Research on Financial Market Development and Commercial Bank Strategies under the "Dual Circulation" Pattern

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Abstract: "Establishing the new development pattern with domestic circulation as the mainstay and domestic and international circulations reinforcing each other" was proposed for the first time in 2020. The enormous domestic market is a crucial carrier of the "dual circulation" pattern and is the greatest advantage and confidence for China's long-term economic growth and its ability to face internal and external pressures and challenges. The reorganization of China's economic order and economic factors under the "dual circulation" pattern presents both opportunities and challenges for the high-quality development of commercial banks. Commercial banks should focus on areas such as deepening regional development, implementing the "commercial bank" + "investment bank" model, refining industry client classification, enhancing risk management, and emphasizing talent cultivation to further promote high-quality development in the financial market.

***Keywords*:** dual circulation, financial market, commercial bank

1. Introduction

To address the complex and severe domestic and international situation, our country proposed to "accelerate the formation of a new development pattern with domestic circulation as the mainstay and mutual promotion of domestic and international dual circulations", known as the "dual circulation" strategy. This is a significant decision aimed at solving medium- and long-term issues and is an important way to achieve stable growth and risk prevention in the long term, as well as to reshape new international competitive advantages.

2. Developing Domestic Demand: Economic Growth Reliant on the "Internal Circulation" System

From the demand perspective, consumption, investment, and net exports are the three main drivers of China's economic growth. Since joining the WTO, China has deeply engaged in the process of economic globalization, shared the benefits of globalization, and become a major trading nation. However, this also exposed many problems, such as being at the low end of the trade value chain, high consumption of energy and resources, serious environmental pollution, and a coarse domestic economic development model, along with the pressure of trade surpluses on international relations. Events like the China-U.S. trade friction in 2018 and the global outbreak of COVID-19 in 2020 have increased pressure on global foreign trade and investment development, prompting us to accelerate the development of the domestic market. Therefore, the central government has proposed focusing on internal circulation primarily to provide a larger buffer space to address international severe situations and pressures. Relying on internal circulation, steadily increasing the domestic market's contribution to GDP, and building a sound internal circulation system are proactive adjustments to the traditional domestic economic development model and an important strategic adjustment in the economic development process.

3. Opportunities and Challenges Facing Commercial Banks under the "Dual Circulation" Pattern

The implementation of the "dual circulation" strategy will involve a reorganization of China's economic order and economic factors. The development of domestic demand, primarily driven by consumption and investment, will be elevated to a higher position, and the concentration of resources towards these two fundamental engines will increase. These changes will have fundamental and comprehensive impacts on commercial banks.

3.1 Opportunities

3.1.1 More Stable Economic Fundamentals

Facing unprecedented global changes, economic development is fraught with significant uncertainty and instability. Relying on external demand for development brings substantial risks. Furthermore, the greater the dependence on foreign trade, the higher the reliance on international finance, and the inevitable risk of international financial contagion. The dual circulation strategy, with a focus on internal circulation, aims to stabilize external demand while strengthening and expanding internal demand, thus solidifying the foundation for sustained economic growth and seizing the initiative in development. For commercial banks, this provides a stable environment for implementing long-term development strategies.

3.1.2 Stronger Consumer Demand

The expansion of consumption, a key component of domestic demand, will drive explosive growth in related consumer financial services offered by commercial banks. Traditional areas for commercial banks such as long-tail customers, rural finance, pension finance, health finance, and travel finance will enter a new phase of development. Various reforms will significantly increase the income of middle- and low-income groups, bringing new deposits and sources of funds to commercial banks and optimizing their asset structure. Current practices show that consumer loans have the lowest default rates among financial products, providing new opportunities for improving the quality of commercial banks' credit assets.

3.1.3 New Round of Infrastructure Investment, Emerging Industries, and Technological Innovation

With increased infrastructure investment and more fixed asset investment projects, commercial banks will need to adjust their credit asset structures accordingly. By increasing investments in fixed assets, commercial banks can effectively boost the scale of high-yield assets. The development of the digital economy and the societal shift towards digital transformation involve technologies such as big data, blockchain, artificial intelligence, mobile internet, and the Internet of Things, leading to the rise of fintech industries. This greatly enhances cost management and risk control in the financial sector and fosters emerging industries and enterprises. To maintain leadership in the economic dual circulation, technological leadership must be preserved. Therefore, the state will support the development of technological innovation enterprises, integration of production, education, and research, transformation of scientific achievements, and innovative activities of high-caliber talent. For commercial banks, supporting technological innovation enterprises will be more confident, motivated, and secured, further enriching financial products for technological innovation and improving financial productivity.

3.1.4 Development of Supply Chain Finance

The "dual circulation" pattern requires the smooth operation of production, circulation, distribution, and consumption, with a spiraling increase in scale and continuous contribution to the economy. To keep the economic dual circulation smooth, seamless integration of various nodes in the industrial and supply chains is required, ensuring unobstructed flows of funds, information, and goods. For commercial banks, supply chain finance will become a crucial support for the smooth operation of the "dual chains." Banks need to accurately grasp the financial needs across the "dual chains," actively innovate supply chain finance products, and ensure the rapid and healthy development of supply chain finance to maintain the continuous and stable operation of the "dual chains."

3.1.5 Development of Green Finance

With China’s clear goals of "carbon peak by 2030" and "carbon neutrality by 2060," low-carbon transformation promotes consumption upgrades and technological self-innovation, aligning with high-quality economic development. Thus, ESG (Environmental, Social, and Governance) investment is gaining popularity in the asset management field. ESG investment is value-oriented, incorporating social responsibility into investment decisions to improve investment structures, optimize risk control, and ultimately achieve higher long-term returns. There is significant potential for commercial banks to expand their business in the ESG investment sector.

3.2 Challenges to Address

3.2.1 Increased Risk in Asset Quality Management

Under the "dual circulation" pattern, industries and enterprises will be subject to categorized management and policies of selective support and pressure. Projects related to consumption, investment, and technology will be strengthened, while others may be weakened, especially those with overcapacity, which will accelerate market clearing. Commercial banks will concentrate their resources on high-quality domestic clients, which could lead to further intensification of large client accumulation and increased concentration of loan risks.

3.2.2 Increased Risk of Customer Attrition

With the focus shifting to domestic customers due to the internal circulation, the customer market might transition from a seller's market to a buyer's market. Previously neglected customers, inclusive finance, and small and micro enterprises will become targets of competition among major commercial banks. In this market environment, large state-owned commercial banks, with their scale advantages, lower funding costs, advanced financial technology, and nationwide service networks, will gain a competitive edge. As financial products become more homogeneous and competition intensifies, particularly for small and medium-sized commercial banks, it becomes more challenging to market to customers, increasing the risk of customer attrition.

3.2.3 Increased Difficulty in Product Innovation

The emergence of new industries and enterprises in the dual circulation pattern presents both new opportunities and risks for commercial banks. Due to limitations in understanding and information asymmetry, there is often inadequate comprehension of the operational rules of the new economy. Especially in the context of uncertain economic development, predicting new industries, deepening long-tail client relationships, and navigating financial regulations and policy constraints all contribute to the increased difficulty of financial product innovation.

4. Recommendations for Promoting the Development of Financial Market Business for Commercial Banks

(1) Deeply Integrate with Regional Economic Development to Enhance Support for the Real Economy.In recent years, local governments have integrated large state-owned enterprises (SOEs) to improve their market competitiveness. These transformations present both opportunities and challenges for commercial banks. The opportunity lies in the expanded business areas for providing financial services and advisory to these large SOEs, while the challenge includes the significant impact of SOE restructuring and mergers on investment banking and financial markets, which raises higher requirements for risk prevention.

(2) Strengthen Top-Level Design and Fully Advance the "Commercial Bank + Investment Bank" Development. Leverage the advantages of investment products to drive collaborative development across various business areas. With "investment" as the core, radiate across all business sectors of the bank, maximizing the benefits of investment products and fostering comprehensive collaborative development. The head office of commercial banks should actively implement a full-license operation philosophy and accelerate the creation of a "large, strong, stable, and excellent" financial group. In the future, the head office can secure more licenses for funds, asset management companies (AMCs), securities firms, and direct banks to facilitate "one-stop marketing" and "full-process service" for the bank. By leveraging advantages such as customer base, funds, and channels, banks should vigorously expand their financial market business and pursue a distinctive path of comprehensive operations. Promote the "Commercial Bank + Investment Bank" service model, continuously improve the collaborative marketing mechanism between corporate finance and financial markets, integrate resources from corporate, investment banking, asset management, financial markets, and custodial services, and strengthen the meticulous and smooth coordination mechanisms between head offices and local branches, business management departments, and marketing departments to form an integrated operational and collaborative marketing mechanism.

(3) Refine Industry Classification to Accurately Enhance Control Efficiency.Provide targeted guidance and support to key branches, implementing "one-on-one" client management for key clients of these branches at the head office level. Integrate corporate, investment banking, interbank, and investment business resources at the head and branch office levels, implementing closed-loop management for key clients in bond underwriting, bond investment, traditional credit, and account settlement. Branches should closely follow local credit and investment policies, focusing on high-quality industries such as urban investment companies, new infrastructure, emerging industries, and green industries, identifying high-quality projects and client lists, avoiding issues of tight internal and external scales, and increasing support. Update the whitelist of clients quarterly based on local customer groups, strengthen cooperation with state-owned enterprises rated AA or above and high-quality private enterprises, promote systematic development and deep cooperation with target clients and their upstream and downstream partners, effectively supporting rapid and comprehensive development of branch business, particularly by enhancing cooperation with key provincial enterprises to stabilize the commercial bank's bond issuance position.

(4) Formulate Client Segmentation Strategies to Improve Business Implementation Efficiency.The head office of commercial banks should define the business requirements for various lines and products based on market conditions, internal policies, client access, and risk management. They should actively promote "head-to-head" cooperation and establish a rolling "Commercial Bank + Investment Bank" client database to provide a basis for precise marketing by branch offices. For the client list within the database, streamline approval processes to improve business implementation efficiency and enhance the customer experience. Branch offices should actively respond to the head office's credit and investment policies, refine industry classification, and develop client segmentation strategies based on regional characteristics. Deepen the use of the "Commercial Bank + Investment Bank" service model to direct resources towards high-quality areas such as advanced manufacturing, strategic emerging industries, infrastructure, livelihood construction, and green ecology, and continuously

optimize the client and asset structure of commercial banks. In high-quality industry sectors, guide central and local state-owned enterprises towards direct financing; for medium-sized enterprises with good growth and stability, aim to capture all their basic accounts, credit, cash management, and payroll services; for small and micro enterprises, increase support through bill discounting and supply chain finance, and continuously enhance the "SME Financial Service Provider" brand.

(5) Improve Risk Control Mechanisms and Actively Prevent Various Risks.On the path of developing the "Commercial Bank + Investment Bank" business, continuously improve the risk management mechanisms of commercial banks. Focus on risk isolation, as investment banking carries much higher operational risks compared to simple settlement, custody, and other intermediary services. Pay particular attention to risk prevention and isolation, actively analyze and study the various risks that investment banking may bring, and develop corresponding risk contingency plans to achieve effective risk isolation and establish an independent control system. Strengthen fund management to avoid confusion between credit funds and investment banking funds; strictly adhere to operational procedures for investment banking, disclose relevant information truthfully, and prevent potential issues.

(6) Emphasize Talent Development and Build a High-Quality Talent Team.Financial market business is a typical knowledge-intensive sector that requires providing customized, efficient, and knowledge-intensive services to clients. Commercial banks should place high importance on talent development and building a talent pipeline, creating a high-quality, professional team. Increase efforts to attract talent with practical experience in finance, industry, law, and accounting, and expand the recruitment of outstanding professionals with practical experience in securities firms and investment banking. Improve team coordination processes, clearly define responsibilities, powers, and benefits for each link, and enhance team operational efficiency. Refine performance evaluation and incentive mechanisms for bank staff, establish a scientific and market-oriented compensation system, fully stimulate employee motivation, and leverage the core role of professional talent.

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