China towards a healthy capital market

– A China Business Centre Public Lecture by Professor Oliver Li, January 28, 2016, in Suzhou, China

NUS Business School China Business Centre (CBC) conducted its fourth public lecture by Professor Oliver Li, Director of the centre, on 28th January 2016, at the Jinji Lake Grand Hotel in Suzhou China. This lecture was jointly hosted by NUS and the Financial Affairs Office of the Suzhou Municipal Government, and organized by the China Business Centre and the NUS Research Institute (NUSRI) in Suzhou, with support from Agricultural Bank of China Suzhou Branch and Soochow Securities.

CBC Director Prof. Oliver Li in his presentation

Prof. Li in his presentation

Prof. Li highlighted that economic policies uncertainties and investor irrationality contribute to the meltdown of China's A-share market. Economic uncertainties lead to stock price synchronicity and large overall volatility. Emotional factors easily affect individual investors' behaviors, leading to irrational decisions. Both regulators and investors are responsible for this unpleasant market adjustment.

The Q&A session

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While many criticisms point to a significant increase in leverage and shorting selling in securities trading in recent years, Prof. Li believed that leverage is unlikely to cause the meltdown, due to its relatively limited size while a sound short selling mechanism can in fact serve as a buffer to stabilize the market by increasing liquidity and reducing volatility.

Prof. Li expressed concerns over certain trading mechanisms that can potentially exacerbate market volatility. For example, price limitation can artificially disrupt an equilibrium between supply and demand, causing investor panic.

Interacting with the audiences

Panelist interacting with the audiences

Prof. Li also argued that a structural problem within the Chinese investors and their short-sighted investment behaviors can be another underlying cause for the market crash. 80% of China's stock market trading volume comes from individual investors who are less sophisticated compared with institutional investors. An analysis on individual investors' trading behaviors shows that individual investors underperform the market and that the more they trade, the more they communicate with each other and share information, the worse is their performance.

NUSRI director Prof. Xu Guoqin delivering closing remarks

Prof. Xu and Prof. Susanna Leong presenting gifts of appreciation

Looking forward, Prof. Li is optimistic given the phenomenal economic growth the country has achieved in the past and the upward development trajectory. An optimization of the trading system and the education of individual investors are necessary. At the macroeconomic level, the government can direct investments through industrial policies. A carefully designed taxation system on capital gains can also be deployed to encourage longer stock holding to reduce volatility.

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