

The Analysis of Informal Credit Behavior in Hui Autonomous Prefecture of Linxia: The Investigation Based on Hui Autonomous Prefecture of Linxia China

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Abstract

Nowadays, the informal credit, the financial form which the access to the loan capital derived from Informal financial institutions, and it plays the important role on the economic activity, and have a profound impact on the development of local finance. Through the roundly questionnaire survey in the Hui autonomous prefecture of Linxia to understand the present conditions, reasons and purposes of the region's informal credit, and analyze the problems arise during the development of informal capital raising, and finally propose the policy advice to promote the development of informal capital raising.

Keywords: informal credit, Hui Autonomous Prefecture, minority regions, Linxia

1. Introduction

Informal credit is also called the "folk credit" or "personal credit", and it refers the credit that provided between the resident individuals and the collective, and generally takes the mode of discussed interests and direct transaction. The formation and development of informal credit in China has been a quite a long time, in recent years, with the policy adjustment of country's interest rate and the influenced by the difficulty of farmers' micro-credit loans, the informal credit market became more active, and had the deepening impact on the local finance.

Hui autonomous prefecture of Linxia is located in the south central of Gansu province which lives more than two million people of 22 nationalities, such as Hui, Han, Dongxiang, Bao'An, Salar, Tu, Tibetan. Informal financing make up for the shortage of formal finance to a certain degree, and it plays a supplementary role on the development of Linxia's national economy. Informal financing satisfied the fund demand of private economy, individual business and the residents due to its simple, flexible, fast, and it also makes up the fault age of county financial system; increasing the usage efficiency of social idle funds, and promote the development of Linxia's national economy, especially the non-public sectors of the economy.

The questionnaire is design for the informal credit conditions in Hui autonomous prefecture of Linxia, and analyzed the income of loaner and borrower, reason of credit, and the period and interest rate of credit separately to understand the current situation and existing problems in the local informal financing. Totally, more than 500 questionnaires were sent out, covering the city, urban and rural regions. Through the form such as field research, document consulting, and news searching, the investigation is lasting for seven days.

Facing to the development status of informal credit in Hui autonomous prefecture of Linxia, through field research, we know the characteristics and existing problems in the development of informal financing in this region, to hope put forward the countermeasures, and lead the standardization development of this region's informal credit.

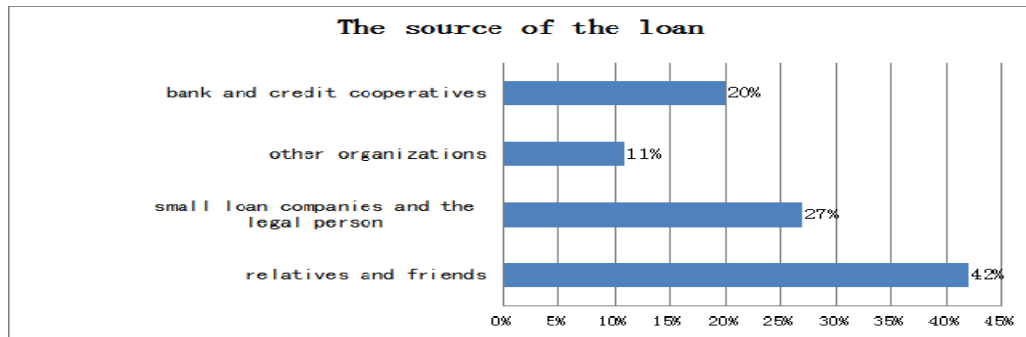
2. The Present Situation and Characteristics Analysis of the Informal Credit

2.1 The Understanding of Informal Credit

The generalized informal credit refers the credit behavior without the formal financial institution in the society, it also can be called the informal finance outside the system, and the narrow sense of informal credit refers credit activities between individuals, and it's pretty confusing in part. According to the judicial interpretation of Supreme

People's Court: Informal credit is the behavior of credit between people, citizens and legal persons, citizens and other organizations. These definitions are reflected some characteristics of informal credit: informal, simple procedure, low cost, flexible interest rate on the high side, and high risk.

Through the investigation by questionnaire, the significant data shows that the people in Hui Autonomous Prefecture of Linxia has a very limited understanding of informal credit, most people agree with personal loan belongs to the folk, then it's a type of informal credit that borrow from small-scale loan company and legal person. And still have 20% of people think that borrowing from commercial banks, credit cooperatives belongs to informal credit. In fact, the credit behavior from the formal financial institution is not informal credit; therefore, it is ambiguous on the understanding as shown following.



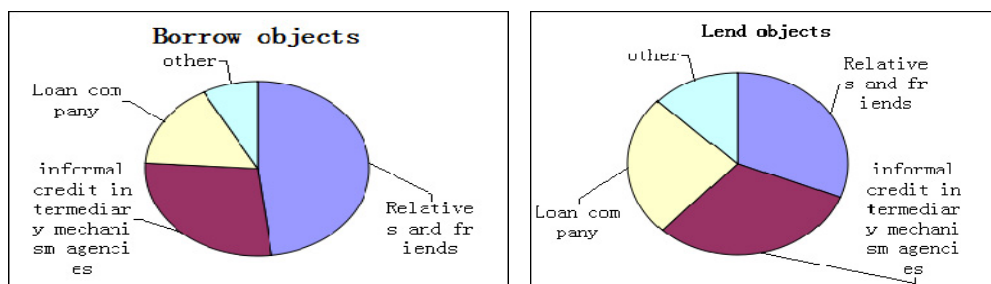
2.2 Participation and the Dispute in Informal Credit

The investigation showed that 51% of the respondents had never been involved in informal credit, 49% of the respondents involved in informal credit. It can be seen from the data, the degree of participation of non-governmental financing is pretty high, the participant has a considerable scale.

The survey data showed that 92% of respondents think that the disputes has been happened in the informal credit, and only 8% of respondents think that there is no dispute in this activity.

2.3 The Active Characteristics of Loanees and the Loaners in Informal Financing

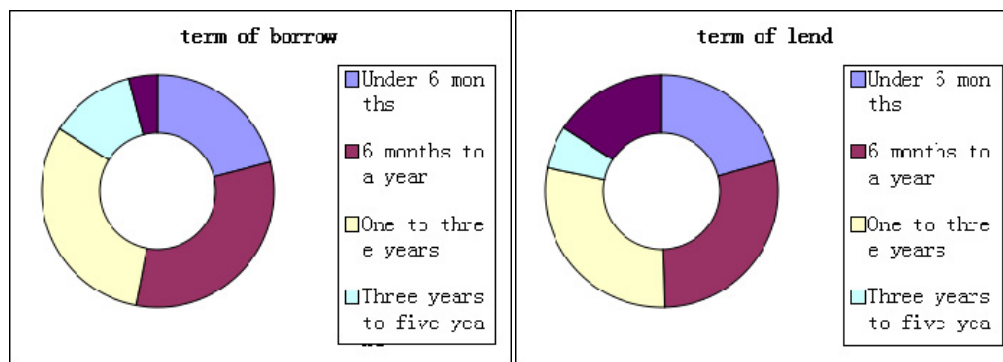
During the survey, we found that the people who was loanee is in the majority, and it accounted for 59%; the people who was loaner is in the minority, and it accounted for 41%. The 48% of the loanees would borrow from relatives and friends, and the people who choose to lend money to friends and relatives accounted for 31% of the total. We think the reason for the choices are the trust among Chinese is based on relationship, blood relationship, and friendship, people tend to borrow from their relatives, friends, because they know each other, there is a high credit between each other, and it is more likely to success; of course, there still has some people to choose borrow from informal intermediaries, and it accounted for 28% of the total, the people who lend to intermediaries accounted for 31%. And according to the visit, the most of alleged informal intermediaries are small local organizations, and loaning from the informal intermediaries has a simple procedure, and a low cost. The people who loan to informal intermediaries thinks the interest is higher than bank or deposit financial institutions, etc, and can get some interests from the spare money, what's more, this kind of credit behavior belong to the short-term and medium-term loans, there almost have no long-term loan, therefore, it is safe and reliable in the case of have certain formalities; but the people who borrow from loan corporation accounts for only 16%, the people who lend to loan corporation accounts for 25%, this kind of loan company have complicated procedures and high threshold, usually need some guarantee to borrow, and it also have certain stipulation of guarantee, and most of the loan behavior belong to the mid-term and long-term lending, considering the basic situation of Hui Autonomous Prefecture of Linxia, we think such loan is minority in the local. Though it is, it could get considerable earnings in this way; of course, there is some people choose other way of financing, but accounts for only 8%. The people who lean to other credit also accounts for only 13%.



In the flourishing informal credit activities, most of that belongs to unsecured loans, which the unsecured borrow accounted for 55% of the total proportion, and unsecured lend is accounted for 70%. The reason is that the most people borrow or lend money to relatives and friends, informal credit is not operated on the basis of the official framework, it formed a trust foundation base on geography, kinship, friendship and relationship, etc. and then it carried out organized or interdependent financial activities among individuals. Borrowing among individuals is debtor-creditor relationship which formed with the civil contract relationship among residents and individuals, there is no strict legal contract generally, it is usually in the form of written and oral, and a third party is involved in witness and reached a lending agreement. Generally adopt unsecured loans.

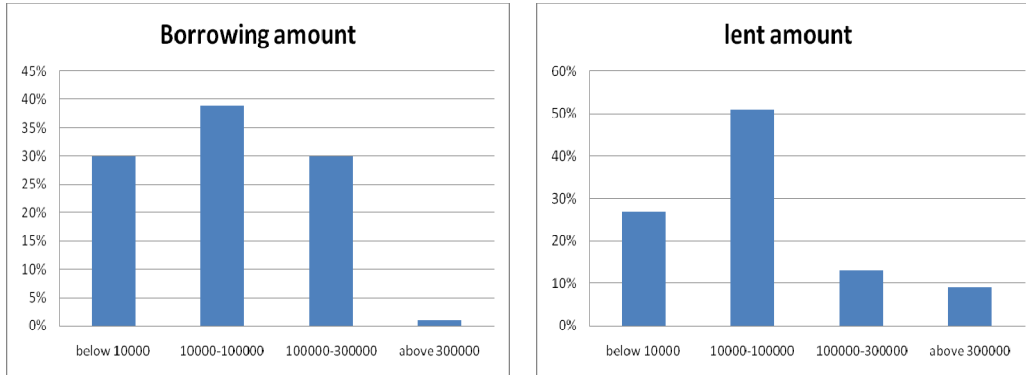
In the above borrowing behavior, the borrowed money has plenty of purposes, and the people who choose to buy a house is in the majority, reached about 30% of the total, at present, it needs huge money to afford a house, common family is difficult to purchase demands rely on their own financial resources, so based on the purpose of buying a house, a lot of people will choose to private lending. Because this group choose the survey area in Hui Autonomous Prefecture of Linxia, where there is much people doing business and develop by themselves, so, 18% of people borrow money for the productive cycle. Nowadays, it has become a common problem of expensive and hard to visit doctors, so 18% of informal credit is for medicinal purposes. There is also part of the people to borrow money to their Children's school fees. The costs of undergraduate, graduate, doctoral or studying abroad are huge costs for ordinary families, so 8% of people choose to use informal credit to solve this difficult. And 8% of people choose to borrow for finance investment, people choose this kind of choice think manage money matters have highly profitable and it could offset the borrowed money and the corresponding interest on a loan, it is a good way to make money. To borrow money for other purposes accounted for 18%. And 42% of lend money is designed to help friends and family, the purpose of this kind of lending activity is very common in our daily life, and lend money to friends and relatives, its purpose is for its solution. 41% of people choose to earn profits; the interest of informal credit is higher than banking institutions, so it is a way of earning money of lots of people.

Because the purpose and the way of the borrowing is different, borrowing period is also different. Choose to borrow deadline under 6 months accounted for 21%, 6 months to a year accounted 32%, the most of its purpose is revolve cash or emergency. And the most people choose this lend term lend money to friends for emergency or lend money to informal intermediary organization, the above-mentioned deadline all belong to short-term lending activities. The people choose borrow one to three years accounted for 31%, three years to five years accounted for 12%, the people choose to lend for the two class periods accounted for 29% and 6% respectively, most of the people choose that borrow money from relatives and friends. But because of the economic income, the people would lend money for three years to five years accounted for only a few people. And the people who choose to borrow more than 5 years accounted for only 4%, most used in the large spending such as house-purchase. And the people lend money for five years or above accounted for 15%, and most of that lend money to the lending institution, because that could get interest income, it is equivalent to financial investment.



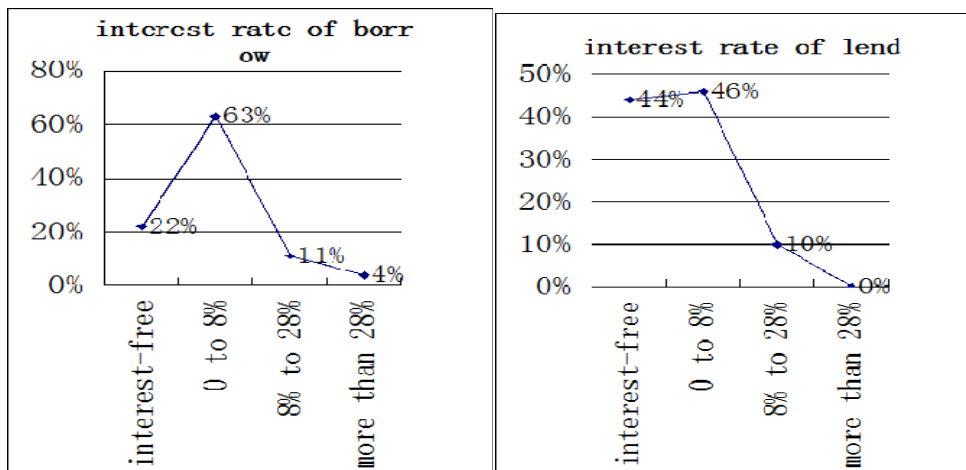
This investigate found that in Hui Autonomous Prefecture of Linxia, lots of lend activities occur among relatives and friends, the amount of lending to each other has a lot of restrictions due to the condition of lenders' family in this kind of way, the amount of borrowing and lending within 10000 Yuan, accounts for 30%, 27% respectively, the amount of borrowing and lending between 10000 to 100000 Yuan accounts for 39%, 57% respectively. When borrowing from relatives and friends should consider whether the economy can afford what money you borrowed, and lenders are also need to consider their own economic strength to proceed lending activities. The people choose to borrow money between 100000 to 300000 accounted for 30%, 13% respectively, most people choose borrowed such large amount to buy houses and other large consumer spending, and the most ordinary lenders can't afford, so this

amount of lending is significantly reduced. The people choose lend or borrow 300000 accounted for 1% and 9%, respectively, the borrower in this limit interval is very few, everyone will consider their repayment ability, as a last resort, many people won't choose the amount of borrowing in the interval. And if someone has the ability to lend the money, would choose to lend money to that most reputable informal credit mechanism, so that he can get higher interest income than bank.



State has its definite provisions about informal credit: interest rate of informal credit shall not exceed four times of the highest bank lending rate at the same time, the two sides could negotiate in the condition of the interest rates within four times of bank loans in the same time, which can be summarized as it is legal when the interest rates within four times of bank loans in the same time, and it belong to the usury when the interest rates more than 4 times, the part of the usury are not protected by law. The rules of individual-to-individual lending activities is: at normal state, the borrowers could get capital once they found credit intermediary and reach an agreement, the annual interest rate of this kind of credit is usually 15% 20%, lower than four times of the current benchmark interest rate stipulated by the people's bank, belong to the category of protected by law.

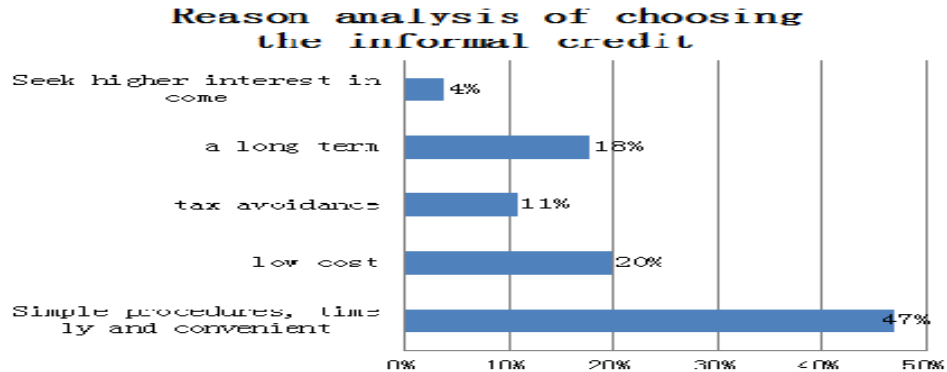
From the data we got form this investigate, it is almost belong to the interest-free loans which used to lend to relatives and friends, so the interest-free loans accounted for 22% and 22% respectively. The interest of lending and borrowing money from informal credit institutions is between 0% and 8%, and the loans in this interval accounted for 63% and 63% respectively, this interval is acceptable to both sides. and interest between 8% and 28% makes borrowed feel a lot of pressure, the borrowers in interval accounts for only 11%. Lenders accounted for only 10%, because agencies also don't want to appear too much high interest savings. The interest rates more than 28% belongs to usury, and it won't be protected by the state, so that lenders won't lend easily, so this interval is 0%, and the borrowers have no alternative but borrowing this usury of this interval of interest, but the number of less, only 4%.



2.4 The Agreement Form and Reason of Choosing the Informal Credit

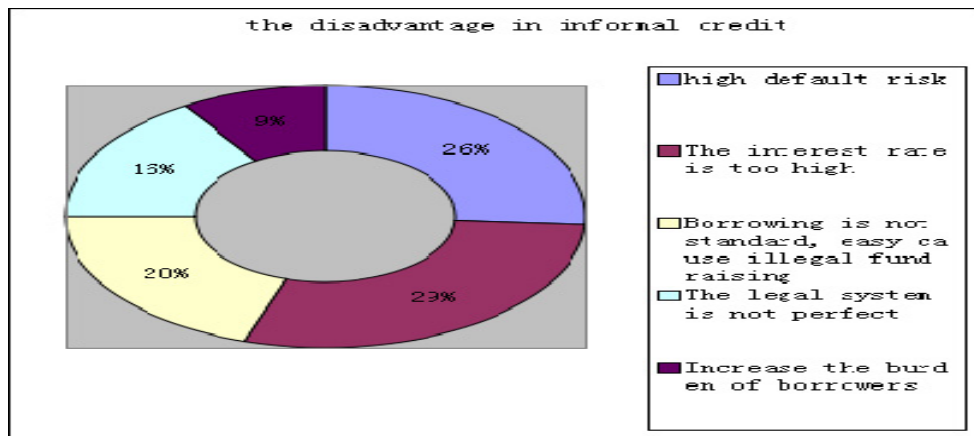
In this investigate, 30% of the respondents tended to choose oral agreement, 70% of the respondents would choose to sign a written loan agreement. Can be seen from the data, the legal consciousness of both sides in informal credit is not very strong, it tends to produce more debt disputes for the small percentage of the oral agreement.

The investigate shows that 47% of borrowers choose it cause of the simple procedure of informal financing, convenient and in time, while 20% of borrowers think the cost is low, and then is its longer term and tax avoidance, only 4% of borrowers think informal financing can be better used to reasonable tax avoidance.



2.5 The Analysis of the Disadvantage in Informal Credit

In the investigation, the participants of informal credit think the interest rates of informal credit and default risk is too high, and the borrowing is not standard, 16% of respondents believe that the legal system is not perfect, only 9% of borrowers think informal financing increased the burden of the borrower.



3. The Reason Analysis of Activity of Informal Credit

3.1 The Needs of Economic Development

With the development of commodity economy and the reform and opening up, Chinese informal credit gradually developed. The lending standard of formal financial institutions is high, so it cannot fully meet the demand of social capital, and the imbalances of capital supply and demand stimulate the development of the informal credit. Because China has a very strong sense of kinship, and mutual understanding and trust has been established between friends and relatives, which makes informal credit established on the basis of individual credit gradually active, and the lower transaction costs has been favored by the borrower. So, despite the informal credit has not obtain legal status in China, it will boom with the development of economy.

3.2 The Procedure Is Simple, and the Term Is Long

In order to ensure the stability and safety of the financial system, almost all formal financial institutions will strictly control lending, deposits-loans surplus in each commercial banks are pretty big, the problem of loan is difficult has gradually become a social problem. Whether in the production and operation, or in the event in life such as weddings, children education, build or cure, etc. The people in Linxia city undertook the great fund pressure, they need borrow, and nearly half of the informal financing needs shows its importance. It is because of the informal financing has its own unique advantages that allows it complement the blank of the formal financial financing market. The formal credit has the advantage of simple and convenient procedure, small amount, flexible operation, and long deadline, which makes the small enterprises, individual businesses and farmers adjust the funds more easily. Compared with the bank credit, the informal credit avoid the tedious credit check procedure, don't need higher guarantee. At the

same time, some informal credit occurred among friends and relatives, interest-free loans are also common, this way of low cost of financing, also have the necessity of its existence.

3.3 The Assist of Informal Credit

In the survey, we found that the large part of borrowers in informal financing is informal intermediary. The intermediary link capital demanders to providers, but they are different from small loan companies, low risk and high yield make it a vast living space. In the assistance of informal intermediary, borrowers can fully access information to each other, avoid the determination in information asymmetry, and also accelerated the flow of social capital, solved the problem of lenders lack of professional knowledge and law, optimize the allocation of resources. The existence of informal intermediaries make substantial basis for the prosperity of the folk financing.

3.4 The Guidance of Credit Environment

At present, Chinese commercial Bank lending capacity cannot fully meet the demand of social capital; part of the commercial bank loan has been negative, high loan approval condition and the complicated approval system added to the problem. This series of credit macro environment increased the difficulty of financing, make it impossible for small and medium-sized enterprises, individual businesses and farmers to get loan. As for the farmers, small and medium-sized enterprises, individual household who in urgent need of money and without high quality guarantee is hard to borrow money. In the face of such situation, informal credit began to gradually come into being. In some way, informal credit is a supplement to the formal financial, and it is the credit environment since continuously guide and development.

3.5 The Drive of Benefit

At present, Chinese financial market is not developed, for the individual with limited funds and without financial products investment philosophy; it is a good choice to lend money from informal borrowing intermediary. The informal lender, can get higher than the bank deposit interest income, and avoid the high risk of securities investment. Some speculators also raise a larger capital to invest and make a profit through informal credit.

3.6 The Needs of the Small and Medium-sized Enterprises

For private small and medium-sized enterprises in China, the enterprise is at the early stage of development, with the huge capital demand and thin margins, they would choose the informal financing to improve the company's financial leverage and reasonable tax avoidance, so they could expand the size of the power of life. However, the threshold of financing institution such as commercial bank is high, and come into the Growth Enterprises Market is difficult, so, the informal credit is become their better choice.

3.7 Legal and Financial Supervision Is Weak

Most informal credit is very hidden, and the supervision is weak, and in the " some opinions of Supreme People's Court borrowing case" law to private credit norms is also very limited. Therefore, private credit has its own development space and flexibility.

4. The Problems Existing in the Development of Informal Credit

4.1 The Borrowing Is Not Standard, and the Interest Rate Is High

Informal credit procedures are simple, but it lack of necessary management and support by laws and regulations, it is blind, not normative, unstable, what's more, it is easy to cause borrowing debt disputes between the two sides and have a negative impact to the society. They recover loan by violence once informal credit in the event of not repaying debt and it brings danger to the both sides. There arise some dun company with gangdom in folk, part of the folk loan use for gambling, drugs and other serious violations, a bigger threat to society.

4.2 The Informal Intermediary Is Not Standard

At present, different regions in China appeared the behavior of informal intermediary deceives the borrowing individual frequently, and this dispute over obligation is common in Hui Autonomous Prefecture of Linxia. Part of the informal intermediaries defrauds the lender who has idle funds, and they cannot preserve the safety of the funds. High-interest informal lending interest rates, once the interest rates four times higher than bank interest rates, borrowing behavior are illegal, and not protected by law.

4.3 Default Risk Is High, and It Is Easy to Bring Illegal Fund-raising Fraud and Other Problems

Due to the lack of folk financing and financial regulation by law, there might be a lot of legitimacy and even illegal behaviors, and it does serious harm to the social order and social stability. It is difficult to control that the investment

direction of informal financing accumulation fund, some still have a tendency to "violate national industrial policy", and it is easily to lead the problems such as illegal fund-raising fraud. Based on personal credit of the informal borrowing behavior is lack of financial guarantee, the risk of default is more higher than other financing ways, the debt disputes also is unable to avoid.

4.4 Increased the Burden of Operators, Contribute to the Existence of Usury, and Destroy the Normal Financial Order

Interest rates of many small and medium-sized enterprises or individuals borrowed money form informal capital are generally higher, and it is up to 3-4 times higher than the same period bank interest rates. High interest rates, on the one hand, increase the operator's financial burden, form a vicious circle, and it's bad for the healthy development of private economy and individual economy; on the other hand, it leads to the existence of usury, produced a part of the rentier class in society.

4.5 Credit Risk Is Difficult to Control

Firstly, the most basic of credit system is relatives, friends, acquaintances, but with the development of market economy, borrowing range has been far beyond the range of this relative network, so this kind of trust mechanism becomes more and more fragile, prevention for risk is becoming more and more unreliable. The second is the speculation, sensationalization factors further raised lending rates, increased the risk of default, to a certain extent, the worse is it could bring chain reaction easy once the bubbles burst.

4.6 Law Is Imperfect, the Legislation Lagged behind the Social Practice

Relevant laws and regulations refer to "general rule of civil law", "property law", "guarantee law", "contract law", "criminal law" and "suppress method for Illegal financial institutions activities", "general rules" and other laws and regulations, exposed imperfection of fragmentation, and make informal credit wandering in the gray area outside the formal financial system; then, reasonable and normal informal credit has mixed up with illegal fund-raising, fraudulent fund-raising and other illegal and criminal activities, there is no clear legal guidelines to distinguish, free between legal and illegal; what's more, there is almost no judicial guidance for the all kinds of new forms and patterns in informal credit.

4.7 Regulation Does Not Reach the Designated Position

Informal credit would not be supervised by the special regulator such as CBRC, CSRC, and CIRC, so its slowly expansion and modification does not cause the government's strong concern at first, each time only when the situation is relatively serious will government take strict measures to punish. Released in March 2011 "Interim Procedures for financing guarantee company management" is formulated by CBRC, NDRC, MIIT, ministry of finance, Ministry of Commerce, People's Bank of China, SAIC seven departments altogether. Regulation subject is too diverse, make fuzzy real supervision subject, daily supervision, in fact, is in the vacuum state.

Informal credit is a kind of underground finance, its non-public mode of operation make it unclear that the capital source and flow direction, the overall lending interest rates, credit risk, such as information, so, it is hard to supervise. In addition, with the innovation of the mode and expansion of the scope of business those years, there is no such legal guidance, make it almost in a blank area of regulation.

5. Countermeasures and Suggestions to Promote the Development of Informal Credit

5.1 For the Government and the Financial Supervision and Regulation Department

1) The government should formulate reasonable informal credit rules and method, guide the informal credit practices correctly. According to the present development trend of informal credit, countries or related department should establish more perfect informal credit laws and regulations as soon as possible to regulate and protect normal informal credit practices, lead informal credit to the normal orbit. And they should also punish and outlaw the usurer who take advantage of others precarious situation to make high profits at the same time to maintain the social stability.

2) The government should improve the investment environment practically, to encourage and guide non-governmental capital investment directly. The government should increase the intensity of investment system reform, establish the core mechanism of conversion between saving and investment, speed up the development of capital market, broaden the channels for civil society capital access the investment field smoothly, and remove obstacles. The government should also accelerate reform of the financial system; provide a full range of financial services for different ownership economic subject.

3) The CBRC should earnestly shoulder the responsibilities of supervising finance, standardize the behavior of informal credit. Financial regulators should make strict regulations to give informal finance some legal status, especially strengthen supervision to the spontaneous organized financial activities in order to avoid "financial storm"; and determined to protect legitimate loan activities at the same time to safeguard the legitimate rights and interests of creditors. Must let some rural informal finance, folk finance appeared during procession of reform and improve the formal financial.

4) Strengthen citizens' concept of credit, guide the healthy operation of informal credit. Only strengthen the education of citizens' concept of honesty and credibility, awareness of investment risk, can make whole society form a good atmosphere of honesty and trustworthiness, to reduce the occurrence of dispute, it is system engineering, and is also a social problem.

The first is to strengthen the demonstration effect of cases trial, they should Invite all sectors of society audit when they judge the typical case, and judge case on the table in the case focused areas to let more people attend and explore the case to learn a lesson from that; in view of new features of the borrowing cases at the same time, report to the superior court and the party committee, National People's Congress timely and advance judicial Suggestions to the government to cause their attention. Set up credit information collection agencies, establish special collection system, release authoritative information to the society in time, and release risk early warning to improve citizens' risk consciousness and avoid business risk by this education to effectively reduce the occurrence of such cases. The court should strengthen communication and coordination with related functional organization while trialing this kind of case, the whole society should make concerted effort to manage together, can we truly achieve the effect.

5) Strengthening the management of interest rate, regulate informal credit further. People's Bank of China, China Banking Regulatory Commission, and business administration departments and so on should strengthen the management of informal credit, Allow to carry out the informal credit within the scope of reasonable interest rates, punish several usury behavior sharply, especially the village leader participates in the usury behavior, the government should investigate seriously to maintain social stability and financial order.

6) Increase the intensity of financial reform, sunlight the informal financial mechanism. Governments and financial mechanisms should increase the intensity of financial reform; they should establish the timely and effective market exit mechanism according to the market-oriented principle. They should allow to set up new financial organizations, while close the poor financial institutions, should allow to set up a new voluntary, mutual cooperative financial organizations in particular such as small loan companies, financial support, credit collaboration, etc., and can consider setting up private bank when conditions are ripe, exploit a way for informal capital step into financial industry legally by the system, give those who want to start lawful operation a legitimate way.

5.2 For the Financial Service Department

Financial departments should raise funds actively, and raise the service level. The Financial mechanism should make efforts to improve service levels, provide residents with simple and quick deposit service by modern technology. The credit funds of each state-owned commercial bank should meet the reasonable fund needs of local economic development properly while inclining to large and medium-sized enterprises or large projects to relieve the contradictions of capital supply and demand. The financial departments should create conditions, expand financing market actively, create conditions for direct financing for the enterprise to standardize enterprise behavior, and provide reliable financial conditions for the investors grasping the direction of investment correctly as well.

5.3 As for the Individual Participants of Informal Credit and the Small and Medium-sized Enterprise

1) Choose informal credit intermediary mechanism carefully. First of all, they should choose a high credit intermediary mechanism as far as possible, and has a long operating time and lots of successful cases, and must require intermediary mechanism only provide the work of consult, pair and joint, could not handle customers' funds. Secondly, lenders should participate in the whole lending process pellucidly to prevent funds put into Illegal purposes. Finally they must take some necessary guarantee measures, such as house property mortgage, etc.

2) Strictly prohibit usury. For the participants of informal credit, they should not indulge the usury for personal benefits, because this not only break the law, but also do harm to the security and stability of society. During the usury, the lenders' found cannot be protected by the law, they will be punished instead.

3) Avoid debt disputes, clear the funds' allocation. The individual of informal credit should lend money carefully, clear the allocation of funds, and should pay special attention to the long-term and high-risk investment, cannot break the law to get personal interests, and finally affect social stability because of debt disputes. As for the borrowing behavior established between relatives and friends, participants should treat more rational rather than blind

4). Small and medium-sized enterprises should be careful to borrow money. During the process of small and medium-sized enterprises' informal financing, they should consider the company's financial situation cautiously; use the money in a planned way to prevent the debt crisis.

6. Conclusion and Implications

Through investigate and analyze the situation of informal credit in Hui Autonomous Prefecture of Linxia, investigate the problem in the development of informal credit; and put forward the strategy to promote the development of informal credit. Based on the above analysis, only take the effective guidance measures could the informal finance serve the real economy better, and play its due contribution to the economic society.

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