

РОЗДІЛ 4

Наукові повідомлення

Research of Development in Internet-Based Finance in China

Tu YUXIAⁱ, HAO SUINIANⁱⁱ

There is a definite lack of financial resources in China for small and medium enterprises (SME) and they face continues problem of availability of financial services. Therefore paper underlines importance of Internet finance development in China to address the problem of SME financing, promoting the transparency and safety of informal financing. Taking deposits and issuing loans is now not confined only to banks in China. Internet giants such as “Alibaba”, “Baidu”, “Tencent” are the new players in the financial market of the country. Internet finance highly reduces transaction costs and improves resource allocation efficiency. Compared with indirect financing Internet finance have several specific features, including the use of social networks to generate and spread information, the use of search engines to structure and sequence information and the use of cloud computation to ensure rapid processing capabilities for mass information. Web Banking is an attempt to create a new mechanism for lending and among functions of the new financial institution are service deposits, issue of bonds, loans, design calculations, currency exchange, and issuance of bank cards.

Keywords: Internet finance, e-commerce, Internet banking, online payment, China.

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Introduction. Internet based companies which were specialized in e-commerce businesses, online web portals, data-centric cloud computing services are starting to open new directions of business becoming financial intermediaries. Usually in theory there are two types of financial intermediaries: 1) commercial banks and security markets. They play an important role in resource allocation and promote economic growth, but also incur huge costs. The origin of Chinese Internet banking dates back to online stores. The rapid development of e-commerce in China, as well as the factor of high population density in the country creates good conditions for logistics. This is unlike the Western countries, where the predominant small population living dispersed and there is no possibility to create a large-scale efficiency, resulting in high cost of logistics. That is the main reason for Chinese rapid development of e-commerce. When the development of e-commerce has reached a certain extent, it led to a concentration of a large number of small and micro-enterprises and entrepreneurs, the last is accompanied by huge financial needs. It is the existence and expansion of these needs contributed to the birth of the Chinese sphere of Internet finance.

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Comparison of traditional and Internet finance in China

There is a significant difference between traditional finance and Internet finance, the first one provide services such as financing, payment and settlement through commercial banks, the second one do provide digital financial services based on Internet platforms, flat service model and minimized cost of interaction. According to Xie Ping and Zou Chuanwei (2013) within interment finance the markets become much more efficient and resemble the world without financial intermediaries described by general equilibrium theory. Additionally, Internet finance would highly reduce transaction costs and improve resource allocation efficiency.

Compared with indirect financing through commercial banks and direct financing through security markets Internet finance have several specific features: 1) Internet finance use social networks to generate and spread information (especially information without disclosure obligations; 2) Internet finance use available search engines to structure and sequence information and alleviate problem of overload 3) Internet finance use cloud computation to ensure rapid processing capabilities for mass information. The use of cloud computation (as stated in Xie Ping, Zou Chuanwei (2013), would reveal, concentrate and standardize dynamic information though social networks about capital suppliers and demanders, therefore risk assessment would be performed at extremely low costs.

Interment finance according to Claessens et.al (2000) offer wide opportunities like widening access and improving financial services, emerging new markets, modernizing and strengthening national legal systems, and improving technology-related infrastructure. Combining Internet and financial sector practices according to Liu et. al, (2014) creates a new synergy of customers statistics, data mining, interactive and user feedback, social media and other ways to provide personalized services to meet customer needs and enhance the competitiveness of enterprises. In general, Internet finance is multiple category, which includes: Internet banking, third-party payment, P2P lending, Internet insurance, crowd funding, big data analysis (fig. 1).

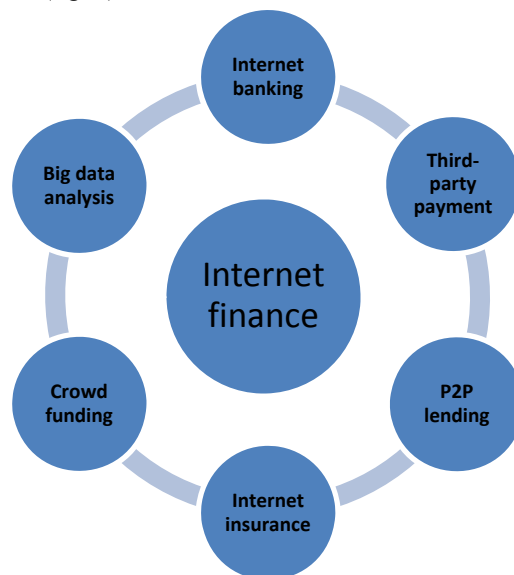


Figure 1. Basic concept of Internet finance*
Adapted from KPMG Huazhen (2014)

Over the past ten years, Internet-based platforms in world started to allow individuals to lend money to each other. This has become known as person-to-person or peer-to-peer lending (P2P lending), this allows people to bypass traditional banks to borrow or lend. P2P platforms offer lenders the potential to earn relatively high returns (compared with deposits) and a wide choice of borrowers with different levels of credit risk. Definitely there exists a certain risk that lenders could lose their principal and interests on investments.

There are two major types of P2P companies: first type serves as a financial platform (not taking any liabilities in the case of a loan default, making a profit by charging a service fee); the second type P2P company bears partial or full responsibility for credit risks taking advantage of the spread between the return from loans and return paid to the investors. Also, some P2P platforms in China offer guarantees on P2P loans by a third party or itself to attract investors.

According to Leon Qi et al, 2014, among various Internet finance services, online-payment services do have very good positions to compete with traditional banks. The last is explained by the fact that this area requires wide expertise in terms of financial risk management and has the lowest connectivity with other financial services.

Empirical evidence of Internet finance development in China. Taking deposits and issuing loans is now not confined only to banks in China. Internet giants such as «Alibaba», «Baidu», «Tencent» and even sells electronics «Suning» are the new players in the financial market of the country. Internet companies have pretty good developed on-line products and able to propose investment services which are easy and fast, moreover financial products are being accessible not only to the elite, but common people in China are more and more using it. As for the commercial banks they see new competitors as a serious threat. For example, «Alibaba» offered to anyone who wants to invest in financial market products online an annual profit in four and a half percent, while bank deposits to earn less-half of the year. As a result, just two weeks after the launch of an online platform, «Alibaba» two and a half million people are donated to a little less than six billion yuan. Billion yuan was able to earn the first day of opening their own fund company «Baidu». The exponential growth and attractive returns offered by Yuebao (money market fund operated through Alibaba) has drawn significant market attention and led to investor concerns about the stability of banks' deposit funding.

According to Leon Qi et al, 2014, among the all Internet players in China it is Tencent that has a strong competitive advantage in the Internet finance field. The last is achieved through its leading position in China's Internet industry and strong mobile platform. Internet financial products and services offered by Tencent are directed to improve its user traffic giving opportunity to its users to purchase financial products online, educating those users to use Tencent's payment service, which paves the way for further development of its payment-related business.

New financial products of Internet companies in China enable consumers to buy as money market funds, payment service provided by Tencent. Many Internet companies have launched investment products in 2014, however according to Leon Qi et al, 2014 it is considered that only Yuebao and Licaitong (Alibabas products) are potential competitors to the banks. The main problem for the small Internet companies to be successful in financial sphere is huge requirements on large retail-customer base and residual funds in accounts. On the contrary, Alibabas products have several advantages: 1) a large number of accounts with real identity information, and 2) residual funds in accounts due to e-commerce activity. While, Tencent products are supported by huge clients base as well as e-commerce partners on its powerful social platform, WeChat.

According to KPMG Huazhen (2014) there is a significant difference in advantages of Internet and traditional finance. Thus Internet finance proposes low rates when buying online usual bank purchase rate for buying funds is 1.5 percent, but it is 0.6 percent for Internet firm. The second advantage of Internet finance is low threshold (RMB 1 vs RMB 50,000 for traditional banks) also the third advantage of Internet finance is short-term periods starting from even one-day periods vs. traditional wealth management plans not less than 1 month.

Also the traditional banking institutions have convention channels, high security and relatively low risks. Thus investors can buy more diverse types of funds with professional wealth management plans and advice.

BAT (Baidu, Alibaba and Tencent) are acronym for the three giants of the Chinese Internet. More than 10 years ago, «Baidu» offered services only as a search engine, «Tencent» was offering only QQ, and «Alibaba» was offering an e-commerce. Currently, three companies have formed a complex structure of comprehensive services.

During the 2010-2014 three Internet giants were constantly increasing its sphere of influence and created on their language «ecosystems». Currently BAT through investing of huge amounts of capitals has created fierce competition in areas such as culture, catering, transport, payment, entertainment, finance to build their economic empires.

Chinese technology giant Tencent Holdings Ltd and Alibaba Group Holding Ltd for the first time bypassed state-owned companies and became the most expensive brands of China in the begging of 2015. The three largest Internet companies in China, including Baidu Inc., are in the top 5 list of most expensive brands of China. Annual ranking is based on the income from the brand and the response to its customers, takes into account only public companies. Tencent brand was valued at \$66 billion, rising over the year by 95 percent. Chinese giant social media is valuated more than Facebook Inc. and is the fifth biggest global technology brand after Apple, Google, International Business Machines and Microsoft. The total value of the top 100 Chinese brands for the year grew by a record 59 percent to \$464 billion, surpassing the growth rate of the top 100 global brands

According to China Internet Watch (2015) Alibaba group was started in 1999 when Jack Ma founded the website Alibaba.com, a B2B portal to connect Chinese manufacturers with overseas buyers. In 2012, two of Alibaba's portals handled 1.1 trillion yuan (\$170 billion) in sales. Alibaba Group Holding, the largest company in the field of e-commerce in China, which also intends to end of 2015 to open a bank. Banking activities would be operated with Ant Financial Services Group, the financial branch of Alibaba. The total revenue of Alibaba Group Holding reached \$8.4 billion, and profit –\$3.74 billion in 2014. Earlier it was reported that at the end of July-September 2014, the income of Alibaba, which also owns Taobao and Tmall, amounted to 16.829 billion yuan. This is 53.7% more than in July-September 2013 net profit exceeded 6.8 billion yuan (\$1.1 billion). By the end of September 2014 on the website Taobao and Tmall visited by 307 million customers. This is 52% more than the year before. Alipay is a branch of Alibaba Group, and number one China Internet payment service provider started in 2004, which dominates the sector with almost 50 percent of the market share, having around 300m users. The Alipay products online payment, mobile supports Android, iOS and Windows and Yuebao. According to iResearch among most frequently used usage scenarios of mobile payment in China are online shopping, transfer of account, payment for local life services etc. (Fig. 2).

Governmental regulation of Internet finance and microcredit companies development. There is no clear legislative regulation in the field of web finance and web banking in China and officials are just beginning to develop specific legislation for the

financial market online. Internet companies that took advantage of this opportunity started a new game and Chinese government has good reason not to interfere with this new players. The country's authorities understand the importance of providing loans to private companies. Traditional financial institutions are unable to fully meet the credit crunch.

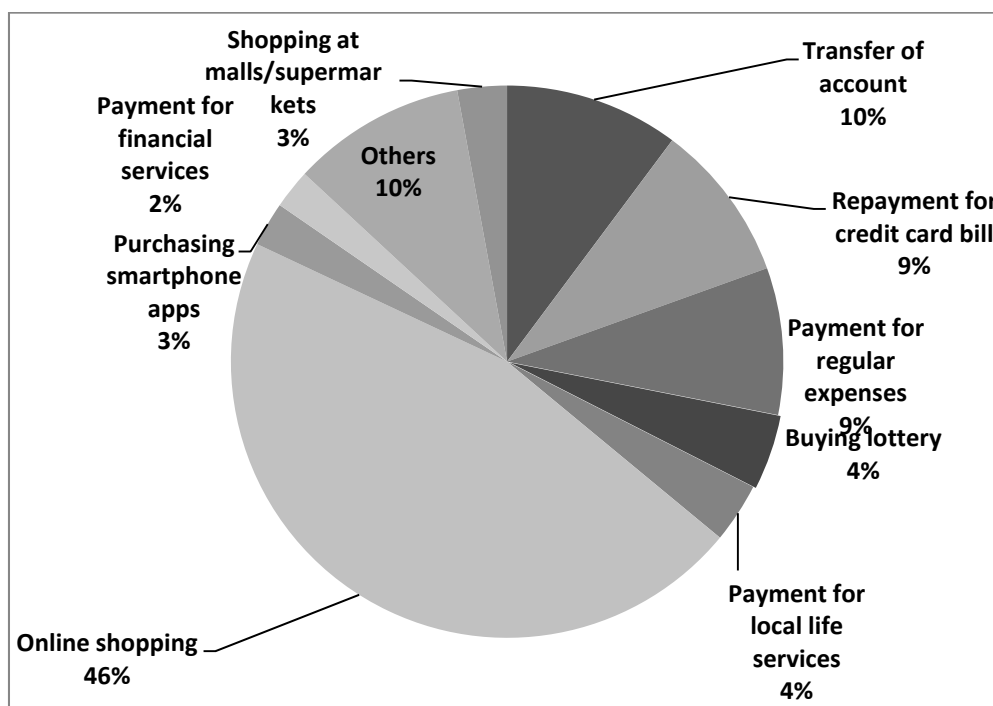


Figure 2. Most frequently used usage scenarios of mobile payment in 2013*

*Based on information of iResearch Consulting Group, 2014

The new trend attracts a lot of attention especially on the eve of the plenum of the Central Committee of the CPC. The government's decision should determine the future of not only online financing, but in general the private sector in China, as well as to show the scale of the forthcoming economic reform. However, incredible energy that Internet companies are moving into the financial sector despite the risks is a sign that the liberalization of China's financial market is inevitable. Web Banking is an attempt to create a new mechanism for lending. The main customers of web banking are individuals and small businesses. To the functions of the new financial institution belong service deposits, issue of bonds and other securities, loans, design calculations, currency exchange, issuance of bank cards. Thus, one of the founders WeBank is the largest Internet company Tencent Holdings Ltd. The purpose of the WeBank is lending to the consumer sector and small businesses. The specific feature of the bank is work only via the Internet, using face recognition technology and credit history of potential borrowers. The Bank operates exclusively via the Internet, using face recognition technology and credit history of the borrower. WeBank is taking into account the credit history and information about its clients from social networks and various services of Chinese Internet giant Tencent. According to a representative of the bank, at the disposal of

WeBankare 40 trillion informational messages from the Internet, so bank customers do not need to provide additional guarantees its reliability. The new era in development of banking sectors allows financial institutions to process and record statistical data on its clients including: residence time of the user online, media and social network activity, the presence or absence of the Internet property, the chain links to other potential borrowers, photos and other avatars, etc.

The reason that Chinese Internet banking are developing so fast (in addition to technical factors in the form of a networks), has also a socio-economic nature of poor development of China's financial sector. Thus, the channels of funds accumulation are rare and small and micro enterprises are experiencing some difficulties of financing. Internet banking to some extent changed this situation facing small and micro enterprises, displaying three major trends. The first major trend is that mobile payments at Internet banking were replaced by traditional forms of payment, the second trend is the peer microfinance Internet banking, which would replace the traditional deposits and loans, and the third trend is that crowdfunding Internet banking services will replace traditional securities.

Also there is a governmental support for development of Internet banks, and Chinese authorities intend temporarily allow the Internet banks not to create reserves for certain categories of deposits. In order to stop weakening economic growth of China in 2015 the Chinese authorities are using measures to support lending and commercial banks are able not to create reserves for deposits made by non-bank financial institutions. Chinese Central Bank through this step tries to avoid the need for direct reduction of reserve requirements of banks, fearing that it would be too strong signal to mitigate its policy, which can cause instability in the stock market.

There are two specific features of Chinese electronic commerce. First of all, near 90% of electronic retail business comes on the virtual markets sponsored due to an advertisement. These platforms that remind eBay and Amazon Marketplace different producers, salespeople and private persons offer goods and services to the consumers through shop windows. The situation in US, Europe and Japan is different and approximately 70% of e-commerce is performed through online shops located on the own web sites. Normally in most countries the sector of retail business is developed in three stages: local and regional players prevail at first stage, later the initiative is intercepted by the less number of national companies, and finally online shops affront to traditional business. The history of micro-credit companies dates back to 2005 when China launched the experiment and ten micro-credit companies were created, the current number of microcredit companies soared to 9,000. According to statistics from the People's Bank of China, by the end of 2014, China had 8791 company providing microcredit, the outstanding balance on the credit score was 942 billion yuan. The average registered capital of microcredit companies does not reach 100 million yuan, the number of employees on average 12 people, the amount of loans to individual farms is up to several hundred thousand yuan. The rapid development of micro-credit companies, in which the key word is «micro», played an important role in resolving the financial difficulties of Chinese small and medium enterprises, as well as in solving the problems of increasing income of farms.

Currently microcredit companies are uniting in different associations. Thus, association of micro credit companies of China was formally established at the begging of 2015. This Association was established with the approval of the China Council for the Control and Management of the banking industry, the People's Bank of China and with the permission of the Ministry of Civil Affairs. It is the national industry-autonomous organization, formed at the request of microcredit agencies and local self-regulatory organizations. Microcredit companies being focused on micro and small enterprises, individuals and low-income farmers are rapidly growing in China during the last years. It is considered that microcredit is an

important part of the financial activities and plays a significant role in the economic development of the regions. During the last years financial companies are currently experiencing a period of microcredit Wild Growth and objective phenomena such as large sums of microcredit and rejection in certain regions of microcredit companies lead to disordered development of this sphere, threatening to shareholders and orderly financial system possible overflow.

Conclusions. There are considerable amounts of private capital which is experiencing an acute need for more effective methods and channels of investment. The marketization of interest rates and launch other reforms will contribute to the development of Internet finance. Definitely development of Internet finance in China is a gradual process of related areas development, such as on-line payments, finance, banking, investment, insurance, etc. All of this would gradually bring some changes lead to Internet banking to maturity.

For the current state, financial products do not provide large contribution to the profits of the Internet companies. It is rather improves user traffic, stickiness to existing services and extend businesses into the finance industry. There is a definite lack of financial resources in China for SME and they face continues problem of availability of financial services. Therefore one of the most important features of Internet finance for Chinese government is opportunity to address the problem of SME financing, promoting the transparency and safety of informal financing.

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Исследование развития интернет-финансов в Китае

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Существует определённая нехватка финансовых ресурсов в Китае для малых и средних предприятий (МСП) и они продолжают сталкиваться с проблемой доступности к финансовым услугам. Поэтому в данной статье подчеркнута важность развития Интернет-финансов в Китае для решения проблемы финансирования малого и среднего бизнеса, содействие прозрачности и безопасности неформального финансирования. Принятие вкладов и выдача кредитов в настоящее время не ограничивается только банками в Китае. Интернет-гиганты, такие как "Alibaba", "Baidu", "Tencent" являются новыми игроками на финансовом рынке страны. Интернет-финансы существенно снижают транзакционные издержки и повышают эффективность распределения ресурсов. По сравнению с косвенным финансированием интернет-финансирование имеет ряд особенностей, в том числе использование социальных сетей для создания и распространения информации, использование поисковых систем для структурирования и упорядочивания информации и использование облачных технологий для обеспечения быстрой возможности обработки массовой информации. Веб-Банкинг – это попытка создать новый механизм для кредитования и среди функций новой финансовой структуры – служебные депозиты, выпуск облигаций, займов, проектные расчёты, обмен валюты, выдача банковских карт.

Ключевые слова: Интернет-финансы, электронная коммерция, интернет-банкинг, онлайн-платёж, Китай.

Дослідження розвитку інтернет-фінансів в Китаї

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Існує певна нестача фінансових ресурсів у Китаї для малих і середніх підприємств (МСП) і вони продовжують стикатися з проблемою доступності до фінансових послуг. Тому в даній статті підкреслена важливість розвитку Інтернет-фінансів в Китаї для вирішення проблеми фінансування малого та середнього бізнесу, сприяння прозорості та безпеці неформального фінансування. Приймання вкладів та видача кредитів в даний час не обмежується тільки банками в Китаї. Інтернет-гіганти, такі як "Alibaba", "Baidu", "Tencent" є новими гравцями на фінансовому ринку країни. Інтернет-фінанси істотно знижують транзакційні витрати і підвищують ефективність розподілу ресурсів. У порівнянні з непрямим фінансуванням інтернет-фінансування має ряд особливостей, в тому числі використання соціальних мереж для створення та розповсюдження інформації, використання пошукових систем для структуривання та впорядкування інформації та використання хмарних технологій для забезпечення швидкої можливості обробки масової інформації. Веб-Банкінг – це спроба створити новий механізм для кредитування і серед функцій нової фінансової структури – службові депозити, випуск облігацій, позик, проектні розрахунки, обмін валюты, видача банківських карт.

Ключові слова: Інтернет-фінанси, електронна комерція, інтернет-банкінг, онлайн-платіж, Китай.