

Rise of Bank Competition: Evidence from Banking Deregulation in China*

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Abstract

Using comprehensive loan-level data in China, we investigate how the deregulation on bank entry barriers alters local banking industrial organization and its economic consequences. We document a novel trade-off: the potential benefits of deregulation are adversely mitigated by entrant banks' preferences for lending to SOEs over more productive private firms. This credit misallocation accounts for 0.25% of GDP losses and is mainly due to SOEs' soft budget constraints. Private firms need to provide more guarantees and higher ratings to borrow from entrant banks but enjoy lower interest rates. Access to these loans increases private firms' investment, employment, profit, and ROA.

Keywords: Banking Deregulation, Credit Misallocation, Big Data, Growth

JEL Classification: G21, G28, L50, O40

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