularly accurate, although we have certainly tried to track down accurate market statistics and other information to the best of our ability. But when the Shenzhen exchange, Qianlong Data Systems and Wind Information Systems all widely disagree, what can you do? We have stuck with the exchanges in each case. We feel sure that the overall climate, trends and general details of China's unique experiment with stocks through the end of 1999 are accurately portrayed. We eagerly await, however, the books we hope will be written by some of the early shapers of China's stock markets who most assuredly have something to say. In the meantime, if this book stimulates interest, a variety of related Internet websites are provided in the Bibliography so that Chinese A share day traders in New York or even Edinburgh can keep on top of the action.

We would like to express our deep appreciation to CICC's Chief Executive Officer, Ms Elaine LaRoche, for her interest and support, to Mr Yang Changpo for sparking the idea, as well as to various other

colleagues at Morgan Stanley, CICC and elsewhere who steered us in the right direction from time to time. We also thank Vladimijr Attard who provided useful data on convertibles and Helen Hua Haiyue who proved the master of the Wind Information System from which we accumulated so much market data. To Professor Peter Nolan of The Judge Institute at Cambridge University we would like to express our heartfelt thanks for bringing the project to fruition. A portion of the royalties derived from this book will be donated to the Project Hope school now being sponsored by CICC and built in Hebei. Finally, we thank our families whose support and forbearance during the long evenings, weekends and holidays we worked on this project is so much appreciated and could not be done without.

We are quite certain we have made mistakes or errors of omission for which we alone are responsible. Our hope is that this work will prove useful to all those who are involved with China and provide at least the basis for the research and analysis many of our friends and colleagues will do over the next few years as China's securities markets become truly open to outside participation.

Beijing
January 2000

List of Abbreviations

CB	convertible bond
CGB	Chinese government bonds
CICC	China International Capital Corporation
CSRC	Chinese Securities Regulatory Commission
FMC	Fund Management Company
GDP	gross domestic product
IPO	initial public offering
JV	joint venture
M&A	mergers and acquisitions
MOF	Ministry of Finance
MOFERT	Ministry of Foreign Economic Relations and Trade
MOFTEC	Ministry of Foreign Trade and Economic Cooperation
NAV	net asset value
NETS	National Electronic Trading System
NYSE	New York Stock Exchange
OTC	over the counter trading
PBOC	People's Bank of China
P/E	price/earnings ratio
PRC	People's Republic of China
RMB	Renminbi
SAEC	State Administration for Exchange Control
SAMB	State Asset Management Bureau
SC	State Council
SCRES	State Committee for the Restructuring of the Economic Systems
SCSC	State Council Securities Committee
SEHK	Stock Exchange of Hong Kong
SLMB	State Land Management Bureau
SOE	state owned enterprise
SOET	State Council Office of Economics and Trade
SPC	State Planning Commission
SPCB	State Price Control Bureau
SSCCRC	Shanghai Securities Central Clearing and Registration Company
SSE	Shanghai Stock Exchange
SSSC	Shenzhen Securities Settlement Company

ST	special treatment (listed companies)
STAQ	Securities Trading Automated Quotations System
SZSE	Shenzhen Stock Exchange
TVE	Township and Village Enterprise
WTO	World Trade Organization