Analysis on the current situation, problems and potential solutions for the Chinese precious metals futures market

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Abstract. Since 1980, China's futures market has developed vigorously under the influence of the reform and opening-up system. Over the past forty years, the Chinese futures market has been on a steady rise and has become an important part of the Chinese economy. Since the outbreak of COVID-19 in 2020, the global economy has been hit by significant inflation in various countries, and the anti-inflationary properties of precious metals futures have played a great impact during this special period. This paper examines a series of problems in the precious metals futures market in China from the current situation of the market and proposes possible solutions. With China's accession to WTO, the globalization of China's financial market has accelerated, and in the process of acceleration has also brought many hidden dangers to China's financial market. China's financial market is not well regulated, thus leading to a chaotic situation. Therefore, it is important to analyze the current problems of the precious metal futures market through the current situation of China's precious metal futures market to stabilize the development of China's precious metal futures market.

Keywords: Problem; Solution; precious metals futures market.

1. Introduction

Over the past few decades, China's economy has grown at a very fast pace, which has driven the development of many industries in China. However, as the global economy has been hit hard by the epidemic in the last two years, countries around the world have adopted loose monetary policies in order to promote rapid economic recovery, which has led to significant inflation around the world and is expected to remain highly inflationary in the future. Against this macro background, precious metals have anti-inflationary properties and are expected to maintain stable price growth in the future, while demand for Chinese precious metal products futures will continue to pick up and grow. The Chinese precious metal products futures market started late and has had a tortuous journey. This paper will discuss the problems and possible countermeasures from the current situation of precious metal futures in China.

2. Current situation

Compared to the start of the precious metals futures market in the United Kingdom and other European and American countries, the Chinese precious metals futures market started late and developed in a tortuous process due to many reasons such as the socio-economic system. After the founding of New China, especially after the reform and opening up, the Chinese precious metals futures market started to develop [1].

According to the volume data from the Futures Industry Association (FIA), in the first half of 2022, among the futures exchanges in mainland China, DME, ZhengME, SFE and CME ranked 8th, 10th, 12th and 26th, respectively, in the global exchange futures and options volume rankings. In the global ranking of various futures and options varieties in terms of volume, Chinese futures varieties held 3 seats in the top 20 precious metals varieties.

Even with a late start, precious metal product futures are among the earliest to enter the Chinese futures market, the most mature in operation, and one of the most market-oriented and internationalized industries [2]. After China's accession to the WTO, China's financial market is accelerating globalization and gradually relaxing the scope of regulation [3]. Foreign banks will be able to operate RMB personal business, and domestic finance will directly face the impact of international investors. Precious metals investment is still a young industry in China. As time goes

by, it is gradually gaining acceptance and precious metals investment companies are springing up in China. On the one hand, it lays the foundation for the prosperity of the precious metals investment industry; on the other hand, due to the lack of maturity of the market management system, the domestic precious metals industry may have a chaotic situation with a mix of good and bad precious metals companies.

Since the outbreak of covid-19 in the world, various industries went into depression. Many people are disappointed with stock investments, and real estate has caused huge psychological pressure on investors because of the possible state regulation at any time. And precious metals (such as gold and silver) have the function of risk aversion and value preservation. Therefore, in the case of severe inflation, economic depression and unstable world political situation, it plays a role in diversifying asset risks for sound investors, and a large amount of money will flow into the precious metals market, and the price of precious metals will rise. At the same time, nowadays, the derivative investment products of precious metals are becoming more and more abundant, and their trading characteristics make it possible for investors to operate and make profits no matter when the price of precious metals rises or falls. In other words, no matter what time of year it is, precious metals investing will never go out of style. Therefore, the demand for precious metals investments is relatively strong whether it is physical demand or financial investment demand. Now that the number of precious metals investors is increasing year by year, many of them are new entrants, and the proportion of investors is much higher, more diversified and widespread. Not only is there a demand for preservation of value, but the momentum of speculation has also risen significantly recently. The previous situation was that at one stage there were more investors doing physical gold, on the steady side, and at the next stage it became more investors doing gold T+D and spot gold and spot silver. since the second quarter of 2022, the number of investors investing, and speculating has grown significantly. Precious metal investment represented by gold and silver still has a lot of room for development and profit.

Overall, the Chinese precious metals investment industry is relatively hot. Due to its new investment model, which meets the investment needs of different groups to varying degrees, the number of investors entering the market is gradually increasing. As a result, the precious metals industry is relatively robust in terms of both physical demand and financial investment demand and is expected to continue to grow over the next long period of time.

3. Problem

As the world economy develops, changes in market sentiment play a very important role, and changes in market sentiment are most directly related to policy, economic levels, market conditions and interest rate levels.

Against the backdrop of a significant easing of inflationary pressures in the U.S. in July 2022, once triggered market expectations of future interest rate hikes by the Federal Reserve. The dollar index cooled down, and the precious metals, which are negatively correlated with the U.S. index, were only able to present this wave of upward trend. In addition, the July lows for precious metals were probably the lowest so far this year, spurred by non-agricultural employment data and geopolitical factors at the beginning of the month. Of course, these expectations are based on the premise that the U.S. economy continues to improve. If the recovery is not as strong and Fed officials continue to suppress it, the market will fall into a period of anxiety and the precious metals will struggle to move. For the Chinese precious metal products futures market now, there are 3 main problems as follows.

3.1 Few trading varieties and lack of innovation

China's precious metals futures market has only experienced a short period of more than 20 years, and compared to developed foreign futures markets, China has very little product experience and a dearth of precious metals futures products [4]. The futures market is still dominated by agricultural and industrial products. This is mainly due to the fact that new futures products need to go through complicated and cumbersome procedures before they can be put on the market, which consumes a lot

of time and involves a lot of risk. These shortcomings will become a non-negligible problem affecting the future development of the futures market. First, although the futures market has made remarkable achievements, many systems are not very mature due to the short operation time, the lack of a suitable business environment, and the lack of understanding of futures by market participants, which is also an important reason for the structural imbalance. Second, the listing mechanism of new varieties is defective. The listing of new futures varieties requires a lot of complicated approval procedures. In this process, the new varieties face many problems, such as many links, high cost, long cycle and uncertainty. Now, it is extremely difficult to circulate Chinese precious metal futures in foreign exchange and there are few tradable varieties, which directly limits the trading scale of China's precious metal futures market. If the precious metals futures market does not innovate in varieties and still sticks to the existing varieties, it will not be able to enrich the varieties, and this harm cannot be avoided.

3.2 The relevant legal system is not perfect

When the economic system changed, China gave birth to the futures market under the compulsion of the government in order to prosper the economy and strengthen the motherland. Therefore, the futures market and the government are inextricably linked. The futures market cannot be separated from the government, and the government dominates the entire futures market. Therefore, to a certain extent, the government's prominence can be an obstacle to the development of the market. First of all, the deviation of regulatory philosophy can lead to frequent policy changes and reduce the transparency of the market [5]. The excessive power given by the state to administrative regulation has led to a serious imbalance of power between exchanges, associations and administrative regulation. The dominance of administrative regulation is irreversible. All of them lack mutual checks and balances and equality. The market's ability and motivation to innovate cannot be enhanced, and the market cannot continue to move forward. Second, China's futures laws and regulations are often accompanied by a lag, i.e., they address problems after they occur rather than taking avoidance measures in advance, which is inseparable from China's slow development [6]. Due to the huge potential benefits of the precious metals futures market, it is easy to induce various illegal incidents. This has led to the creation of appropriate laws for these events, resulting in a growing accumulation of relevant regulations that make the operation and implementation of the futures market difficult. In addition, there is a large amount of documentation to address other issues, which ultimately leads to inefficient markets. Finally, the legal regulation of financial futures markets is also flawed. In China, although there are many administrative orders and regulations for the futures market, there is still no futures trading law, supported only by administrative regulations, which are not sufficiently effective and authoritative. Its defect of too strong administrative color is also not conducive to the regulation of the futures market.

3.3 Insufficient market development capabilities

At present, the existing precious metals futures companies in China not only fail to meet the expected targets in terms of number, but also have a low overall level [7]. Not many of them can be ranked in China, which is mainly due to the fact that, first, in the financial sector, the economic benefits of precious metals futures companies are very weak in terms of revenue. Immature futures companies and a single business model make it difficult to operate, and many have even more difficulty in maintaining daily operations. Second, most futures companies have a weak sense of service and innovation and lack personalized service products. Finally, the lack of fresh blood of the times, the lack of understanding of innovation and reform, and the lack of consideration of the context of the times make the development of futures companies risky. At present, professional investment management companies and brokers in China are not yet established and planned, and there is a lack of real institutional investors. Currently, retail investors still dominate. There are few risk shifters and speculators among market participants. When the behavior of market players is not regulated and mature, it is easy to manipulate the market, resulting in violations and defaults [8].

4. Solution

The situation in China's precious metal products futures market is not promising in the future and there are too many problems. In order to continue the better development of precious metal products futures, China must take the appropriate approach to the precious metal products futures market.

4.1 Improve the system related to the precious metals futures market

Although the legal system has not kept pace with the times, it should continue to improve, update and implement as much as possible, so that the relevant departments can strictly follow the legal system and maintain the development of the futures market [9]. It is also necessary to clarify the legal nature of the development of the futures market as soon as possible, and the operation of the market economy can only operate normally under the protection of legal provisions. Futures economy is no exception. Only under the dual protection of laws, regulations and administrative supervision can this futures market develop healthily. However, we need to establish the law as the main body. Cracking down on the market economy with laws has become the norm of international management, and China is also using it. The function of the market rate of return should also be given full play in other aspects.

4.2 Accelerate the internationalization of the precious metals futures market

The government can strengthen the promotion and guidance of the precious metals futures market, improve the international competitiveness and influence of the precious metals futures market, make the precious metals futures market take its place on the international stage, broaden the market, establish friendly cooperation among countries, promote the generation of profit value in the precious metals futures market, and take its place in the international precious metals futures market [10]. First of all, we should always keep in mind the inclusiveness and diversity of the market, actively attract overseas liquid investors, attract overseas companies and economies, enrich the vitality of the futures market with overseas power, and create greater value through extensive trading. Achieve the goal of sustainable development and lead the futures market to the international stage. Secondly, we need to strengthen cooperation and innovation among international futures institutions and develop conflict resolution and regulatory cooperation programs. Establishing market hedging cooperation mechanisms is an important aspect of the international futures market. Finally, innovation in international product pricing power should be expanded. This is the era of economic integration and internationalization of capital, and the gap between developed and developing countries is widening. The precious metal futures market has become a weapon for them to compete for interests. They unscrupulously take advantage of their good economic conditions and background conditions to make huge amounts of money in international transactions. Their behavior has seriously affected the harmony and equality of international development. The consolidation of the precious metals futures market and the establishment of the legal system have become urgent issues. We must compete with developed countries in a better way and ensure our own economic interests.

4.3 Simplify the approval process and actively encourage innovation in precious metals futures products

With the rapid development of China's economy, Chinese investors need more and more types of precious metals futures products [11]. The Chinese government should first actively help futures institutions simplify the approval process for new products and shorten the approval cycle. Secondly, it should help financial institutions reduce the cost of innovation as much as possible, thus reducing uncertainty in the innovation of precious metal futures products. Thus, the size of the futures market for precious metal products should be expanded.

4.4 Improve the financial derivatives market

With the development of China's capital market and the acceleration of the reform process of precious metal products futures, we will gradually improve the financial derivatives market with stock index futures, interest rate futures and foreign exchange futures as the core to enhance the integrity of China's financial system [12]. This is the requirement for risk management by market participants and service recipients. The existence and development of capital markets must meet the needs of corporate development. In an environment of increased marketization, enterprises increasingly understand the role of the futures market in their development and growth, and urgently need to use the futures market to lock in risk and expand investment to create social wealth. This requires us to accelerate the pace of construction, design and provide effective financial derivative services to meet the needs of social development. In addition, the new idea of capital market development requires the financial derivatives market to develop beyond the norm.

5. Conclusion

With the rapid development of China's market economy and further convergence with the international market after joining the WTO, coupled with the reform of the enterprise system, a broad space for the development of the futures market for precious metal products has opened up. With the protection and support of the government, the precious metal products futures market will be further promoted with the positive interaction between the real economy and the precious metal products futures market, thus making the Chinese precious metal products futures market will have good development prospects. The development and continuous maturity of the spot market and the increase of marketization have also laid a good foundation for the development of the futures market for precious metal products. Looking ahead, with the rapid growth of China's precious metal products futures market, the degree of internal integration and external opening will continue to deepen, and China will have more and more say in global commodity pricing and procurement. The development of China's precious metal products futures market is still in its infancy, and there is still much to be done in terms of market system construction, market regulation, variety innovation, opening up to the outside world and expanding institutional investment. However, it is certain that the international status and influence of China's precious metal products futures market will become bigger and bigger. Once the financial futures varieties are gradually launched, the development of China's precious metal products futures market will be immeasurable.

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