Proceedings of the 7th International Conference on Economic Management and Green Development
DOI: 10.54254/2754-1169/39/20231955

Analysis of the Chinese Trust Industry

Wangzi Gao[1,a,*,†], Zhenyi Lu[2,b,†], Leyang Zhang[3,c,†], Zilin Zhang[4,d,†], Xucheng Luo[5,e,†]

[1]College of Letters and Science, University of California, Los Angeles, 90024, USA
[2]Faculty of Business and Economy, The University of Hong Kong, Hong Kong, China
[3]Living World Shanghai, 201107, Shanghai, China
[4]Faculty of Business and Economy, University of Melbourne, 3010, Melbourne, Australia
[5]Waikato Union College, Zhejiang University City College, 310015, China
a. solomon0308@g.ucla.edu, b. yulialzy@hotmail.com, c. joanna0920@hotmail.com, d. zhangzilin606@gmail.com, e. 32011060@stu.zucc.edu.cn
**corresponding author*
[†]All authors contributed equally to this work.

Abstract: China's financial market is one of the largest in the world. The trust industry makes up a great proportion of that market. Analyzing the Chinese industry with examples of top trust companies will improve our understanding of the market. We analyze the entire Chinese trust industry by presenting the case of specific trust companies. The paper contains a definition of the trust industry and products, a comparison of the Chinese trust industry with the American trust industry, an analysis of trust products in China, an analysis of risks of the Chinese trust industry, a comparison of the trust industry with other financial industries in China, and description of Chinese government's policies on the trust industry.

Keywords: trust fund, trust product, China, government policies

1. Introduction

The trust industry is a crucial part of the financial market. According to *The Trust Law of the People's Republic of China*, trust refers to the process of a trustor giving his property rights to his trustee and allows the trustee to dispose of the property in the interest of the beneficiary [1]. In other words, a trusted company manages their customers' properties to earn profit for the customers.

Based on that, trust products refer to all types of financial services in the trust industry with low investment risk and stable returns. A large part of Chinese trust products belongs to the category of loan trust. A loan trust product transfers trust funds into loans to other companies. In China, such loans are often lent to construction companies. Besides, other trust products include equity trust products, financial leasing trusts, and real estate trusts. Unlike the loan trust, they take up less part of the Chinese trust industry. Due to the various features of the Chinese trust fund industry, studying and analyzing the market can help understand the market's current situation and hence predict the future development of the general industry.

In the work, we analyze the Chinese trust industry by comparing it to the same industry in other Western developed countries, analyzing trust products in detail, listing data and governmental policies regarding the industry to predict the future development of the market, and eventually reach a conclusion of the analysis of the industry.

DOI: 10.54254/2754-1169/39/20231955

2. Comparison of Chinese Trust Industry to American Trust Industry

Trust industry was created hundreds of years ago in the west and it has reached its maturity as a financial sector in America. The American trust industry mainly aims to achieve the management of risks, taxation, and the inheritance of wealth by entrusting individual's property rights to the trust companies [2]. As the American trust industry plays a pivotal role in the national financial system, most trust companies in America help their customers to pass their wealth to their offspring without having to follow the state's probate process.

In contrast, over the past forty years of development in the trust industry, China has created its unique trust system. Most Chinese trust companies were established in the 1980s by the government and banks. As a result, the trust industry gradually becomes a method of avoiding bank regulation and gathering funding to make loans. Unlike the American trust industry, the Chinese trust industry focuses less on the purpose of trust of passing wealth through generations and uses more of the trust funds as loans to local construction companies to boost city construction. According to the Chinese Trustee Association, around 16% of the trust funds of the trust industry were used for the basic construction industry in 2019.

One important reason the American trust industry has such a different role from the trust industry in China is that most Chinese trust companies are state-owned, meaning they are closely regulated by the Chinese government and a large percentage of the profit belongs to the local governments. Trust product for local construction often has better returns than other types and hence most trust companies focus primarily on such service.

3. Analysis

3.1. Analysis of Trust Products in China

Chinese trust products are divided into three general categories: fixed-income trust products, securities investment trust products, and equity investment trust products.

There are generally no subscription fees and fixed management fees for fixed-income trust products for ordinary investors. The relevant management fees for this type of trust product are usually paid to the financier and borne by the trust property, and investors usually do not need to pay this part of the fee. Since the actual income of a fixed-income trust may exceed the expected income during the operation, some trust companies will require the excess part as a floating management fee. This part of the floating management fee does not affect the expected income of investors.

A securities investment trust is a pooling of investment funds from individuals, corporations, and groups, and a trust company makes securities investments on behalf of investors. The trust company eventually returns the investment proceeds and principal to the beneficiary and charges a fee to the investor in the process.

The relevant fees for securities trust wealth management products mainly include:

1. Fixed management fee - charged by the trust company, the rate is about 1%-1.5% of the net value.
2. Floating management fee - charged by the investment advisor, the rate is generally 20% of the profit.
3. Subscription fee - usually about 1% of the subscription capital.
4. Redemption fee – usually, a high redemption fee will be charged for redemption during the closed period, and it will be waived if it exceeds.
5. Custody fee - charged by the custodian bank, the rate is generally about 0.25% of the net value.

DOI: 10.54254/2754-1169/39/20231955

6. Others - including information disclosure fees, intermediary fees for trust affairs, liquidation fees when the trust is terminated, transaction fees for securities and other investment products, stamp duty, other related taxes and fees incurred during the management, use and disposal of trust properties.

These fees are very expensive and far exceed the international average.

For equity trust, In China, equity trusts are targeting at high-net-worth individuals, and their selling price starts at RMB 3 million. Management fees for equity trust products are usually calculated as a percentage of total assets under management (AUM). Specifically, the exact fee structure may vary between trust companies and specific products, but is generally based on a tiered scale whereby larger AUMs may attract lower fee rates. Generally speaking, the management fee of China's equity trust products is between 0.5% and 2% per year, and the average fee is around 1% to 1.5%. Management fees for equity trust products are regulated by the China Securities Regulatory Commission (CSRC) and other relevant authorities. The regulator aims to ensure transparency, fairness and investor protection of fee structures and disclosure practices. Trust companies that offer equity trust products in China are required to disclose basic information to investors, which includes regular reporting on fund performance, portfolio holdings, investment strategies, and associated risks.

According to the analysis, there are still some fatal flaws in the current Chinese trust market. Most domestic trust products are less liquid than other financial products. There are many reasons for the lack of liquidity. First of all, China Trust's extremely high management fees lead to higher turnover costs, and the turnover rate is lower than the market average. Secondly, China Trust lacks a complete and mature secondary market: narrow investor base because of high thresholds, mainly targeting high-income people, for investors to enter the market of trust products. Moreover, investors tend to buy trust products with the intention of holding them to maturity.

Although most trust companies in China are controlled by the government, this does not mean that the government will provide unlimited support. The risk of default is still high in the Chinese trust market. For example, the recent well-known incident: State media reported on Wednesday that products worth $126 million issued by Jilin Province Trust Co Ltd, and linked to a loan to a deeply indebted coal firm, failed to repay investors when they matured in recent weeks. That followed a near-default on a similar product from China Credit Trust Co Ltd last month.

3.2. Default Rate and Risk of Trust Products in Recent Years

Trust plays a very important role in the financial industry and is famous for its high yield and high security. However, since last year, the trust industry has suffered a major blow. The latest monitoring data obtained from research institutions shows that in the first quarter of this year, there were 65 default events in the trust industry. Although the number of defaults further increased compared with the first quarter of 2021, the number of default projects decreased by 33.69% compared with the same period last year. Delays and default cases in the trust industry due to the impact of the epidemic are still increasing. According to the latest monitoring data, 65 default events occurred in China's trust industry this year, with a default amount of 27 billion yuan.

3.3. Measures and Policies

Measures on trust default have been further upgraded in recent years. Looking back at the regulatory roadmap of the trust industry, in 2017, the China Banking and Insurance Regulatory Commission ("CBIRC") launched a campaign to crack down on rectifying market chaos. At that time, the trust industry was included. In the three years from 2018 to 2020, the scope of supervision was further expanded. In 2018, the supervision focused on the investment of wealth management funds in equity financial products or financial products with equity characteristics through trust products but did not strictly implement the standards for qualified investors. In 2019, the supervision mainly prohibited

DOI: 10.54254/2754-1169/39/20231955

the real estate business of the trust industry from providing financing in disguised forms, such as incomplete four certificates, substandard funds, public shares, real debts, and accounts receivable. In the special rectification in 2020, CBIRC still focused on the real estate sector, mainly increasing the actual use of funds for real estate development in the name of granting loans to upstream and downstream enterprises, related parties, or construction parties of developers, to avoid the regulatory requirements related to real estate trust loans. Under the joint influence of many factors, such as the downward pressure of the economy, the impact of the spread of the epidemic and the firm promotion of transformation, and the risks accumulated by individual trust companies in the early stage broke out, the operating conditions continued to deteriorate, and the risk events of trust product default occurred frequently. At least six trust enterprises have a non-performing rate of more than 20%. From the perspective of the non-performing rate of trust projects, with the increase of the scale of risky assets, the non-performing rate of trust projects has increased significantly. Before 2017, although the non-performing rate of trust projects fluctuated, it remained below 0.8% most of the time, and rose significantly to 2.67% at the end of 2019.

3.4. Take HuaRun as an Example

Last year, from its establishment to its loss, it never disclosed the product information, resulting in the forced liquidation of the position of investors because they could not make up their capital in time. Finally, the "Red Diamond No. 101" and "Red Diamond No. 102" of Huarun docked the remaining funds of "Wenyi No. 6" and "Wenyi No. 7" investors respectively, and promised to return the principal and annualized income of 5% in one year.

3.5. The Rectification and Development of Trust Industry in China

In the Chinese financial sector, the trust industry, the banking industry, the securities industry and the insurance industry are collectively referred to as the four pillars of finance. Since China resumed the development of the trust industry in 1979, China trust industry has played an important role in optimizing the allocation of social resources for the Chinese market and meeting the financial needs of enterprises [3]. The development of China's trust industry continued from unsystematic and savage growth until the end of the 20th century. It was not until the People's Bank of China promulgated the *Administrative* Measures *for Trust and Investment Companies* in May 2002 that China trust industry began to get a system management and began to develop. The institutional improvement of China's trust industry can also be reflected in the number of trust companies in the figure below. Normative regulations have caused non-compliant trust companies to fail or be merged by large companies.

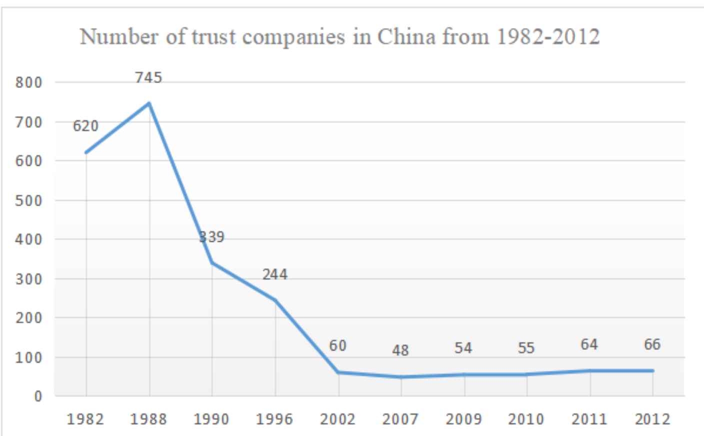

Figure 1: Number of trust companies in China from 1982-2012.

The China trust industry was reorganized by the government in 1982 and 1985 respectively, to coordinate the macro-control relationship between the trust industry and the banking industry. In 1988, the rapid economic development in China led to serious overheating of the economy, and the government carried out a third rectification of the trust industry. The government controlled the currency and stabilized the financial order by cleaning up and rectifying trust institutions, which directly led to the collapse of many trust institutions. In 1993, the government reorganized the trust industry in response to the overheating economy, because China's trust industry invested too much in fixed assets at that time. In 1999, Chinese trust companies generally had problems such as poor asset quality and payment difficulties. Then the government carried out the fifth rectification. Since then, Chinese trust companies no longer operate securities brokerage business and stock underwriting businesses. Before 1999, the development direction of China's trust industry was unclear and the development of the industry was disorderly. From 2000 to 2001, the development of China's trust industry was at a standstill. It was not until the promulgation of the *Trust Law* at the end of 2001 that the trust industry began to develop in an orderly manner. In 2002, trust companies finally began to launch standardized trust financial services. After these five large-scale rectifications, the number of trust companies in China decreased from more than 700 in 1988 to 60 in 2002. The number of trust companies has fluctuated in the range of 40-70 since 2002. With the improvement of the system, the rectification of the trust industry will also make the polarization of the trust industry more obvious. Strong trust companies will become stronger, while weak trust companies will face the risk of being eliminated or merged (China Trust Industry Research Report 2010-2011, 2010), which is also reflected in the high-frequency asset restructuring of China trust industry around 2010. However, it promotes competition among various institutions in the trust industry, which accelerates the development of the trust industry.

3.6. Comparison of the Trust Industry to the other Three Financial Industries in China

Since 2008, China's trust industry has developed rapidly. As Table 1 shows, from 2008 to 2018, the scale of China trust assets continued to rise, and the growth rate from 2009 to 2012 reached more than 50% annually, much higher than the 22.3% growth rate of the insurance industry in 2012.

Table 1: Growth of China Trust Industry.

Year	Asset (trillion)	year-on-year growth rate
2008	1.22	
2009	2.02	65.57%
2010	3.04	50.50%
2011	4.81	58.25%
2012	7.47	55.30%

Source: China Trustee Association

Since the scale of trust assets reached a peak of 26.25 trillion yuan in 2017, it has gradually declined from 2018 to 2020, to 22.70 trillion yuan, 21.61 trillion yuan and 20.49 trillion yuan respectively. This downward trend showed obvious signs of stabilization in the first three quarters of 2021, and achieved a rebound in the fourth quarter.

The 2021 China Trust Industry Development Review released by the China Trustee Association shows that by the end of 2021, the balance of trust assets in the entire industry was 20.55 trillion yuan, an increase of 60 billion yuan over the 20.49 trillion yuan at the end of the previous year, a year-on-year increase of 0.29%. This is the first year that China trust industry has stopped falling and rebounded since it entered a downward period in 2018. This means that the transformation and development of the Chinese trust industry has begun to stabilize, the supervision of China’s trust industry has become stricter, and financing has become easier.

Judging from the performance data of specific trust companies, the growth rate of net profit of trust companies such as CITIC Trust, CCB Trust, China Resources Trust, and FOTIC is above 15%. Among them, CITIC Trust and CCB Trust increased their net profit by more than 30% in 2021.

From the perspective of the overall industry scale, the asset scale of China's trust industry exceeded that of public funds for the first time in 2010, and surpassed that of the insurance industry in 2012. Up to now, the asset scale of the trust industry has exceeded 23 trillion, and it is currently the second largest financial industry after the banking industry (344.8 trillion). It has become an important force in China to support the real economy [4].

3.7. Chinese Government Policy on the Trust Market

The first policy regarding the trust market of China was published in 2001. Before that, China's trust industry was relatively chaotic: The People's Bank of China established trust and investment companies at all levels outside of its purview, and the main work involved cleaning them up. Other tasks include re-registering non-bank financial institutions nationwide and severing state-owned commercial banks' ties to the trust and investment companies they manage. China's trust sector has reached a regulated stage after the promulgation of the Trust Law of the People's Republic of China in 2001, which regulates trust relationships and trust behavior from an institutional perspective. In 2018, the "Guidance on Regulating Asset Management Business of Financial Institutions" was introduced, further tightening oversight of the asset management industry. The size of Chinese trusts has fallen due to the stricter regulations governing asset management. In 2022, which is the first year of the official implementation of China's new capital management policies, the “two compressions and one reduction” will be sticked on, that is to compress the size of the non-compliant finance business, shrink the size of the trust channel business, and accelerate the sale of risk assets both on and off the balance sheet.

3.8. Analysis of the Impact of Lowering Required Reserve Ratio on the Underlying Trust Business

The central bank cut rates by 0.25 percentage points on April 25 in response to the local pandemic disturbance and to keep a broad credit environment for stable growth. From the standpoint of the effects on the trust business, the basic industry trust ushered in a new period of development; the underlying trust can concentrate on value assets and portfolio investment business opportunities to guard against the risk of interest rate upside; the real estate industry's liquidity will improve, and real estate trust entered a period of transformation and development [5].

Financing platforms' reasonable needs for capital are continually satisfied. The percentage of basic industry trusts has been dropping since 2020 and fell to 11% at the end of 2021 due to initiatives including restricting government platform financing and preventing and controlling local government debt concerns. Meeting their acceptable financing demands can assist in fostering stable growth investment on the ground. Financing platforms are essential subjects for local governments to carry out investments in basic industries.

DOI: 10.54254/2754-1169/39/20231955

Due to the increased demand for infrastructure investment, basic industrial trusts have introduced a new growth stage. A result of the current slowdown in sectors, including real estate and industrial and commercial business sector trusts, high-quality government trust products have gained investor awareness, and the issuance scale and share are continuing to recover. According to Table 2 from Ushio Trust Network, the number of basic industry trusts established in March was 25.7 billion yuan, an increase of 121%, and the size of basic industry trusts accounted for 31%, an increase of 8.4 percentage points from the previous month. Trust firms can profit from the current business opportunity by actively marketing the core trust business.

Table 2: Establishment of individual fund-invested pooled trust products in March (Unit: billion yuan).

Investment fund	March size	Size share	February Size	Size Share	Ringgit fall up
Finance	377.97	46.18	206.87	51.51	44.89
Real estate	121.87	14.89	86.69	17.12	40.58
Basic Enterprise	54.17	6.62	39.78	7.85	36.16
Basic Industries	257.36	31.45	116.57	23.02	120.77
Others	7.03	0.86	2.53	0.50	177.69
Total	818.38	100	506.44	100	61.60

4. Conclusion

The China trust industry has developed a unique way of survival that varies from most trust industries in other countries. Through analysis, we realize that a major reason behind this situation is the Chinese government's strict control over the entire industry as well as the fact that China is still a developing country and the trust industry is closely related to the development of the nation. Though finance is the largest investment field of all types, investment in the basic industries is still a crucial part of the trust industry. Based on the changes of the industry mentioned above, we can anticipate that more capital will flow into this industry and the focus of the industry will spread among various fields of investment. As a result, more competition will rise among the trust companies in China.

Acknowledgement

Wangzi Gao, Zhenyi Lu, Leyang Zhang, Zilin Zhang, and Xucheng Luo contributed equally to this work and should be considered co-first authors.

References

[1] *"Trust Law of the People's Republic of China." Pbc.gov.cn, http://www.pbc.gov.cn/english/130733/3842874/index.html.*

[2] *Barone, Adam. "What Everyone Should Know about Trust Companies." Investopedia, Investopedia, 8 July 2022, https://www.investopedia.com/terms/t/trustcompany.asp.*

[3] *Research Report on China trust industry - 2010-2011. (Industry overview). (2010). In China Weekly News (p. 167–). NewsRX LLC.*

[4] *"Comments on the Development of China's Trust Industry in 2018." China Trustee Association, http://www.xtxh.net/xtxh/financeEN/45458.htm.*

DOI: 10.54254/2754-1169/39/20231955

[5] Jinrongjie. "An analysis of the impact of reserve requirement reduction on the trust market" https://baijiahao.baidu.com/s?id=1731072775823199780&wfr=spider&for=pc