

# Financial Openness and Risk Awareness of Government Governance

Lili Tian

Henan Polytechnic University, Jiaozuo, China.

## Abstract

The development of today's world is becoming more and more globalized, financial opening is the general trend, and the government is gradually strengthening the financial opening. At the same time of rapid development, can we keep rational, achieve the maximum benefit, and not cause a huge crisis loss due to the neglect of risks? Finance is of great significance to the development of a country, and the financial opening also makes the development of a country more efficient, faster and more diversified. However, under the great temptation, the role of the government appears to be very important. Therefore, this paper will begin to analyze the risk awareness and means of financial openness and government governance, to emphasize the co-existence of development and risk and how to better play the role of financial openness.

## Keywords

Financial Openness; Financial Risk; Financial Regulation; Government Measures.

## 1. Background of modern financial development

Since the reform and opening up in 1978, China has always adhered to the concept of opening up to the outside world and reforming to the inside. Of course, the opening process of the financial industry also started from there, and it has been nearly 40 years. In these forty years, the financial opening has made remarkable achievements, but there are also many problems, development so far, how to come?

The period from 1978 to 1993 was the embryonic stage of China's financial opening-up. In the early period of opening up, the domestic foreign exchange in the field of foreign trade was extremely short, the introduction of advanced equipment was insufficient, and the industrial development was restricted. Under such basic national conditions, the financial opening at this time is mainly to cooperate with the domestic development and construction of economy, to solve a series of measures such as employment and increase of foreign exchange and capital.

In 1994, in order to learn the experience of market economy, China loosened the admission standards for foreign banks and carried out a series of exchange rate reforms, which will have an important impact on China's monetary policy, financial market and exchange rate system in the coming decades.

However, in 1997, when the Asian financial crisis broke out, China had not yet formed a strong enough ability to resist risks and was severely hit in the storm. The government realized that there were no conditions for vigorously opening up now, so China imposed corresponding restrictions on foreign investment.

In 2001, China joined the WTO, the development of the banking industry entered a period of acceleration, and the business scope of foreign banks continued to expand. China has made a commitment to the opening of the financial industry, but it still retains some restrictions on market access, shareholding ratio, establishment form and other aspects.

The outbreak of the financial crisis in 2008 made it more difficult for foreign financial institutions to enter China.

However, with the gradual improvement of RMB internationalization, the government launched RQFII (RMB Qualified Foreign Investor) in 2011 and RQDII (RMB Qualified Domestic Investor) in 2014 in order to further accelerate the opening of the financial market and the process of RMB internationalization. In the same year, the Shanghai-Hong Kong Stock Connect linking the Hong Kong Stock Exchange and the Shanghai Stock Exchange opened, connecting domestic and overseas markets and providing more options for cross-border trading.

After the "8.11 exchange rate reform" and the successful inclusion of RMB in the SDR currency basket in 2015, the process of financial opening-up began to accelerate.

## **2. Analysis of the present situation of financial opening**

### **2.1. The current state of financial openness**

#### **2.1.1. China's financial opening**

As the economic development becomes more and more globalized, opening to the outside world becomes more and more important. China has made remarkable achievements in the course of opening to the outside world in the past 40 years.

At the Boao Forum held this year, General Secretary Xi Jinping made it clear to the world that "China will only open its door wider to the outside world. In the future, China will significantly ease market access, including in the financial sector." In addition, the central bank governor and other senior officials also indicated that China should further open up, including easing restrictions on the establishment of foreign financial institutions, expanding the business scope of foreign financial institutions in China, and broadening the fields of cooperation between China and foreign financial markets. This series of voice, the implementation of a series of measures, is undoubtedly to pave the way for China to the international market.

The development of the financial industry is becoming increasingly diversified. The introduction of foreign investment, enhanced cooperation and joint development are also hot words of The Times. China has significantly relaxed the market access threshold, which has declared to the world China's positive attitude towards opening up, and demonstrated its determination to open up the financial industry in particular. The further opening of the financial industry is conducive to the integration of China with the international finance and the enhancement of competitiveness, so as to promote the financial enterprises to enhance their own level, accelerate the process of marketization, promote the flow of capital in the world, and can also play an important role in international affairs.

#### **2.1.2. China's financial opening**

Almost all developed countries are open financial market has been basically achieved, their high degree of marketization, allowing the transnational operation of financial assets, although most of the developing countries the accompanying economic and financial development degree low, but the financial transnational management brings positive effect, make them to further open financial markets, improve the international financial dependency. The increasingly securitized international capital market connects the capital supply of developed countries with the investment opportunities of developing countries, forming an international mechanism for the effective allocation of capital.

However, under the general trend of financial opening-up, what risks have been exposed while opening up?

### **2.2. Risk exposure under the condition of financial openness**

#### **2.2.1. Foreign Capital M & A Pressure on Small and Medium-sized Financial Institutions**

Foreign M & A is one of the ways for foreign countries to enter the Chinese financial market. On the one hand, foreign M & A will enhance the vitality of institutions, provide sufficient capital,

increase R & D investment, improve the competitiveness of enterprises and the quality of enterprises, thus strengthening the construction of the securities market.

But on the other hand, if some small and medium-sized financial institutions encounter poor operating conditions, may face greater pressure. Foreign M & A enterprises have strong competitiveness, once they have the opportunity, they will certainly exert pressure on their opponents, or even more serious will cause industry monopoly, endangering national economic security.

#### **2.2.2. Impact on international capital flows**

With the increasing opening of the financial industry to the outside world, the speed of foreign capital entering the Chinese market is obviously accelerated, resulting in the rapid flow of international capital, which is not necessarily a good thing for domestic financial markets.

China extrapolated the "Shanghai Stock Connect", which further strengthened the relationship between domestic and foreign financial markets and produced international capital flows, which would have an impact on the supply and demand of RMB. This has a great impact on China's balance of payments, foreign exchange rate, interest rate and so on. Therefore, the rapid and free flow of capital in China will increase the range of interest rates, thus affecting the exchange rate and increasing the risk of China's financial market. Will affect our policy autonomy.

#### **2.2.3. Cross-border operations increase macro risk**

Financial opening leads to the frequent occurrence of cross-border business, and the political and cultural environment of different countries is very different, coupled with the obvious differences in the financial markets of various countries, the external attitude of the government and so on, all increase the macro uncertainty risk.

Secondly, whether the occurrence of cross-border business has certain safeguards for resident enterprises, whether it can achieve the desired results, and whether the corresponding emergency preparedness measures have been made for national security?

#### **2.2.4. Balance between financial innovation and regulation**

Financial innovation is a necessary condition for the rapid development of financial market and the most basic requirement of financial market. Innovative products are developing rapidly, and the complexity and relevance are hidden under diversified products. Some buyers even blindly follow the trend when they can not understand the trading methods at all. Leading to imperfect markets, this is undoubtedly a barrier to the development of financial markets. Coupled with the subprime mortgage crisis in the United States, we should not begin to pay attention to and reflect on: is financial innovation the driving force of development or the root of the crisis?

So, how to ensure that the market in innovation and development while maintaining health? How to balance financial innovation, financial market efficiency and financial stability? The government has played a vital role, and the relationship between financial innovation and financial supervision is worth pondering.

### **3. Measures of the Government to Address Risks in the Financial Open Environment**

With the further opening up of finance in China, a large number of foreign-funded enterprises will appear in the financial market, which will also broaden the scope of business of foreign-funded insurance brokerage companies and enhance the field of financial market cooperation between China and foreign countries. The implementation of these measures will undoubtedly expand our openness and enable us to draw corresponding nutrients in the environment of financial opening, which is of great significance to development. However, while making

measures to open to the outside world, the government can also realize that development and risk coexist, so risk prevention and control is a matter that the government needs to pay close attention to. Here, I will analyze the government's measures to deal with risks from macro and micro perspectives.

### **3.1. Government's macro strategy**

The macro level is the overall description of risk, which is analyzed from the national and international aspects.

#### **3.1.1. Preparedness at the national level**

In the context of financial openness, risk is exposed, as a government authority, how can we prepare ahead of time? Of course, financial derivatives provide an effective way.

(1) Natural risk aversion in financial derivatives markets

With the deepening of economic globalization and economic liberalization, the global economic connection has become one, financial derivatives have been innovated and expanded more and more, and it has gradually evolved from traditional financial instruments to various financial derivatives. Now, its risk-aversion function has also been recognized and widely used. In the traditional sense, derivatives have two main applications:

On the one hand, as a financial instrument of investment speculation, carry out certain arbitrage behavior to earn income, but you know, because of the leveraged trade, many market participants are more and more speculative,

At this time it itself has a huge risk;

On the other hand, the important role of financial derivatives is to avoid risks, mainly used in risk management. Risk is everywhere, whether the state, government, financial institutions or resident enterprises, in the case of risk, can use derivatives to avoid risk, so that there will be no greater loss. Taking foreign exchange risk as an example, this paper expounds the safe-haven function of derivative instruments:

There are four main types of financial derivatives, namely forward, futures, options and swaps. All four can achieve their goals.

The first is forward foreign exchange contracts. When the expected exchange rate rise or fall to their own disadvantage, this time there will be foreign exchange risk. To sign a forward foreign exchange contract in advance, there will be a specified exchange rate in the contract, that is, the exchange rate of foreign exchange is fixed to a fixed value through the signing of the contract, and then delivered at the delivery date according to the exchange rate of the contract.

The second is foreign exchange futures contracts. After signing the foreign exchange futures contract, the market changes have an impact on both the futures market and the spot market. When the exchange rate changes, if there is a loss in the spot market, then the profit of the futures market will offset the loss of the spot market.

And foreign exchange options. This is a right to buy and sell, can be executed or not, relatively free, with the change of the market, executive options may also obtain unlimited benefits, but the loss is limited, the biggest loss is the option fee.

Finally, foreign exchange swaps. Both sides need to exchange the foreign exchange principal at the beginning and finally. Through the exchange of the foreign exchange principal, the two sides need not bear the exchange rate risk during the exchange period, so they can play a safe role.

The effectiveness of financial derivatives to avoid risk has been confirmed by the market. The government should also respond positively to the needs of the market and give certain financial R & D support to the open application of financial derivatives. Make more abundant financial derivatives appear in the public view. But at the same time, we should pay more attention to strengthen supervision in the process of financial innovation, take the subprime mortgage crisis of the United States as a lesson, and keep the financial market running well.

Therefore, the government should continue to study the effective regulation of financial derivatives:

- ① Combined with the financial supervision model of mixed industry, the multi-level supervision system is constructed.
- ② Strengthen the study of derivative risk and establish a scientific early warning mechanism.
- ③ Establish accounting information disclosure system in accordance with international standards and strengthen the transparency of financial derivatives information disclosure.
- ④ Strengthen the supervision and guidance of financial markets to provide a good external environment for the development of derivatives.
- ⑤ Strengthen international regulatory cooperation and promote exchanges between different markets.

## (2) Building sound capital markets

Capital market is an important part of a country's financial market. Based on the present situation of China's capital market, it is another important measure for the national government to prevent risks by absorbing the experience of capital market construction at home and abroad and steadily promoting the construction of China's capital market system. Only with the ability to guard against open risks can we resist risks and develop better. Therefore, the government is also actively promoting the construction of capital markets.

### ① Promoting capital market structure

This year, the CSRC issued a series of rules, such as the Administrative Measures on the Issue and Trading of Depository Receipts (Trial Implementation), which have made corresponding institutional arrangements for innovative enterprises to issue stocks or depository receipts in China. The return of unicorns to China is also helpful to perfect the structure of capital market, perfect the mechanism of capital market and give full play to the function of investment and financing of capital market.

### ② Scale up capital markets

The scale of China's capital market has not reached a certain degree, the degree of marketization needs to be improved, and diversified capital types are introduced through certain policies.

### ③ Improving the Law and Regulation System of Capital Market

With the increasing scale of capital market, the role of supervision is becoming more and more important. Sound laws and regulations are conducive to the healthy operation of capital market and an important guarantee to prevent financial risks.

## 3.1.2. Active response in the international context

So, in the international market, how can China take the initiative? What policy guidance has our country introduced?

### (1) Significance of crude oil futures listing

On March 26, China's crude oil futures trading at the Shanghai International Energy Trading Center officially listed trading, this major event, and what does it mark?

The biggest bright spot and innovation of the design scheme of crude oil futures contract can be summarized as 17 words "international platform, net price trading, bonded delivery, RMB valuation". RMB pricing directly promotes the process of RMB internationalization and makes China's international importance increasingly prominent. The introduction of crude oil futures has provided risk pricing and price discovery tools for enterprises in China and even the Asia-Pacific region, as well as hedging and risk management tools for Chinese enterprises. China has participated in international oil pricing to a greater extent, achieved greater financial opening, also achieved a large integration of domestic and foreign markets, and attracted diversified investors, injecting new vitality into China's financial market.



In addition, while introducing foreign investors to participate in the Chinese market, it objectively requires China to speed up the convertibility of the RMB and constantly improve the mechanism of marketization of the RMB interest rate exchange rate.

## (2) The process of currency swaps

Currency swap is one of the financial derivatives, however, it also plays a vital role in the process of RMB internationalization. And China is now expanding the national scope of currency swaps, trying to increase global influence through currency swaps, but also promoting international cooperation and financial stability.

The growing number of currency swap agreements signed by the central bank also highlights the trust and dependence of trading partners on China. In the long run, this has greatly promoted the internationalization of the RMB, enhanced China's international status and enhanced China's international influence.

## 3.2. Government's Micro Strategy

After the analysis of the national macro level, the purpose of the corresponding measures taken by the government is basically understood. Therefore, for the microeconomic subject, how to better play the role of various financial futures options is also a major topic.

### 3.2.1. Provide risk prevention tools to companies

No matter what industry, the pursuit is a relatively stable return, however, in the real market, price is a constantly fluctuating factor, the fluctuation of price is a serial effect, that is, there is a certain connection between commodity prices. A price change will affect the price of other goods. So in the industrial chain, how can we keep the profit of the enterprise under the condition of poor market environment, or how to realize the minimum loss?

As we all know, futures options are effective risk management tools. They have the functions of "price discovery" and "hedging", which can solve the above problems. Futures options have been applied in many fields, such as the use of option risk management, the simplest way is two: one is afraid to buy call options. Worried that the price of raw materials will rise when the purchase, can not achieve the expected income, achieve a goal of locking in the expected cost; second, fear of buying put options. Worried that the price of the product fell, the sale did not reach the expected profit, so the selling price was fixed. In this way, enterprises in either case can lock in profits, achieve the desired goals, to achieve risk avoidance function.

The government authorities should understand the risk management basis of social grass-roots enterprise units, strengthen policy guidance, provide them with a more convenient and perfect system, introduce diversified preservation tools, strengthen the principle of prudent supervision, promote the normal operation of enterprises, and provide guarantee for the vitality of our market.

### 3.2.2. Risk prevention measures for individuals

On the individual level, I divide it into two parts: one is a one-way supplier based on farmers, the other is the participants in the financial market.

(1) Farmers' agricultural products are sometimes provided to certain physical enterprises, and in the process there is also a risk of falling prices, so they can maintain their value by signing forward contracts with the acquiring company or buying and selling futures contracts. However, due to the limitation of the scale of individual farmers, it is difficult to realize the hedging of large quantities of farmers to prevent price risk in China. Previously, because of various reasons, the crop harvest is not good or the market condition is not optimistic, causes many farmers to appear the situation which can not receive the expenditure, causes the agricultural product massive waste. Therefore, the government will pay more attention to agricultural products, on the one hand can improve the living conditions of farmers, on the other hand, to a certain extent,

enhance the market risk resistance, which will also be one of the problems that our government should focus on.

(2) China has a large number of financial market participants, but the vast majority of investors still lack relevant professional knowledge, resulting in blind follow-up operations, exposing themselves to risk. Therefore, for these people who speculate in the financial derivatives market, increasing risk awareness is the most fundamental means to prevent them from being swallowed up by risk. The government should strictly supervise and restrict speculative operations, ensure the normal and healthy operation of the financial market, prevent the emergence of huge losses, the supervision process should be targeted, the implementation of policies should be targeted, while strengthening policy guidance to prevent the emergence of bad phenomena in the securities market.

#### 4. Conclusion

This paper mainly analyzes how the Chinese government should disperse risks under the background of financial opening, how to combine risk prevention with financial risk avoidance tools, and emphasizes the important role of government governance in the process of financial opening. It also provides relevant opinions and suggestions for government departments in practical application.

The risk consciousness of financial opening and government governance is a big research topic. The focus and innovation of this paper are mainly from the perspective of the government to analyze the financial opening more deeply. The important role of financial instruments in financial markets is strengthened by linking government risk management with the risk avoidance of financial derivatives.

#### References

- [1] Qi J.Y., Qi S.B.: Financial regulation under globalization. Capital University of Economics and Trade Press, 2011(06). (In Chinese)
- [2] Zhang M, Kong D P, Pan S and Li J. The dimension, order and risk prevention of China's financial opening [J]. New Finance, 2021(04):4-10.
- [3] Shi J.H. A study on the impact of Financial opening on the effectiveness of Financial Supervision. China Fiscal and Economic Press, 2007(04).