POLICY PAPER

The Architecture of Global Finance: Opening with Control

A Framework for Financial Opening with Stability: Policy Design Ideas for China's Pilot Zones

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By Sidney Shauy, MBA (帅緒堂)

Author, Wall Street for Global Investors | Risk Management & Deivatives Markets | RISP 500 Algorithm & Risk Index | US-BRAZIL-CHINA G3 Global Macro Allocator

ABOUT THE AUTHOR*: Sidney Shauy, MBA (Wharton School, University of Pennsylvania), BEng (Universidade de São Paulo), is a Wall Street veteran with over 30 years of experience at Citigroup, Morgan Stanley, JPMorgan Chase, ABN Amro, Lloyds Bank, and BBVA, spanning New York, São Paulo, Hong Kong, and Madrid. He is the founder of Risk Scientific LLC, developer of the SMIGRM risk management and RISP 500™ Risk Indicator & Algorithm, and the G3 Macro Allocator (US-China-Brazil) framework. Author of five books including Wall Street for Global Investors. Taiwan-born of mainland Chinese parents, lived in Brazil/USA.*

E-mail: sidneyshauy@qq.com | WeChat: sshauy

EXECUTIVE SUMMARY

Drawing on over three decades of experience across global financial markets, I have had the unique opportunity to observe firsthand the dynamics of financial crises in both emerging and developed economies. Having lived through Brazil's hyperinflation and volatile cycles in the 1990s, as well as major global events including the dot-com collapse, the 2008 Great Financial Crisis, the European sovereign debt crisis, and the 2020 pandemic-driven market shock, I've drawn important lessons from each and every crisis that devastated societies, especially the poor.

These experiences shaped my perspective on one of the most important questions facing China today: **how to deepen financial openness and attract global capital without compromising stability and policy control**.

This policy paper offers a structured approach to that challenge. It combines lessons from international experience with a set of original frameworks—including a **rules-based system for managing capital flows (ACFF), a real-time experimental model using China's Pilot Zones (FTZ) as financial laboratories, and measurement tools to guide policy sequencing and assess readiness**.

The objective is not to advocate for rapid liberalization, nor to preserve rigid controls, but to propose a middle path: a **system in which openness is engineered, risk is continuously monitored, and policy responses are predictable, transparent, and adaptive**.

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1. IS IT POSSIBLE TO OPEN WITHOUT LOSING CONTROL?

China is entering a new phase in its financial evolution—one defined not by growth alone, but by the ambition to integrate more deeply into global capital markets.

For decades, China's development model has balanced global integration with domestic control. This approach has delivered extraordinary results: sustained growth, vast foreign exchange reserves, and a financial system that expanded in scale and sophistication without experiencing the recurring crises seen in many emerging markets.

But success has created a new objective. China is no longer focused solely on exports and industrial expansion. It is increasingly seeking to deepen its financial markets, attract foreign capital, and elevate the international role of the renminbi. Initiatives such as expanding cross-border investment channels, opening bond and equity markets, and developing alternative payment systems all point in the same direction: **greater financial integration with the world**.

Yet this ambition is carefully qualified. China is not pursuing openness at any cost. Access is expanding, but through structured channels. Capital inflows are encouraged, but remain monitored. The renminbi is gradually internationalized, but not fully left to market forces.

This reflects a consistent principle:

Openness is desirable but only if it preserves stability, policy autonomy, and strategic control.

This principle defines the central challenge ahead. To become a global capital destination, China must deepen market access and build investor confidence. But the same forces that attract capital in favorable conditions can reverse quickly under stress. Without the right structure, financial openness can amplify volatility and weaken the very stability that enabled China's rise.

The question, therefore, is not whether China wants global capital—it clearly does. The real question is:

Can China open its financial system further without importing the instability that has accompanied financial liberalization elsewhere?

To answer this, we must first understand what China is trying to avoid.

2. RISKS OF LOSING CONTROL ARE REAL

China's cautious approach is often misunderstood as reluctance to embrace openness. In reality, it reflects a clear understanding of the risks that can emerge when openness is not properly structured. These risks are not theoretical. They are well documented across countries that liberalized capital flows without adequate safeguards.

At the forefront is the risk of **capital flight**. In an open system, shifts in expectations—driven by domestic developments, global financial conditions, or geopolitical events—can trigger rapid and large-scale outflows. What appears stable can change quickly when confidence weakens, forcing policymakers to respond under pressure.

Closely related is the risk of **exchange rate instability**. Volatile capital movements can drive sharp currency appreciation during inflow periods and abrupt depreciation during outflows. These swings complicate monetary policy, affect inflation dynamics, and introduce uncertainty for both domestic and international participants.

A third concern is **financial system exposure**. Capital flow volatility can propagate through banks, non-bank institutions, and corporate balance sheets, creating feedback loops that amplify stress. In a system as large and interconnected as China's, such dynamics are difficult to contain once they take hold.

There is also the issue of **pro-cyclicality**. Capital tends to reinforce economic cycles—expanding during periods of optimism and reversing during downturns. Without countervailing mechanisms, this dynamic can intensify both booms and contractions.

Finally, greater openness raises questions about **policy autonomy**. As capital mobility increases, domestic financial conditions become more sensitive to external factors. Interest rates, liquidity, and exchange rates are increasingly influenced by global forces, potentially constraining policy flexibility.

Taken together, these risks define China's core constraint:

The objective is not simply to open—but to open without losing control over the stability of the financial system and the direction of economic policy.

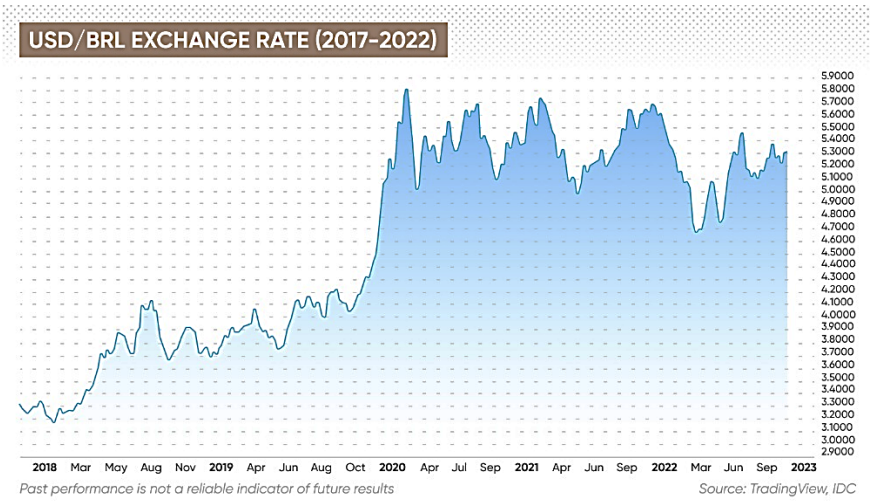
This makes financial liberalization a **sequencing problem** rather than a single decision. Each step must be aligned with the system's capacity to absorb and manage risk.

China's current approach reflects this logic. Access is expanded gradually, channels are structured, and flows are monitored. This has helped China avoid the types of disruptions seen elsewhere—but it also raises an important question.

What happens when openness moves faster than the system's ability to manage it?

To answer that, it is useful to examine a contrasting case—one where openness came first, and stability proved much harder to sustain.

3. BRAZIL: WHEN OPENNESS OUTRUNS CONTROL



I'd like to bring the Brazilian experience to this discussion because I personally experienced it firsthand. My family emigrated to Brazil when I was 5 years old. I grew up in the country and experienced hyperinflation in the 80s, emerging markets crises in the 90s while managing risks of billion-dollar portfolios, and later in the U.S., the 2008 GFC, 2009 EU Debt Crisis, the 2020 Covid Crash, the 2025 Tariff War Crash, etc. From my life experiences across 30 years in the markets, I have important lessons to share with the motherland as a small contribution, hoping she will develop a smoother path toward a bright future. Over 15+ years, I developed a proprietary risk management system called SMIGRM, a risk indicator (RISP 500), and I'm still developing a US-Brazil-China Macro Allocator for global investments based on macro variables. Here, I want to start with the Brazil experience as a contrasting model.

If China's approach reflects caution shaped by risk awareness, Brazil offers a contrasting experience—one that illustrates what can happen when financial openness advances more rapidly than the system's capacity to manage its consequences.

Over the past several decades, Brazil has broadly followed a model aligned with global financial orthodoxy: an open capital account, a floating exchange rate, and deep integration with international markets. In principle, this framework offers clear advantages—efficient capital allocation, access to global savings, and strong price discovery.

In practice, however, the experience has been highly cyclical. Periods of global liquidity—often associated with easing cycles from the Federal Reserve—have historically driven significant capital inflows into Brazil. These inflows strengthen the currency, compress risk premia, and support asset prices. Financial conditions loosen, credit expands, and growth accelerates.

Yet these phases are frequently followed by sharp reversals. When global conditions tighten or risk sentiment shifts, capital flows can quickly reverse direction. Outflows place pressure on the currency, financial conditions tighten, and inflationary risks emerge. Policymakers are then forced to respond—often through higher interest rates, foreign exchange intervention, or fiscal adjustment—precisely when economic conditions are already weakening. The result is a recurring pattern:

Capital flows amplify economic cycles rather than stabilizing them.

Several structural features reinforce this dynamic. Brazil's openness allows capital to respond rapidly to external conditions, often independent of domestic fundamentals. Shifts in global interest rates, investor sentiment, or commodity prices can trigger large movements of capital. The country's exposure to commodity cycles further intensifies this interaction, linking external shocks directly to domestic financial conditions. Over time, this has contributed to a system characterized by:

- pronounced exchange rate volatility
- persistently high interest rates
- unstable investment horizons
- alternating periods of expansion and stagnation

Brazil has developed credible institutions, including an inflation-targeting framework and an independent central bank. Its markets are liquid and accessible, offering clear price signals and ease of entry and exit for investors.

These are important strengths.

But the Brazilian experience highlights a critical limitation:

Openness, in the absence of mechanisms to manage volatility, can introduce instability rather than reduce it.

This is not a failure of markets, but a limitation of system design. Capital does not inherently stabilize economies. It follows incentives, expectations, and global conditions—often reinforcing trends rather than counteracting them. The contrast with China is therefore instructive.

- Brazil demonstrates the advantages—and risks—of openness
- China demonstrates the advantages—and constraints—of control

WHERE EACH COUNTRY SITS TODAY

Dimension	Brazil	China
Openness	High	Medium
Stability	Low–Medium	High
Efficiency	Medium	Medium–Low
Control	Low	High
Global integration	High	Rising

Neither model is sufficient on its own. What emerges from this comparison is a more fundamental insight: **The challenge is not whether to open or to control—but how to design a system that can do both.** If neither full liberalization nor strict control offers a complete solution, what would a system look like that reconciles the strengths of both?

4. BEYOND THE IMPOSSIBLE CHOICE: CAN A COUNTRY BE OPEN AND STABLE?

The contrast between China and Brazil highlights a long-standing assumption in global finance: that countries must choose between openness and stability. On one side lies openness—associated with efficiency, liquidity, and global integration, but often accompanied by volatility and exposure to external shocks. On the other lies control—associated with stability and policy autonomy, but typically at the cost of reduced market dynamism and limited capital participation. This framing, however, is increasingly insufficient.

It treats openness and stability as mutually exclusive outcomes, rather than variables that can be jointly managed through system design. The experiences examined so far suggest a different conclusion:

The outcomes of financial openness are not determined solely by the degree of openness, but by how the system is designed to handle capital flow dynamics. This shifts the problem from one of policy preference to one of financial engineering.

Financial systems do not operate under static conditions. They evolve through phases—periods of stability, rising stress, and, at times, dislocation. A system that applies the same rules across all conditions—whether fully open or tightly controlled—lacks the flexibility to respond effectively.

In contrast, other areas of finance already incorporate adaptive mechanisms. Equity markets use circuit breakers to contain extreme volatility. Banking systems apply counter-cyclical buffers to strengthen resilience during expansions. Risk management frameworks adjust exposures dynamically as conditions change.

These systems share a common principle:

They do not eliminate activity—they modulate it in response to risk.

Capital flows, however, remain largely governed by **static regimes** across the world.

In open systems, they move freely regardless of conditions. In controlled systems, they remain restricted regardless of conditions. When stress emerges, responses are often discretionary, reactive, and introduced under pressure—creating uncertainty about both timing and magnitude. This uncertainty can itself become destabilizing. Investors cannot anticipate how policy will evolve, and may adjust behavior abruptly in response to perceived risks of intervention. In this sense, unpredictability can amplify the very instability policymakers seek to avoid.

The issue, therefore, is not whether capital should be free or controlled. The more relevant question is:

How should capital flows behave under different states of the system?

This reframing opens the possibility of a different type of financial architecture—one in which openness is preserved under normal conditions, but complemented by structured, pre-defined responses as risk increases.

Such a system would not rely on discretionary intervention. It would be based on measurable indicators, transparent thresholds, and proportional responses. Capital would remain mobile, but its impact on stability would be managed through design rather than restriction.

This is similar to the core principle in SMIGRM – the risk management-based system for equity investments I developed, though I'm not the inventor or the only practitioner to use similar systems. Unlike the traditional investing methods based on portfolio management using diversification to face all types of environment (bull, bear, volatile, range, etc.), SMIGRM uses risk information to tactically rotate assets to match risk environments. It's the same idea: ***measurable risk indicators, pre-set thresholds, and appropriate responses to risk fluctuations as market action unfolds****. Instead of depending on correlation inside a portfolio of diverse assets to hold at all-times (which they don't), SMIGRM dynamically matches the best-performing assets to the risk context.*

For China, I believe this perspective is probably particularly relevant.

The country has demonstrated that stability can be preserved through structured control, while also signaling a clear intention to expand financial openness. The next step is not simply to relax existing constraints, but to introduce **mechanisms that allow openness to evolve without compromising control**. This requires moving beyond static frameworks toward a system that is both **predictable and adaptive** - a system in which:

- capital flows freely when conditions are stable
- friction is introduced gradually as risks rise
- stronger safeguards are activated only under clearly defined circumstances

Can such a system be constructed in a way that is credible, measurable, and operational? That question leads directly to the next step:

What would a system look like that embeds these principles into the structure of capital flow management itself?

5. THE ACFF FRAMEWORK: ENGINEERING OPENNESS WITHOUT LOSING CONTROL

If the challenge is to reconcile openness with stability, the solution must move beyond principle into system design. The question is no longer whether capital should be free or controlled, but how to construct a system in which capital moves efficiently under normal conditions while its destabilizing effects are contained as risk rises. This requires shifting from static regimes to what can be described as **state-dependent capital mobility**.

In such a system, openness is not fixed. It changes with conditions. When financial environments are stable, capital flows with minimal friction. As pressures build—through exchange rate volatility, shifts in global liquidity, or accelerating cross-border movements—the system responds in a measured and predictable manner.

Capital is neither fully free nor permanently constrained—it is modulated in response to measurable risk conditions and according to transparent thresholds

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For this approach to function, however, it must be grounded in **quantification**. This can be achieved through a composite indicator—a **Capital Flow Systemic Risk Score**— which aggregates signals across key dimensions of the system, including currency dynamics, capital flow velocity, reserve changes, and broader market stress. The role of this score is not to predict crises, but to identify transitions: moments when stability begins to give way to pressure.

Capital Flow Risk Score (CFRS)

A composite score (0–100) based on:

- FX volatility
- Capital flow velocity
- FX reserve drawdown
- Offshore/onshore spread
- Cross-border funding stress
- Market stress indicators

Regime Classification

CFRS	Regime	Interpretation
0–30	Normal	Stable
30–60	Elevated	Early stress
60–80	High Stress	System pressure
80–100	Crisis	Tail risk

These transitions define thresholds. Crucially, they are pre-specified and transparent. As the system moves across them, it activates corresponding responses that are gradual, proportional, and reversible. This transforms capital flow management from a static and discretionary process into a dynamic **rules-based system**, where actions are linked directly to observable conditions.

At lower levels of stress, the system introduces only mild adjustments. These may include modest, temporary costs on very short-term capital movements, encouraging longer holding periods without restricting exit. Settlement conditions or leverage parameters can be refined at the margin, slowing the buildup of imbalances without disrupting normal market functioning.

As stress intensifies, responses become more pronounced but remain targeted and time-bound. Measures focus on segments of capital most sensitive to short-term dynamics, while preserving the mobility of longer-term and more stable investment. Only under clearly defined extreme conditions would stronger safeguards be activated—and even then within a framework that is transparent, temporary, and automatically reversible.

An important feature of this approach is that it combines incentives with discipline. By introducing time-based cost structures that decline with holding periods, the system subtly encourages stability without limiting flexibility.

Capital remains mobile—but impatience carries a price

The Adaptive Capital Flow Framework (ACFF)

At the heart of this approach lies a framework designed to transform capital flow management from a static policy choice into a dynamic system. The **Adaptive Capital Flow Framework (ACFF)** is built on a simple but powerful idea: capital should move freely under normal conditions, and only be modulated—predictably and proportionally—when systemic risk begins to rise.

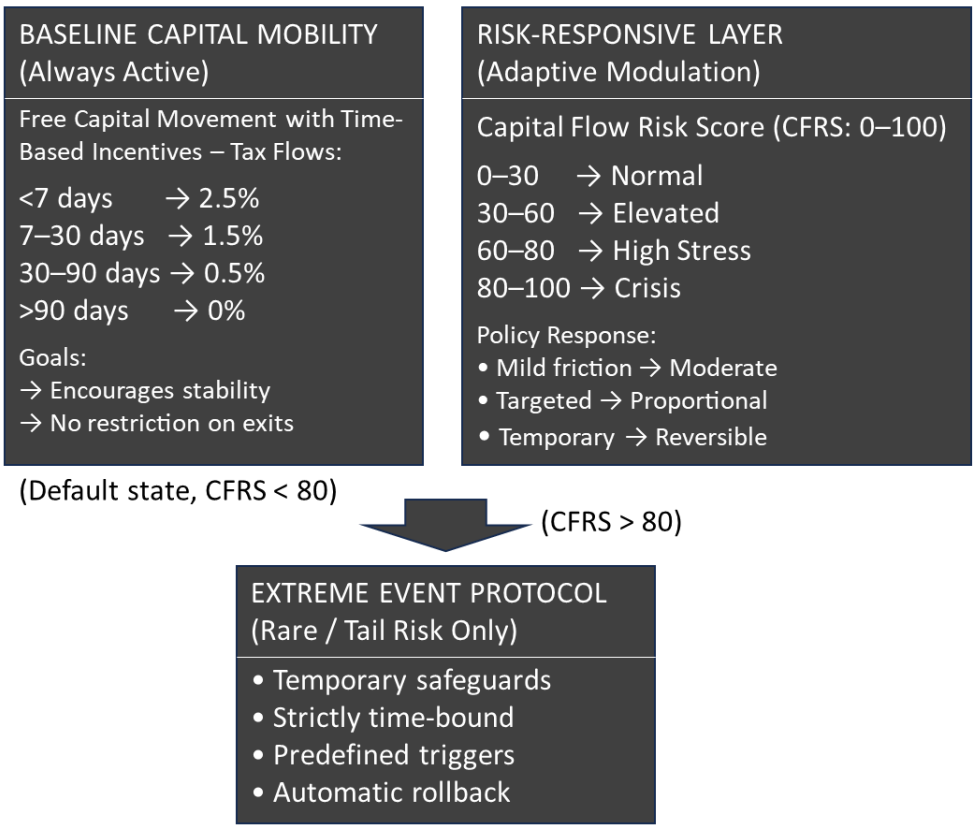
The response is governed by a composite risk indicator, the **Capital Flow Risk Score**, which aggregates signals across multiple dimensions of the financial system. As the score moves across

predefined ranges, the system transitions through corresponding regimes, each associated with a calibrated set of responses.

What distinguishes this framework is not the presence of control, but how that control is exercised. Instead of relying on discretionary intervention—often implemented under pressure and subject to uncertainty—control is embedded within the structure of the system itself. Triggers are known in advance, thresholds are visible, and responses follow predefined rules.

This predictability is critical.

The Adaptive Capital Flow Framework (ACFF)



For investors, uncertainty about potential policy action is often more destabilizing than the existence of rules. A system in which conditions are observable and responses are transparent allows expectations to adjust gradually, reducing the likelihood of abrupt shifts in behavior. For policymakers, it enables earlier, more consistent intervention—before imbalances escalate.

POLICY RESPONSE LADDER

Regime	Policy Response
Normal	Baseline system only
Elevated	+0.5% temporary surcharge on short-term flows
High Stress	+1–2% surcharge, tighter leverage rules
Crisis	Stronger safeguards (targeted, time-bound)

Design Principles:

- Proportional (not binary)
- Targeted (focus on volatile flows)
- Temporary (auto-reversible)
- Rules-based (not discretionary)

Core Insight: Capital is not stopped—it is slowed when needed.

ACFF vs. Existing Frameworks

Feature	Brazil-style openness	China-style controls	ACFF
Capital mobility	High	Low–medium	High (conditional)
Stability	Low	High	High
Predictability	Medium	Low	High
Efficiency	Medium	Medium-low	High
Investor confidence	Volatile	Mixed	High (if credible)

For China, such a framework offers a way forward that aligns with its broader strategy. It allows **deeper integration with global capital markets while preserving the sequencing and risk management principles** that have guided its development.

Yet a framework, however well designed, must prove itself in practice.

The question, therefore, is where such a system can be implemented, observed, and refined under real-world conditions before being considered for broader adoption.

China has already created such environments perfect for experimentation: Pilot Zones (FTZ).

6. CHINA'S PILOT ZONES: A REAL-TIME LABORATORY FOR CONTROLLED OPENNESS

If a framework such as ACFF is to be more than a theoretical construct, it must be tested under real-world conditions—where incentives, behavior, and market dynamics interact in ways no model can fully anticipate.

China has already created such environments. Its network of Pilot Zones, including the Hainan FTP, the Shanghai FTZ, the Qianhai Special Cooperation Zone in Shenzen, and the Greater Bay Area (GBA) cross-border financial corridors — represents a distributed laboratory for financial experimentation. Each zone is a jurisdiction where new forms of capital mobility can be introduced, observed, and refined without exposing the broader system to undue risk.

The Hainan Free Trade Port is particularly illustrative of this approach. Often described in terms of trade liberalization and regional development, its deeper significance lies in its role as a controlled setting for financial experimentation—a jurisdiction where near-full capital account openness can be introduced, observed, and refined at scale. The GBA's Connect programs—Stock Connect, Bond Connect, and Wealth Management Connect—constitute a functioning HK-mainland capital account boundary operating with real-time flow data. The Shanghai FTZ and Qianhai contribute institutional depth and cross-border monitoring infrastructure.

These pilot zones collectively reflect a different approach—one in which capital is enabled to move, but within a system that remains visible, measurable, and responsive. Flows are permitted, but not left entirely unmanaged. Each zone applies slightly different configurations; together they allow policymakers to compare outcomes across regulatory designs in real time.

The introduction of a framework such as ACFF would represent a **natural extension of this approach**. China's Pilot Zones already provide the key conditions required for such a system. Capital flows are sufficiently open to generate meaningful signals. Institutional structures allow for monitoring and calibration. And the scale, while significant, remains contained relative to the national economy—limiting systemic risk while preserving realism.

The value of these environments lies not only in implementation, but in observation. How do investors respond to clearly defined rules governing capital flows? Do modest, time-based incentives alter behavior? Can early signals of stress be used to moderate imbalances before they escalate? And importantly, does a transparent, rules-based system enhance confidence rather than undermine it?

These questions cannot be answered in theory. They require empirical evidence.

China's Pilot Zone network provides the mechanism to generate that evidence—while allowing for continuous refinement across multiple environments simultaneously. Parameters can be adjusted independently across zones, thresholds recalibrated as zone-specific data accumulates, and responses benchmarked comparatively. This reflects and extends a broader pattern in China's reform strategy: testing locally, evaluating carefully, and scaling selectively.

If successful, the implications extend well beyond any single Pilot Zone.

The lessons derived from this distributed experimental environment can inform the broader evolution of China's financial system. Mechanisms that prove effective can be adapted and expanded, gradually shaping a model of financial openness that remains consistent with China's emphasis on stability and control. In this way, China's pilot zone network serves a dual function. It is both a testing architecture and a signal. To domestic stakeholders, it demonstrates that openness can be pursued without abandoning control. To global investors, it offers a preview of how China may structure its financial system in the future—more accessible, but governed by clearly defined rules.

This leads to the next question - If the Pilot Zone network is the laboratory, how should success be measured? How can policymakers distinguish between temporary fluctuations and meaningful structural progress? Answering that requires a framework capable not only of observing activity, but of evaluating its quality and sustainability over time.

7. MEASURING THE EXPERIMENT: THE PILOT ZONE SUCCESS INDEX

If a Pilot Zone is to function as a laboratory for financial opening, its outcomes must be evaluated with precision. Observation alone is not sufficient. In a system where openness and stability must be carefully balanced, it is essential to distinguish between temporary fluctuations and meaningful progress. This requires a structured approach to measurement—one that captures not just the volume of activity, but its **quality, sustainability, and resilience**.

This can be described as a **Pilot Zone Success Index**. The framework is designed to be applicable across any pilot zone in China's financial opening network. The following dashboard illustrates its application to the Hainan Free Trade Port, using the latest officially reported values available as of March 27, 2026 (in several cases, end-2025 or Q1 2026 readings).

Pilot Zone Success Index — Illustrative Application: Hainan FTP

Bucket	Wt	Indicator	Latest value (Hainan FTP)	Update rule	Scoring guide
Capital plumbing	15	Banks offering EF accounts	11 banks by end-2025	Update when official Hainan/PBOC releases a new count	0–5=under 5; 6–10=5–8; 11–15=9+
Capital plumbing	15	EF accounts opened	810 accounts by end-2025	Update monthly or when new official release appears	0–5=under 200; 6–10=200–500; 11–15=500+
Capital plumbing	15	EF transaction volume	RMB 350.9bn by end-2025	Track absolute level and 3-month growth	0–5=under RMB 50bn; 6–10=50–150bn; 11–15=150bn+
International reach	10	Countries/regions via EF transfers	91 countries and regions by end-2025	Update on each official Hainan/PBOC release	0–3=under 20; 4–7=20–60; 8–10=60+
Portfolio opening	15	Cross-border asset-management pilot	Pilot live; quota RMB 10bn; first public fund opened March 3, 2026	Score on new quota expansions, new product launches	0–5=framework only; 6–10=live but narrow; 11–15=expanding
Trade-finance	10	Post-customs trade momentum	First 100 days after Dec. 18, 2025: RMB 80bn+, up 32.9% YoY	Update monthly from customs releases	0–3=weak; 4–7=positive; 8–10=strong double-digit
Investor traction	10	Actual use of foreign capital	RMB 25.1bn in 2025, up 19.9% YoY	Update when province releases FDI data	0–3=flat; 4–7=single-digit growth; 8–10=double-digit
Two-way opening	5	Outbound direct investment	Non-financial ODI $3.62bn in 2025, up 20.7% YoY	Update on provincial commerce releases	0–1=stagnant; 2–3=moderate; 4–5=strong growth
Enterprise traction	5	New foreign-funded enterprises	After customs ops began, new foreign-funded enterprises up 13%	Update monthly if available	0–1=flat; 2–3=modest growth; 4–5=strong growth
Policy depth	10	Customs/opening architecture	Dec. 18, 2025 launch; zero-tariff coverage 21%→74%, list expanded from ~1,900 to 6,600+ items	Score only when new policy layers added	0–3=rhetoric; 4–7=meaningful framework; 8–10=major step

The **Pilot Zone Success Index Scoring**:

- 0–5: pilot exists, but usage is thin
- 6–15: adoption is real but still narrow
- 16–25: usage is broad, growing, and internationally connected

Interpretation bands for total score

Scoring scale per indicator bucket:

- **0–25**: symbolic pilot
- **26–45**: functioning sandbox
- **46–65**: meaningful opening platform
- **66–80**: credible financial-opening laboratory
- **81–100**: genuine model for wider mainland rollout

Current Assessment: Hainan FTP (Early 2026)

Based on the currently visible evidence, I would place the Hainan FTP around **55–65 on this index**, which means:

More than a showcase, not yet a full breakthrough.

Why that range:

- The infrastructure and policy architecture are clearly real: EF accounts, customs launch, asset-management pilot, and official trade/investment facilitation volumes are already in place.
- But the scale is still small compared with Hong Kong, Shanghai, or China's national markets, and I have not seen evidence yet that Hainan is handling enough portfolio capital to call it a true rival center.

The **Pilot Zone Success Index** is designed to be applied comparatively across zones. A similar dashboard can be constructed for the GBA Connect programs, the Shanghai FTZ, or the Qianhai zone—each generating zone-specific data that, taken together, provides the empirical foundation for deciding which configurations to scale nationally.

The purpose is not to produce a single definitive score, but to organize key dimensions that together determine whether financial opening is evolving in the intended direction. It shifts the focus from measuring activity to evaluating outcomes.

A first dimension is the **composition and behavior of capital flows**.

Rising inflows, by themselves, do not signal success. What matters is their nature. Are flows predominantly long-term and aligned with productive investment, or driven by short-term positioning? Are outflows orderly, or do they accelerate under stress? Distinguishing between these patterns helps assess whether the system is attracting capital that supports stability rather than undermines it.

A second dimension concerns **investor participation and diversity**.

A system concentrated among short-term or highly reactive participants is inherently more fragile. Broader participation—particularly from long-term institutional investors—tends to stabilize markets and extend investment horizons. Monitoring the composition of participants therefore provides insight into the system's resilience.

A third dimension is the development of **market infrastructure and liquidity**.

As financial opening progresses, markets must be capable of absorbing increased activity without generating excessive volatility. This includes not only the depth of equity and bond markets, but also the **availability of hedging instruments** and the **efficiency of settlement systems**. Improvements in these areas signal that the system is becoming structurally stronger.

Equally important is the link between financial flows and the **real economy**. Sustainable opening requires that capital supports productive investment, rather than circulating primarily within financial markets.

Periods of stress provide an additional, critical test. Moments of volatility reveal how the system behaves under pressure. Do flows remain orderly? Does the exchange rate adjust within manageable bounds? Are financial institutions able to absorb shocks without disruption? These conditions offer the clearest indication of whether the system's design is functioning as desired.

Finally, the index must capture **policy transmission and scalability**.

No Pilot Zone is an isolated system; it is a testing ground. When mechanisms prove effective, these dimensions provide a multi-layered view of progress. Success is not defined by the volume of capital entering or leaving a given Pilot Zone, but by the system's ability to **manage those flows in a stable, predictable, and economically meaningful way**. A successful experiment is not one in which volatility disappears, but one in which **volatility remains contained and does not escalate into instability**. In this sense, the Pilot Zone Success Index functions as more than a measurement tool. It is a feedback mechanism—one that allows policymakers to continuously assess whether the balance between openness and control is being maintained, and to adjust accordingly.

Yet any Pilot Zone, by design, represents a localized environment. While it provides valuable insight into how financial opening can be managed in practice, it does not by itself determine China's broader trajectory. To understand that trajectory, a wider framework is required—one that situates the Pilot Zone network within China's overall strategic positioning and the paths available for its financial evolution.

8. CALIBRATING THE PATH: THE CHINA READINESS SCORECARD

As controlled environments, China's pilot zones allow policymakers to observe how different configurations within this spectrum perform in practice. They provide insight into how capital behaves under varying degrees of openness, how markets respond to structured frameworks, and how stability can be maintained as integration increases. In this sense, the Pilot Zone network acts as a bridge between China's current position and its potential future state. The lessons generated within these environments can inform the broader transition, helping to identify which mechanisms support stability and which introduce risk.

Yet understanding position and direction is only part of the challenge. To navigate this transition effectively, policymakers must also assess how prepared the system is to move forward at each

stage. Progress must be aligned with capacity, ensuring that financial opening does not outpace the system's ability to sustain it.

This introduces a final dimension to the analysis. If the Pilot Zone network measures the success of localized experimentation, and the strategic framework maps the space of possible outcomes, then a complementary tool is required to evaluate readiness at the national level—one that can guide sequencing and ensure that progress remains aligned with stability.

A final element is required to connect insight with action. That element is **calibration**.

Financial opening, in practice, is not a single decision. It is a sequence of steps taken over time, each of which must be aligned with the system's capacity to absorb and manage risk. Moving too slowly can limit efficiency and delay integration. Moving too quickly can expose the system to instability. The question, therefore, is not simply whether China is ready to open further. It is:

How far can the system move at any given point without exceeding its capacity to maintain stability?

Answering this question requires a structured approach—one that allows readiness to be assessed in a consistent and measurable way.

This is the role of the **China Readiness Scorecard**.

China Readiness Scorecard

Pillar	Wt	What it measures	Why it matters	What would improve the score
1. Capital-flight resilience	20	Ability to handle outflows without panic	SAFE repeatedly stresses monitoring, early warning, and counter-cyclical management of cross-border capital flows	More ring-fenced pilots, better real-time monitoring, more success with controlled two-way channels
2. FX-stability readiness	15	Ability to tolerate more capital mobility without disorderly RMB moves	SAFE says it wants to keep the RMB at an adaptive and equilibrium level and maintain balanced international payments	Deeper hedging markets, wider tolerated trading bands, less need for administrative smoothing
3. Monetary-policy autonomy	10	Capacity to open while preserving domestic policy control	IMF work on China argues exchange-rate flexibility helps preserve monetary-policy independence and that weak financial-system conditions make rushed capital liberalization risky	Better sequencing: more FX flexibility first, then deeper capital opening
4. Financial-system resilience	15	Whether banks and markets can absorb freer flows safely	Chinese official messaging continues to center financial-risk prevention and overall financial stability	Cleaner balance sheets, better stress testing, stronger market-based risk absorption
5. Quality of foreign-capital access	10	Whether China can attract long-term capital rather than hot money	The PBOC highlights multi-channel opening in stocks, bonds, derivatives, and FX rather than a fully open capital account	More access for pensions, insurers, sovereign funds, and long-term allocators
6. Infrastructure for controlled opening	20	Availability of practical mechanisms for two-way capital movement	Hainan's EF-account rollout is a live example: by end-2025, 11 banks, 810 accounts, RMB 350.9bn in transactions, links to 91 countries and regions	Bigger pilot volumes, more institutions, more replicated channels across zones
7. Policy willingness to scale	10	Whether Beijing looks ready to broaden successful pilots	PBOC says it has promoted two-way opening and removed foreign equity restrictions in key financial sectors	Expansion of successful pilot mechanisms into more provinces or national rules

Scoring Rubric for Each Pillar

- **0–25% of pillar weight** = low readiness
- **50% of pillar weight** = partial readiness
- **75% of pillar weight** = credible readiness
- **100% of pillar weight** = high readiness

Example: for a 20-point pillar, score it 5, 10, 15, or 20.

Current Provisional Score for China

Using the evidence we've discussed, my **illustrative current score** would be:

Pillar	Weight	Current illustrative score
Capital-flight resilience	20	12
FX-stability readiness	15	9
Monetary-policy autonomy	10	6
Financial-system resilience	15	8
Quality of foreign-capital access	10	6
Infrastructure for controlled opening	20	15
Policy willingness to scale	10	7
Total	100	63

What that means

A score around **63/100** suggests:

China looks meaningfully more prepared for controlled liberalization than it did in the past, but not yet ready for a fully open-capital-account model.

Interpretation bands

Use these bands for decision-making:

- **0–35** = not ready
- **36–55** = selective opening only
- **56–70** = controlled liberalization feasible
- **71–85** = broader liberalization plausible
- **86–100** = high readiness for major capital-account opening

At **~63**, China currently sits in **"controlled liberalization feasible."** That is exactly where Pilot Zone experiments – Hainan FTP, the GBA Connect channels, and related partial-opening initiatives – make the most sense.

That conclusion fits the evidence. On the one hand, China has clearly broadened foreign-market access and built financial-opening infrastructure; on the other hand, SAFE still emphasizes monitoring, early warning, macro-prudential control, and guarding against cross-border capital-flow risk rather than embracing full convertibility.

Rather than treating readiness as a binary condition, the scorecard frames it as a continuous assessment across the key components that determine the system's ability to manage capital flows. Different elements of the financial system evolve at different speeds, and opening must reflect this reality.

The scorecard captures this through a set of core dimensions. It evaluates the resilience of capital flows, the capacity to manage exchange rate dynamics, the strength of financial institutions, the quality of incoming capital, the depth of market infrastructure, and the credibility of the policy framework. Each dimension reflects a different aspect of the system's ability to absorb cross-border capital movements without generating instability.

The value of this approach lies in its link to sequencing. As these dimensions strengthen, the system can support greater openness. Where gaps remain—whether in market depth, risk management tools, or institutional capacity—progress can be calibrated accordingly. Financial liberalization becomes a **measured and conditional process**, guided by observable indicators rather than fixed timelines.

This framework also integrates naturally with the dynamic mechanisms introduced earlier. While the **Readiness Scorecard** assesses **structural capacity**, tools such as the **Capital Flow Risk Score** capture **real-time conditions**. Together, they provide a two-layer system: one defining how far the system can safely move, the other guiding how it should behave as conditions evolve.

This combination allows policymakers to balance long-term objectives with short-term stability. At the national level, the scorecard also supports coordination.

Financial opening interacts with monetary policy, exchange rate management, and regulatory frameworks. A structured assessment of readiness helps ensure that progress in one area does not outpace developments in others, creating a more coherent and resilient path forward.

It also enhances communication. A transparent framework for assessing readiness allows policymakers to explain the pace and sequencing of reforms more clearly. This reduces uncertainty and strengthens confidence among both domestic and international stakeholders.

Financial opening is no longer perceived as discretionary or reactive, but as a deliberate process anchored in the system's capacity to sustain it.

In this sense, the China Readiness Scorecard is not only a measurement tool. It is a **credibility mechanism**. It signals that progress is not arbitrary, but structured—aligned with the system's evolving strength and guided by a clear logic of stability. Taken together with the broader architecture, the framework becomes complete.

ACFF governs how capital flows behave dynamically. The Pilot Zone network provides real-world testing environments. The Success Index measures performance at the pilot level. The Strategic Regime Framework defines direction. The Readiness Scorecard calibrates national progression.

What remains is to translate this integrated approach into practical action.

9. FROM DESIGN TO EXECUTION: A PRACTICAL PATH FOR CHINA

The challenge is now clearly defined. China's objective is not to choose between openness and control, but to design a system in which both can coexist. The frameworks outlined—adaptive capital flow management, real-world experimentation through China's Pilot Zone network, structured measurement, and readiness-based sequencing—form a coherent approach to navigating this transition. The remaining task is execution.

This does not require a departure from China's existing strategy. On the contrary, **it builds directly upon it**. China has long relied on gradualism—testing reforms in controlled environments, refining them through observation, and scaling them once proven effective. The approach proposed here extends that model by embedding greater structure, predictability, and coordination into the process. A practical path forward begins where the necessary conditions already exist.

The Pilot Zone network provides the natural starting point. Within this environment, a rules-based system for managing capital flows can be introduced progressively—beginning with measurement and transparency, followed by calibrated activation of threshold-based responses. The objective at this stage is not restriction, but credibility: to demonstrate that **capital can move within a system that is both open and governed by clearly defined rules**.

As the system operates, the Pilot Zone Success Index provides continuous feedback. Patterns of capital flows, investor behavior, market stability, and policy transmission can be observed and evaluated across zones, allowing for iterative refinement and cross-zone comparison. This

process recognizes that system design cannot be perfected in advance, but must **evolve through real-world application**.

At the same time, insights from the Pilot Zone network can inform national progression through the **China Readiness Scorecard**. Rather than following a fixed timeline, financial opening becomes conditional on measurable improvements in market depth, institutional strength, and risk management capacity. This ensures that integration advances without exceeding the system's ability to sustain it.

Throughout this process, one principle remains central:

Control is not removed—it is optimized.

Equally important is **communication**. A system based on rules and thresholds must be clearly understood. Transparency in how risk is measured, how thresholds are defined, and how responses are triggered allows expectations to adjust gradually, reducing the likelihood of abrupt shifts in behavior.

Over time, as confidence in the framework strengthens, its scope can expand. Mechanisms tested in Pilot Zones can be adapted to other regions and integrated into national policy. Financial opening then evolves not as a single transition, but as a series of calibrated steps supported by data, observation, and refinement.

The implications extend beyond China. In a global environment where capital flows remain both a source of opportunity and instability, the development of a system that reconciles openness with control would represent a meaningful contribution to the global financial architecture. It would offer an alternative to the long-standing dichotomy between liberalization and restriction.

If successful, China will not only open its financial system on its own terms—it may also help redefine the terms of financial control and openness globally.

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