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Fiscal Stimulus, Deposit Competition, and the Rise of Shadow Banking: Evidence from China

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Abstract


The rise of shadow banking and attendant financial fragility in China can be traced to intensified deposit competition following the global financial crisis (GFC). A large, state-owned bank's deposits from cross-border money inflows fell significantly following the GFC, and it supported the government's fiscal stimulus more aggressively than other large banks by issuing larger volumes of new loans. Small and medium-sized banks with more branch-level overlaps with this large bank relied more on shadow banking, and issued more Wealth Management Products (WMPs)—short-maturity, off-balance-sheet substitutes for deposits. Greater amounts of WMPs created rollover risks for the issuers, as reflected by higher yields on new WMPs, higher borrowing rates in the interbank market, and lower stock-market performance during liquidity stress.

Keywords: Bank deposits, off-balance sheet liabilities, wealth management products, rollover risk, financial fragility

JEL Classification: G2, E4, L2

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