

# **Hidden Non-Performing Loans in China**

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## Loan Level Data from Local AMC

- Buys loans from banks with minimal discount
- Sells loans with small markup
- Buyers are mostly customers of bank
- Banks are “hiding” non-performing loans on balance sheet of their customers

# Questions

- Are these non-performing loans?
- If they are non-performing loans, then need to answer two questions

## 1) What do we want AMCs to do?

- AMC are effective when associated with shift from lax to stricter regulatory regime (and with bailout)
- But on a regular basis without regulatory change or a bailout?
  - ▶ Sale of NPL at market prices has no real effect on bank's owners
  - ▶ AMC have better technology to dispose NPLs?
  - ▶ Value of bank more transparent to outside investors?
  - ▶ Future investors don't want to share losses with current investors?

## 2) Who are the buyers?

## Who are the buyers?

- Hidden agreement for compensation by bank?
  - ▶ Other loans will be forgiven in future?
- No hidden agreement, buyers get access to (normal) cheap loans
  - ▶ Banks use rents implicit in subsidized loans to compensate buyers
  - ▶ Is normal subsidy enough?
  - ▶ Allocation of rents from subsidized loans changes
    - ★ Rents of firms with access to loans taxed to pay for NPL
    - ★ Bribes of bank officials taxed to pay for NPL
  - ▶ Bottom line: NPL are off the bank's balance sheet
- Firms with the same owners as the bank
  - ▶ Putting aside tunnelling, NPL are off the bank's balance sheet.
  - ▶ If there is tunnelling, bigger issues to worry about for future investors
- Buyers forced by local government to buy bad debt
  - ▶ This is like a bailout, with bailout funded by firm-specific taxes