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<th>Internal capital market of China I &amp; II</th>
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Formulation of the Research Objectives
There is an increasing number of Chinese firms gaining access to the external capital market for financing, especially from the international capital market. Despite the additional sources of external financing, an increasing number of Chinese firms are still involving in the “guarantee loops”, where Chinese firms provide guarantee to each other for bank loans. The total amount of guarantee can be as huge as over RMB 2 trillion in 2005 from merely 800 listed Chinese firms. This phenomenon reflects the importance of the internal capital market among Chinese firms. The objective of this research is to determine what causes the firms to participate in the internal capital market, particularly in the “guarantee loop”.

Methodology:
Sample size: 2139 firm-years
Year of data: 1999 & 2002

Internal Capital Market of China

Findings: Microeconomic Factors
- Firms use the following financing alternatives substitutively:
  - overseas listing;
  - domestic listing;
  - internal capital market.

Findings: Macroeconomic Factors
- Firms are less likely to be involved in the internal capital market in regions with:
  - better legal system, such as property rights protection;
  - better economic development.

Findings: Interactions between Microeconomic and Macroeconomic factors
- State-owned enterprises are more likely to be involved in the internal capital market. However, the relation between state ownership and internal capital market is weaker in highly marketized regions.
- Non-state-owned firms tend to rely on the internal capital market for financing in regions where government intervention in business transactions is higher and the access to capital is restricted.