



The Linkage between China's Financial System and the Real Economy: Based on "From-whom-to-whom" Flow of Funds Account

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Flow of funds account is an important analytic tool for the financial flows of a nation, but it does not show the information about funds "from whom to whom", therefore, it is unable to fully demonstrate the flow of funds among different institutional sectors as well as the linkage between the financial system and the real economy. This paper proposes a method to estimate the three-dimensional structure of the flow of funds account, namely "from-whom-to-whom" account based on the traditional flow of funds account, and gives the estimates of China from 1992 to 2012. The estimated results show that the real economy had high dependence on the funds from financial sector in China, and the reliance remains quite stable. Meanwhile, there are significant differences between sectors: the non-financial corporate sector has the highest dependence on the funding from the financial sector, but the sector's internal funds and funds from the rest of the world are likely to undermine that dependence; the government sector's funding reliance on the financial sector are strengthened as the government bond market grows, but the dependence has been weakened as the government sector's savings increases in recent years; the household sector's dependence on the financial sector is deepening, but internal funding is still the primary resource of funding for the household sector. Furthermore, this paper establishes an Autoregressive Distributed Lag (ARDL) model to explore the relationship between finance and the real economy in China, and the study finds that the financial sector's funding to non-financial corporate sector does not have significant impact on the growth of value added of non-financial corporate sector, which indicates the possibility that the financial sector lacks efficiency in allocating funds.

Keywords: funding dependence; institutional sectors; ARDL model.