



cutting through complexity

2014

2014 Q3

China's banking sector: Performance of listed banks and hot topics

KPMG Huazhen (Special General Partnership)

December 2014

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Introduction

China's Banking Sector: Performance of Listed Banks and Hot Topics is a KPMG publication that covers the important topics and performance indicators of China's banking industry. It provides in-depth but accessible analyses of the issues to help you understand their impact and the future direction of the banking sector. It also gathers considerable data to analyze the financial position of China's listed banks. We believe our professional experience will help you better understand the current situation of the banking sector.

This issue (2014 Q3) presents the financial position and business performance of the listed banks for the third quarter of 2014 to help you better understand their current situation. The publication also focuses on current hot topics, including insights on Shanghai-Hong Kong Stock Connect, local government bonds, asset securitization practice, and community banks in America. These topics are currently receiving more attention in the banking industry, and we hope that our discussion will help you understand these issues.

We invited Zhou Guangyou, deputy professor from the School of Economics of Fudan University, to provide an academic perspective on internet financial development/money substitution and liquidity management of commercial banks.

For more information, please do not hesitate to contact one of the KPMG professionals listed in the Contact Us section.



01



2014 Q3 economy and finance

Q3 data analysis

In the first three quarters of 2014, China's year-on-year GDP growth reached 7.4%. Q3's growth rate was 7.3%, 0.2 percentage points down from Q2's 7.5%. The growth rate of the first three quarters remained within a reasonable range.

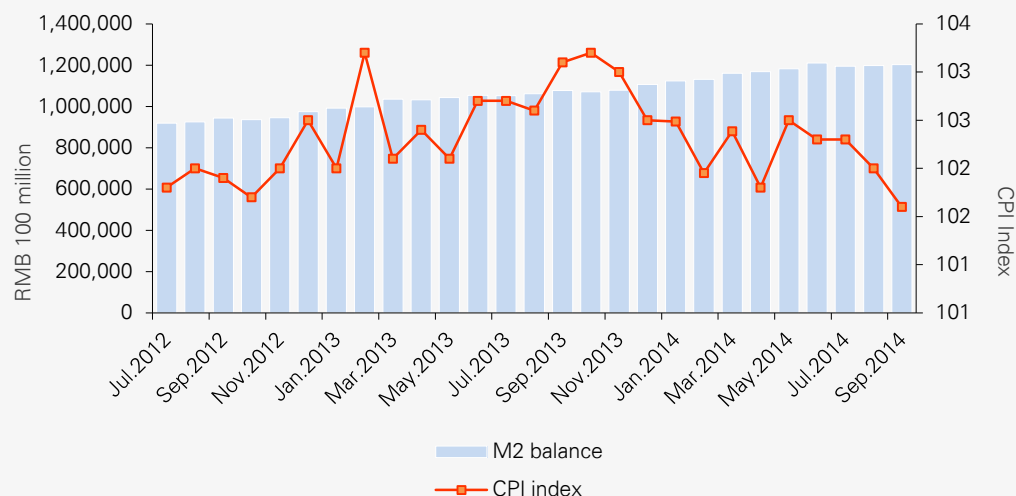
Overall, industrial production remained stable in the first three quarters, consumer prices remained basically stable. The real estate market showed signs of adjustment — national real estate investment increased compared to the same period last year; however, investment growth, commercial housing sales, sales declined compared to the same period last year. The total volume of import and export trade increased by 3.3%, and domestic demand continued to provide impetus for economic growth.

- **Q3 GDP growth stable:** According to preliminary calculations, China's GDP was RMB 41.9908 trillion as at the end of 2014 Sep, representing a year-on-year increase of 7.3% at comparable prices. GDP growth was slightly down by 0.2 percentage points from 2014 Q2. In terms of the performance of different industry sectors, the added values of the primary sector, the secondary sector and the tertiary sector amounted to RMB 3.7996 trillion, RMB 18.5787 trillion and RMB 19.6125 trillion, respectively, representing year-on-year increases of 4.2%, 7.4% and 7.9%.
- **Accelerating growth in imports and exports:** In the first three quarters of 2014, import and export value amounted to USD 3.1626 trillion, a year-on-year increase of 3.3%; the trade balance (exports minus imports) was USD 231.6 billion, a year-on-year increase of 35.5%.
- **Steady growth in consumption:** Total retail sales of consumer goods reached RMB 18.9151 trillion in 2014 Q3, a nominal increase of 12.0% (10.8% in real terms).

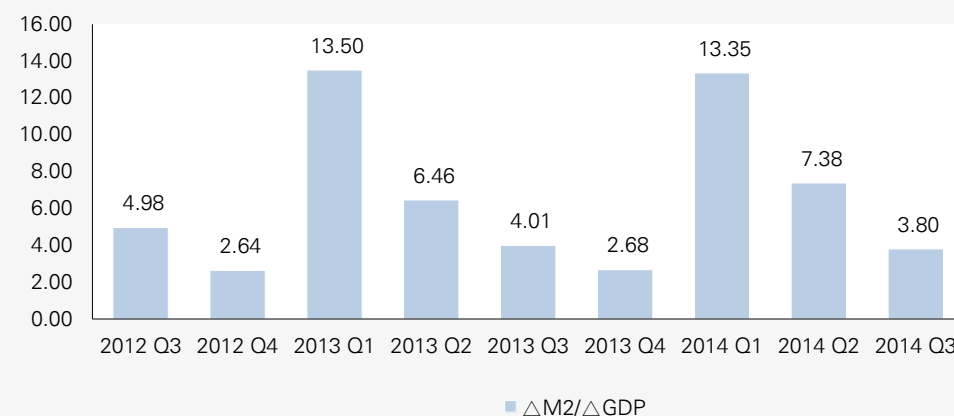
Overview of key macroeconomic indicators	Unit	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4	2014Q1	2014Q2	2014Q3
GDP	Compared to same period last year (%)	7.4	7.9	7.7	7.5	7.8	7.7	7.4	7.5	7.3
CPI	Compared to same period last year (%)	1.9	2.5	2.1	2.7	3.1	2.5	2.3	2.2	2.1
PPI	Compared to same period last year (%)	-3.6	-1.9	-1.9	-2.7	-1.3	-1.4	-2.0	-1.5	-1.6
Industrial added value	Compared to same period last year (%)	9.2	10.3	8.9	8.9	10.2	9.7	8.7	8.9	7.4
Total retail sales of consumer goods	Compared to same period last year (%)	14.2	15.2	12.4	13.3	13.3	13.6	12.0	12.3	12.0
Fixed asset investment	Compared to same period last year (%)	20.5	20.6	20.9	20.1	20.2	19.6	17.6	17.3	16.1
Exports	Compared to same period last year (%)	9.9	14.1	10.0	3.8	-0.3	4.3	-3.4	5.0	5.1
Imports	Compared to same period last year (%)	2.4	6.0	14.1	5.0	7.4	8.3	1.6	1.5	1.3
Trade surplus	100 Million dollars	794.8	832.4	430.7	657.2	615.4	905.5	167.4	859.7	1,280.8
M2	Compare to same period last year (%)	14.8	13.8	15.7	14.0	14.2	13.6	12.1	14.7	12.9
RMB loan growth	Compare to same period last year (%)	16.3	15.0	14.9	14.2	14.3	14.1	13.9	14.0	13.2

Sources: National Bureau of Statistics of China

Money supply and rate of inflation



Velocity of money

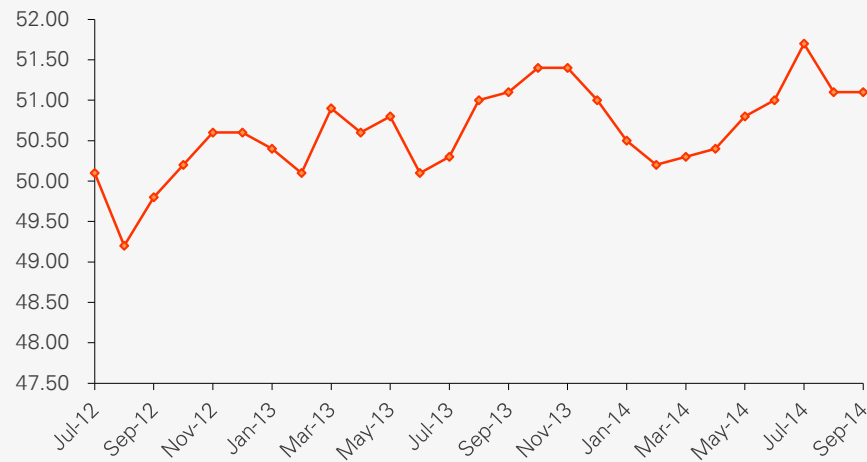


Sources: Wind Info and National Bureau of Statistics of China

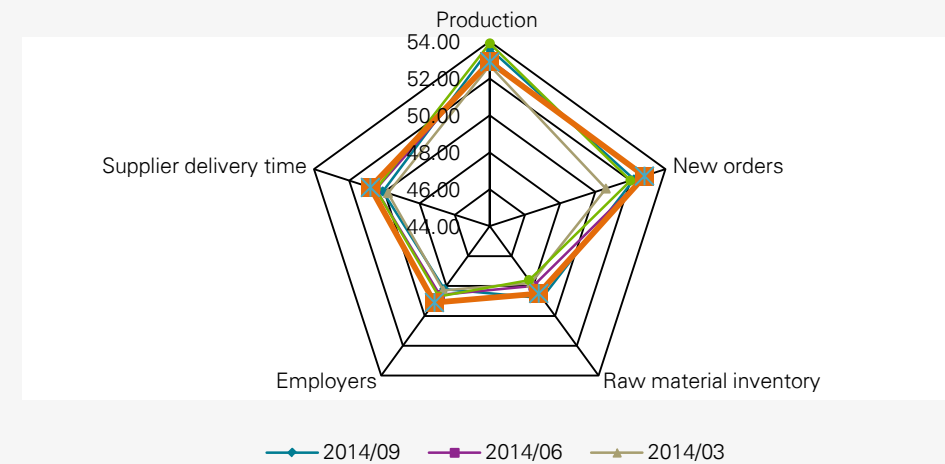
- The CPI growth rate was 2.1% in 2014 Q3. The urban CPI grew by 2.2% and the rural CPI by 1.9%.
- Specifically, food prices increased by 3.3%; prices for tobacco, liquor and articles decreased by 0.6%; clothing prices increased by 2.4%; prices for household equipment and maintenance services rose by 1.2%; prices for medical and personal care products rose by 1.2%; prices for transportation and communication climbed by 0.1%; prices for entertainment and educational products and services rose by 2.2%; and house prices increased by 2.3%.
- As at the end of Sep 2014, the broad money (M2) balance was RMB 120.21 trillion, representing a year-on-year increase of 12.9%; the RMB loan balance was 79.58 trillion, a year-on-year increase of 13.2%; and the RMB deposit balance was 112.66 trillion, a year-on-year increase of 9.3%. As at the end of Sep 2014, the RMB loan increment was 7.68 trillion, representing a year-on-year increase of RMB 0.40 trillion; and the RMB deposit increment was 8.27 trillion, representing a year-on-year decrease of 2.99 trillion.

- At the end of Sep 2014, the narrow money (M1) balance was RMB 37.72 trillion, a year-on-year increase of 4.8%; and the balance of currency in circulation (M0) was RMB 5.88 trillion, representing a year-on-year increase of 4.2%. As at the end of Sep 2014, total social financing was 12.84 trillion, representing a year-on-year decrease of RMB 1.12 trillion.
- Recently, monetary growth has slowed, reflecting economic restructuring, off-balance-sheet financing contracts, slowing of the expansion of the financial sector due to soft constraints, strengthened supervision of interbank business, and a run on the currency overall.

China Purchasing Managers Index (PMI)



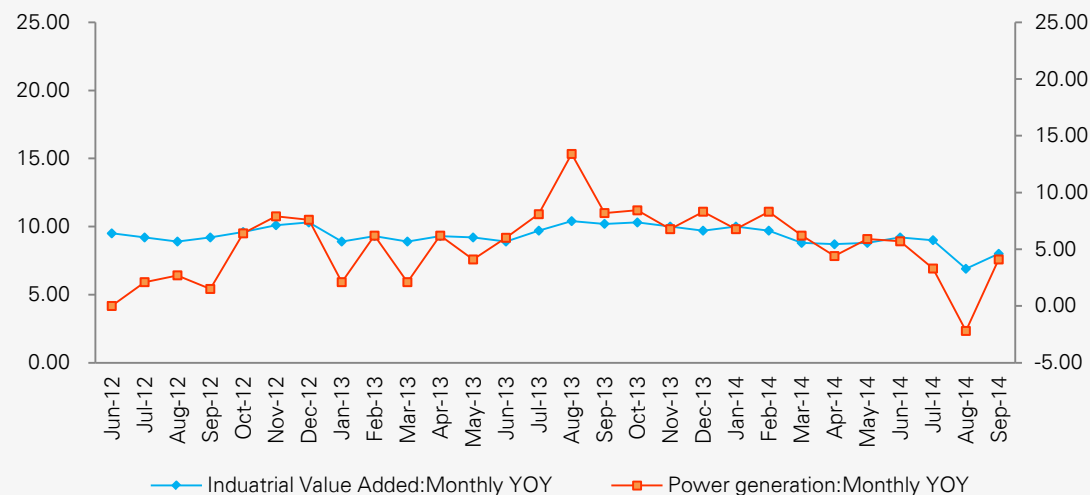
Sub-index under China PMI



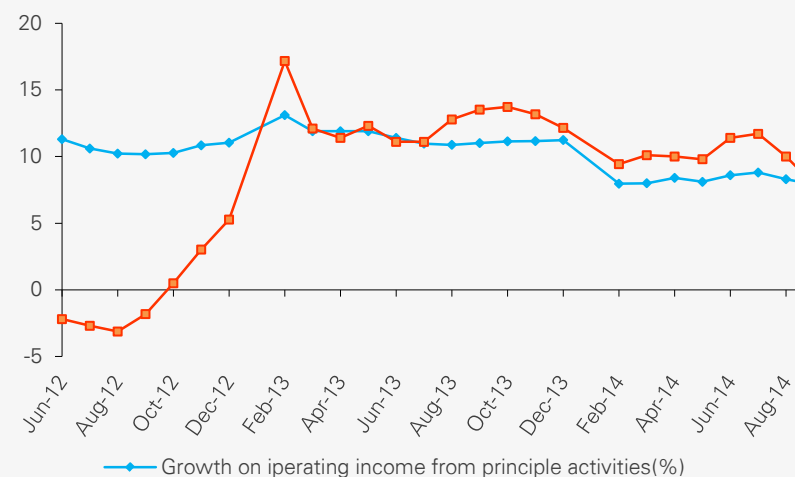
Sources: Wind Info and National Bureau of Statistics of China

- In general, the national economy ran as normal in 2014 Q3, with progress in economic restructuring and upgrading. However, the results also indicate that the economic environment is still complex and changeable, and that the domestic economy is still subject to a certain level of downward pressure.
- In Sep 2014, China's manufacturing PMI was 51.1%, the same as August, and continued the rebound from 2014 Q1, indicating smooth growth of China's manufacturing sector; specifically, the PMI of large enterprises was 52.0%, 0.1 percentage points higher than in August, and remained above the break-even mark; the PMI of medium-sized enterprises was 50.0%, 0.1 percentage points higher than in August; and the PMI of small enterprises was 48.6%, 0.5 percentage points lower, and the second lowest point since April 2014, still below the break-even mark.
- The fresh order index was 52.2%, 0.3 percentage points lower than that in August but still above the break-even mark, reflecting the slowdown in the rebound of manufacturing market demand. Overall, the stable situation of current economy has not changed. The production index was 53.6%, 0.4 percentage points higher than that in the previous month, and remained above the break-even mark, signifying the continued growth of domestic production and the solidification of the development trend of large- and medium-sized enterprises. The business activities expectation index was 56.0%, 1.9 percentage points lower than that in August, but higher than that in June and July, indicating manufacturers' cautious optimism for business activities for the following three months.

Industrial production



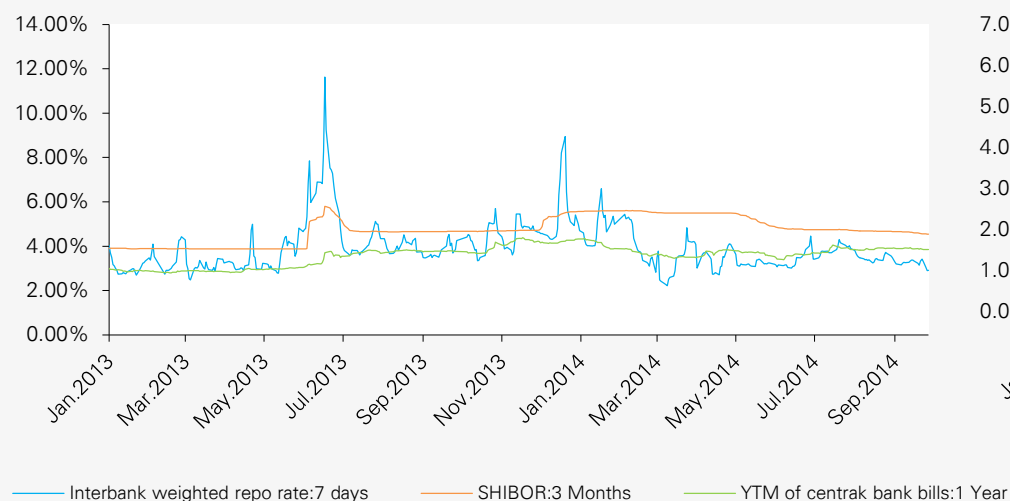
YoY growth of accumulative operating income from principal activities and total profit



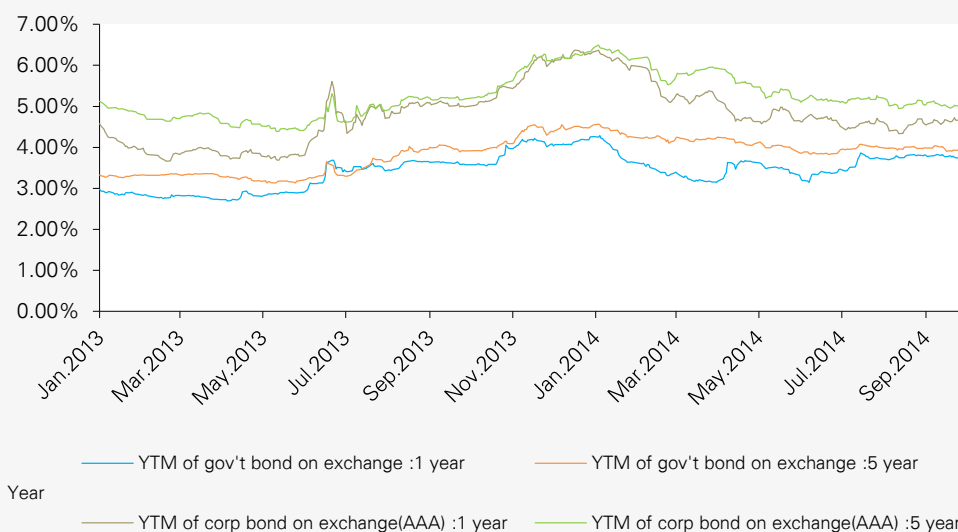
Sources: Wind Info and National Bureau of Statistics of China

- In Sep 2014, the added value of the above-scale industry grew by 8.0% year on year at comparable prices. The rate of increase was 2.2 percentage points lower than that in the same period in 2013. State-owned and state-holding enterprises grew by 4.8%; collective enterprises decreased by 1.0%; joint-stock enterprises grew by 9.3%; and foreign-invested, Hong Kong, Macau and Taiwan invested enterprises grew by 6.4%.
- In terms of industry, the mining industry, the manufacturing industry and utility industries (the production and supply of electricity, heat, gas and water grew) by 3.9%, 9.1% and 2.8% year-on-year, respectively. In terms of region, the eastern region grew by 7.3% year-on-year, the central region by 8.1% and the western region 10.7%. The sales rate of above-scale industrial enterprises stood at 98.0% in Sep 2014, unchanged from that during the corresponding period the previous year.
- As at the end of Sep 2014, the operating income from principal activities of above-scale industrial enterprises was RMB 79.09875 trillion, representing a year-on-year increase of 7.9%; the cost of operating income from principal activities was RMB 68.05641 trillion, representing a year-on-year increase of 8.2%. The increase in cost was slightly higher than that of income. Above-scale industrial enterprises realized profits of RMB 4.36522 trillion, an increase of 7.9% year-on-year; profit from principal activities amounted to RMB 4.08138 trillion, representing an increase of 7.5% year-on-year.
- As at Sep 2014, the mining industry had profits of RMB 468.12 billion, representing a year-on-year decrease of 19.9%; the manufacturing industry had profits of RMB 3.53441 trillion, representing a year-on-year increase of 12.0%; and utility industries had profits of RMB 362.69 billion, representing a year-on-year increase of 19.6%.

Money market rate



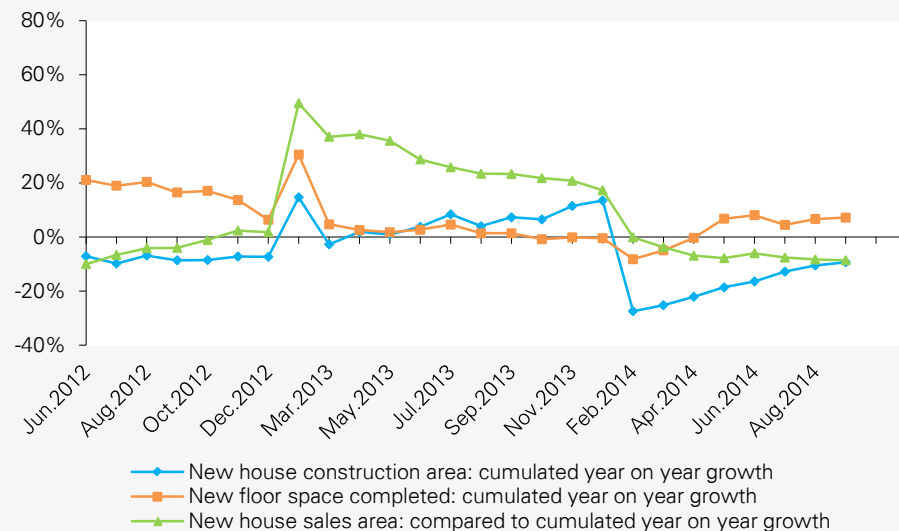
Bond yield



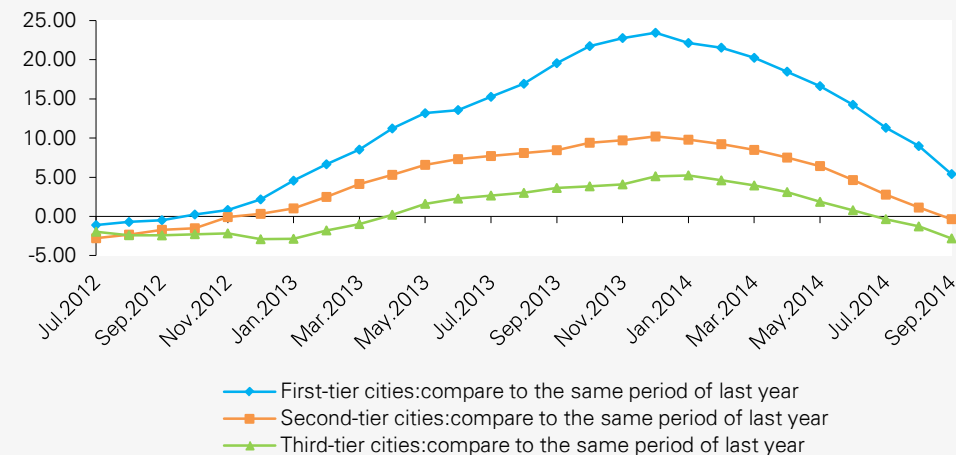
Source: Wind Info

- At the end of Sep 2014, the yield to maturity of one-year central bank bills was 3.85%, 9 basis points higher than that during the corresponding period last year.
- In 2014 Q3, the RMB/USD exchange rate turned to an appreciation trend from depreciation, and trading was active. Direct trading was launched between the RMB and the New Zealand dollar and transactions were relatively active.
- By the end of Sep, the overnight SHIBOR rate, one-week SHIBOR rate and one-month SHIBOR rate had fallen by 59.85 basis points, 210.70 basis points and 191.20 basis points, respectively, as compared to the rates at the beginning of the year, dropping to 2.5325%, 2.8740% and 3.9980%, respectively. As at the end of Sep, the yield to maturity of three-year and seven-year treasury bonds in the inter-bank market were 3.8006% and 3.9499%, down 60.44 basis points and 66.00 basis points, respectively, from the beginning of the year.
- In 2014 Q3, after two consecutive seasons of declines in the first half of 2014, the inter-bank bond market finally had the opportunity to stage a revival. With the anticipated improvement of funding and reinforced regulatory examination of non-standard investment, money started to flow back into the bond market.
- In the first three quarters of 2014, the central bank lowered the reserve ratio, and monetary policy tools were subject to further refined and differentiated management. Overall, the funding situation was looser than that in the second half of 2013 and was also a key driving force in the smoothing of bond yields in Q3.

Growth of saleable area, and floor space completed and under construction



Housing price indices of 100 cities

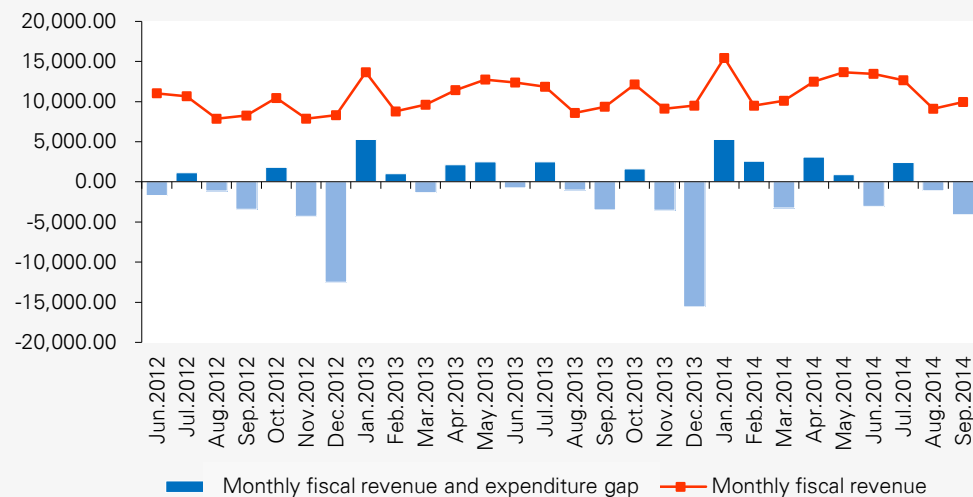


Source: National Bureau of Statistics, Wind Info

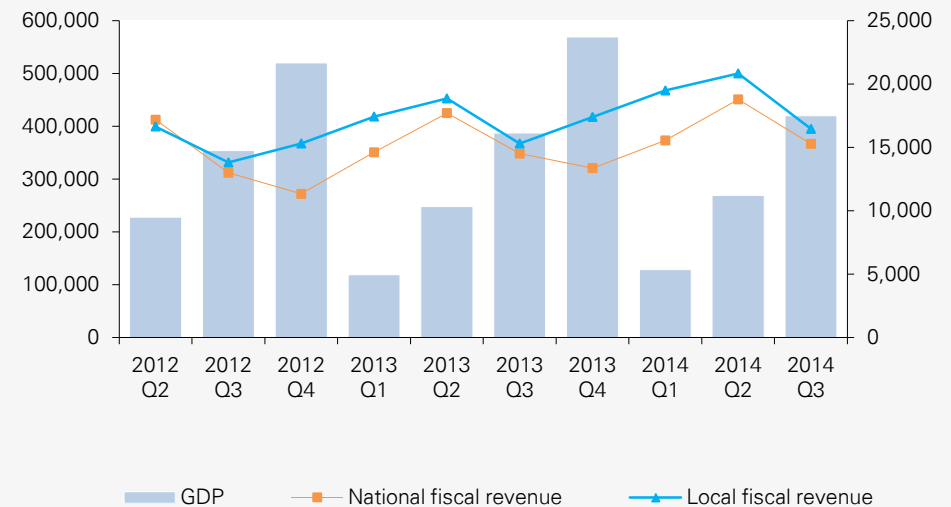
- As at the end of Sep 2014, national real estate investment amounted to RMB 6.8751 trillion, representing a nominal year-on-year increase of 12.5%, with the growth rate down 1.6 percentage points from that of the first half of 2014. Residential housing investment grew by 11.3%. The new floor space under construction was 1,314.11 million square metres, representing a year-on-year decrease of 9.3%; but the new construction area for residential housing fell by 13.5%.
- The saleable area of commodity housing was 771.32 million square metres, representing a year-on-year decrease of 8.6%, of which the saleable area for residences fell by 10.3%. The total sales of commodity housing reached RMB 4.9227 trillion, representing a year-on-year decrease of 8.9%, of which residential housing sales dropped by 10.8%. The land purchase area of real estate developers reached 240.14 million square metres, representing a year-on-year decrease of 4.6%. As at the end of Sep, the available-for-sale area of commodity housing was 571.48 million square metres, representing a year-on-year increase of 28%.

- In 2014 Q3, house prices continued to decline, but the decline slowed. In 70 large- and mid-size cities, new commercial housing and second-hand housing prices decreased except for Xiamen, the price of which remained at the same level compared with that of the same period last year. While prices continued to fall, the decline slowed from the pace in August. According to estimates from the National Bureau of Statistics, the average overall decline of new commercial housing prices in those 70 large and mid-sized cities was 0.2 percentage points less than the rate of decline in August.
- In 2014 Q3, house prices fell in most cities. In Sep, of the 70 cities studied, new commercial housing fell in 58 cities and second-hand house prices in 52 cities, an increase of 39 and 20 cities, respectively, from August.

Monthly fiscal balances (RMB 100 million)



Fiscal revenue and GDP (RMB 100 million)

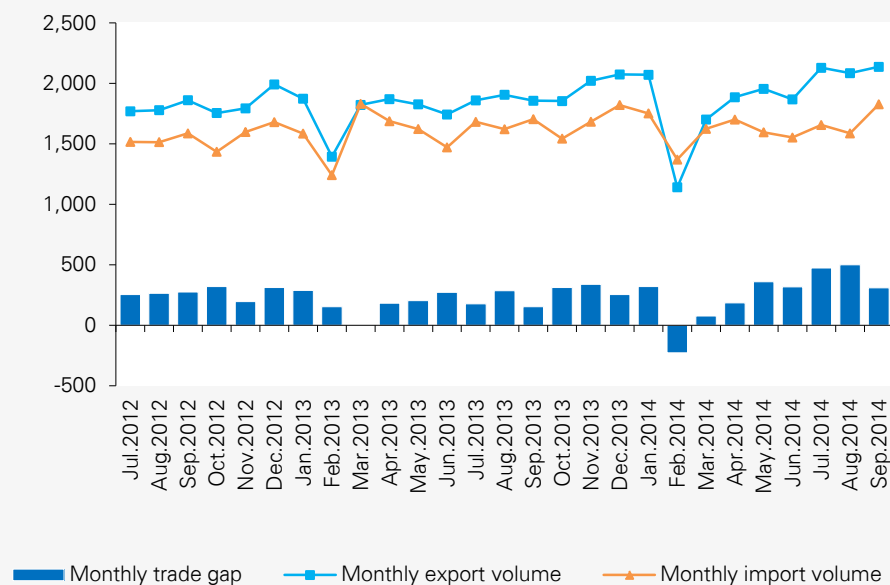


Source: Ministry of Finance

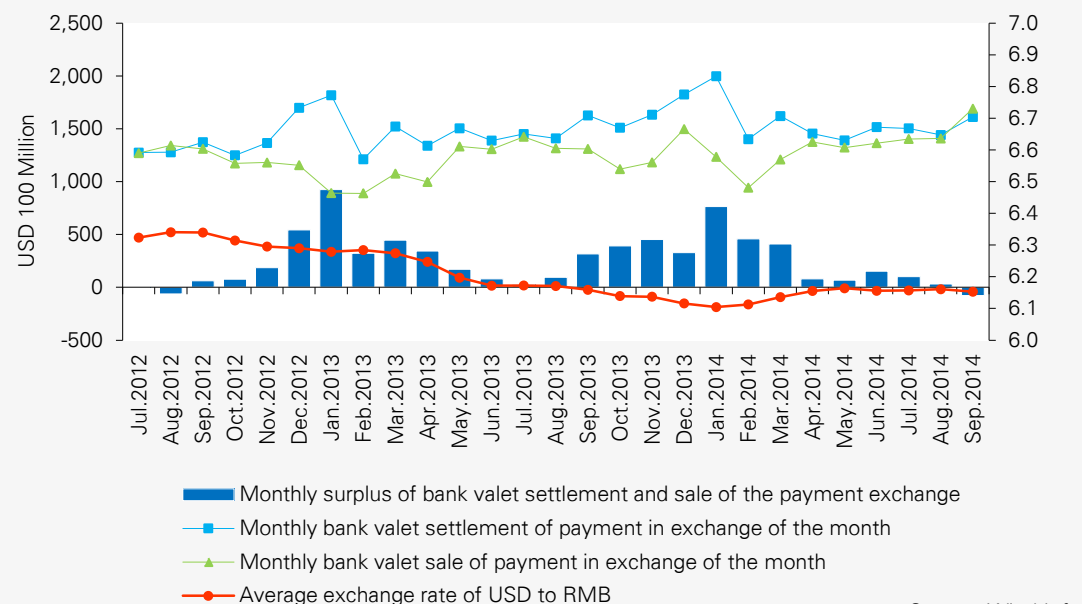
- In 2014 Q3, national fiscal revenue amounted to RMB 3.1724 trillion, representing a year-on-year increase of RMB 192.5 billion, or 6.5%. Central fiscal revenue reached RMB 1.5271 trillion, representing a year-on-year increase of 5.3%, while local fiscal revenue totalled RMB 1.6453 trillion, a year-on-year increase of 7.6%.
- National fiscal expenditure in 2014 Q3 amounted to RMB 3.4486 trillion, representing a year-on-year increase of RMB 266.8 billion, or 8.4%. Central fiscal expenditure totalled RMB 514.8 billion, representing a year-on-year increase of 9.3%, while local fiscal expenditure reached RMB 2.9338 trillion, a year-on-year increase of 8.2%.

- National fiscal revenue amounted to RMB 10.6362 trillion in the first nine months of 2014, an increase of 8.1%, or a year-on-year decrease of 0.5 percentage points. Central fiscal revenue reached RMB 4.9599 trillion, a year-on-year increase of 6.0%, while local fiscal revenue totalled RMB 5.6763 trillion, a year-on-year increase of 10.1%. Of the fiscal revenue, RMB 9.0695 trillion came from tax revenue, a year-on-year increase of 7.4%. Affected by a slowdown in China's economic growth, the revenue growth of first three quarters declined, ending the high double-digit growth of the past. However, national fiscal revenue in the first three quarters of a percentage of GDP stabilized at around 25.3%, remaining the same as that of 2013. Similar to national fiscal revenue growth speed, local fiscal revenue growth of the first three quarters was also down.

Import and export trade (USD 100 million)



Bank valet exchange settlement and sale and exchange rate



Source: Wind Info

- In the first three quarters of 2014, the value of imports and exports amounted to USD 3.1626 trillion, representing a year-on-year increase of 3.3%.
- The value of exports was USD 1,697.1 billion, representing a year-on-year increase of 5.1%; the value of imports was USD 1,465.5 billion, representing a year-on-year increase of 1.3%; and the trade surplus was USD 231.6 billion.
- In Sep, the value of imports and exports was USD 396.4 billion, representing a year-on-year increase of 11.3%. The value of exports was USD 213.7 billion, representing a year-on-year increase of 15.3%; and the value of imports was USD 182.7 billion, representing a year-on-year increase of 7.0%.

- In the first three quarters of 2014, bank valet exchange settlement added up to USD 1,394.3 billion and sales to USD 1,195.5 billion, making the valet exchange settlement and sales surplus USD 198.8 billion.
- In 2014 Q3, the exchange rate of the RMB against the USD gradually appreciated compared to that in 2014 Q2, with the monthly average exchange rate of the USD against the RMB declining from 6.1557 to 6.1528.

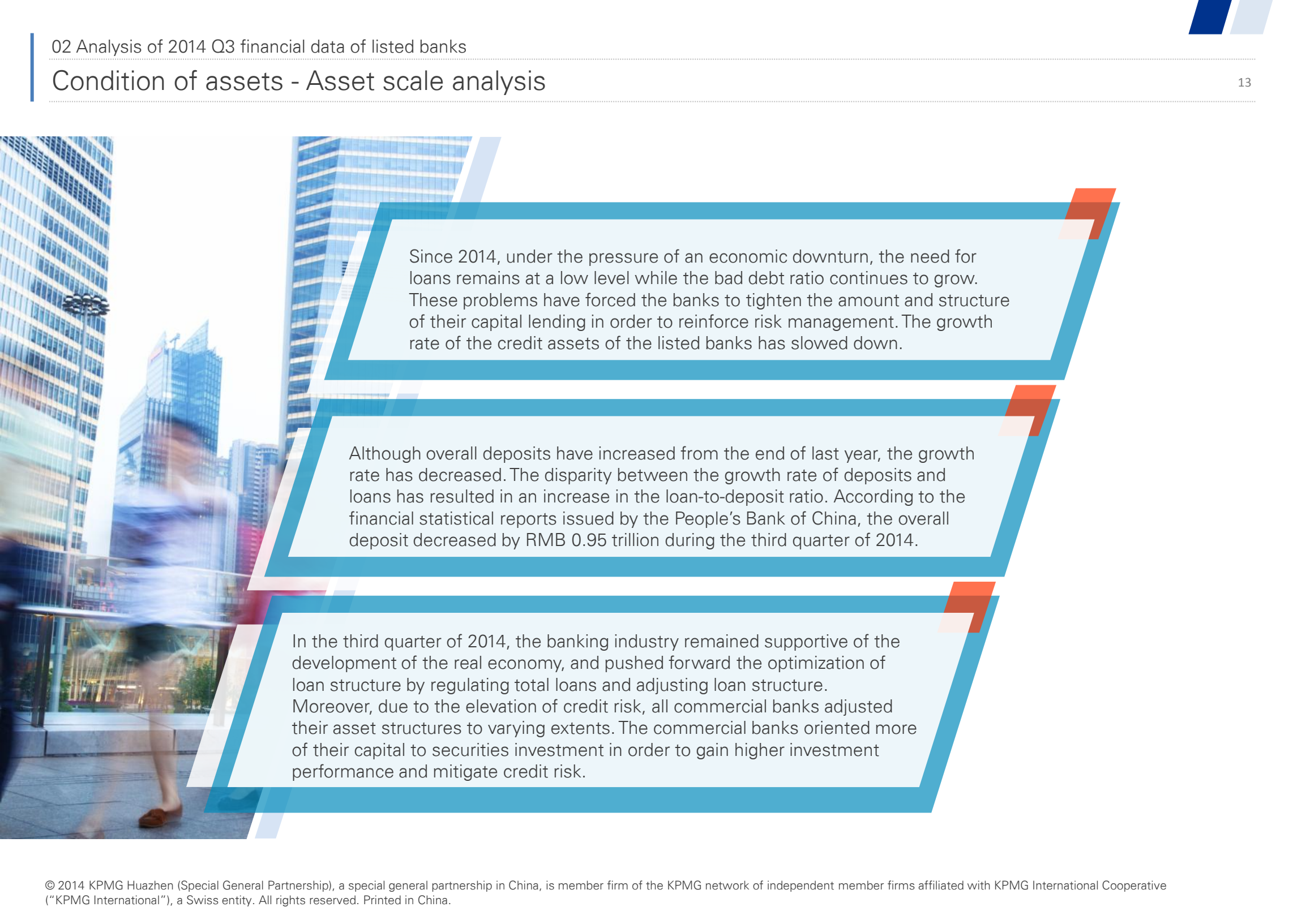


02



Analysis of 2014 Q3 financial data of listed banks

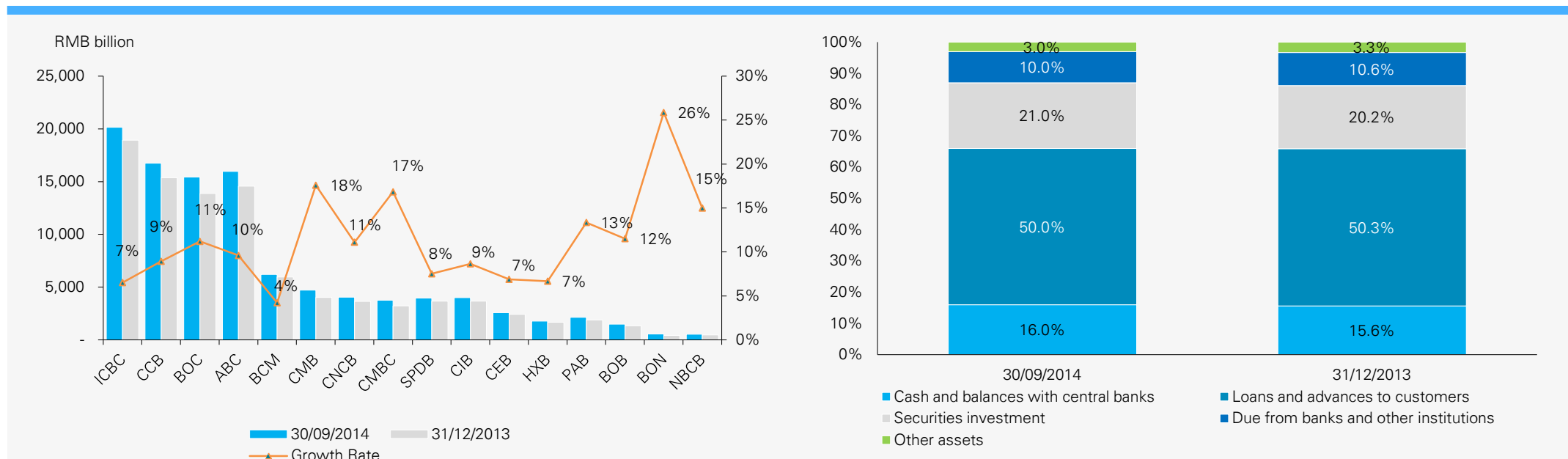
Condition of assets - Asset scale analysis



Since 2014, under the pressure of an economic downturn, the need for loans remains at a low level while the bad debt ratio continues to grow. These problems have forced the banks to tighten the amount and structure of their capital lending in order to reinforce risk management. The growth rate of the credit assets of the listed banks has slowed down.

Although overall deposits have increased from the end of last year, the growth rate has decreased. The disparity between the growth rate of deposits and loans has resulted in an increase in the loan-to-deposit ratio. According to the financial statistical reports issued by the People's Bank of China, the overall deposit decreased by RMB 0.95 trillion during the third quarter of 2014.

In the third quarter of 2014, the banking industry remained supportive of the development of the real economy, and pushed forward the optimization of loan structure by regulating total loans and adjusting loan structure. Moreover, due to the elevation of credit risk, all commercial banks adjusted their asset structures to varying extents. The commercial banks oriented more of their capital to securities investment in order to gain higher investment performance and mitigate credit risk.



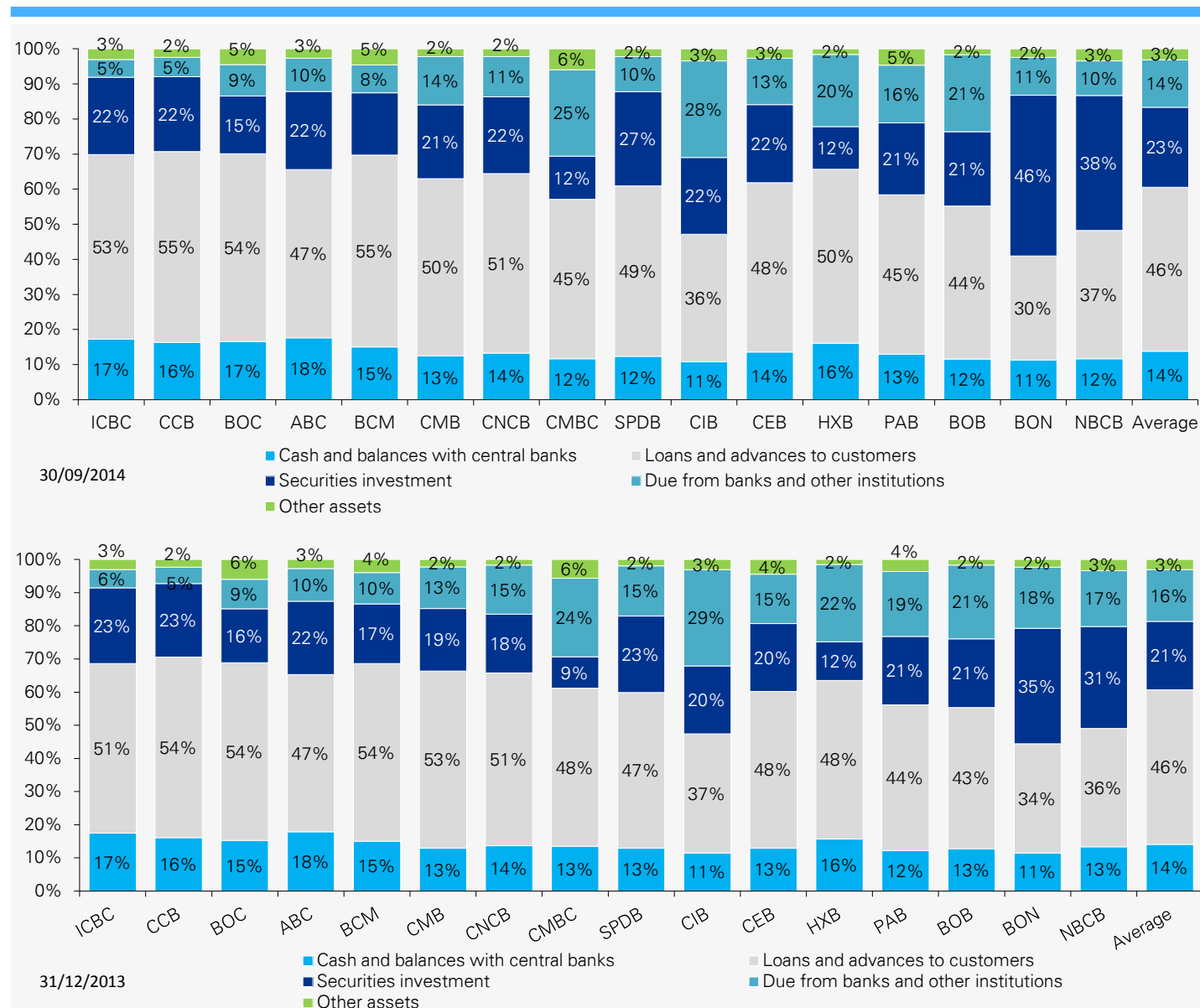
In the third quarter of 2014, the scale of the total assets of the listed banks increased, resulting from the expansion of the scale of credit assets and securities investment.

Compared to five major state-owned banks, some of the shareholding commercial banks experienced more active expansion. BON enjoyed the biggest growth in asset scale, achieving an increase of up to 26% compared with the end of 2013, while China Merchant's Bank (CMB) and CMBC recorded an increase of 18% and 17%, respectively.

The total asset scale expanded in the third quarter of 2014. The asset structure of listed banks also changed from the end of 2013: the ratio of loans and advances to customers was down by 0.3 percentage points; the ratio of due from banks and other financial institutions decreased by 0.6 percentage points; the ratio of cash and balances with central banks increased by 0.4 percentage points; and the ratio of securities investment increased by 0.8 percentage points.

Affected by the slowdown of the real economy and the increase of credit risk, the listed banks took the initiative in mitigating risks through measures such as raising the threshold, cutting lending and controlling credit scale for industries or areas with higher risk. At the same time, they tried to lower their risk exposures by adjusting capital lending direction and optimizing their asset structures.

Condition of assets - Asset structure



Compared with the end of 2013, the average ratio of loans and advances to customers of the 16 banks remained fairly the same.

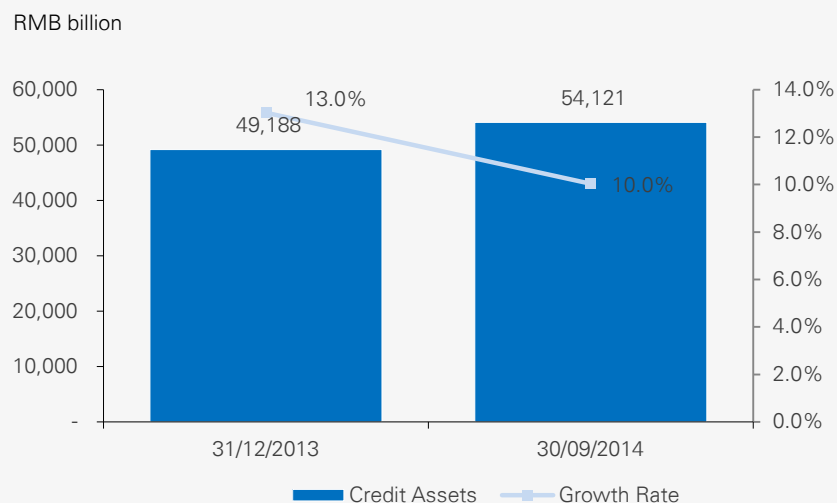
The average securities investment ratio of the 16 banks increased 2% from that of the end of 2013. 12 of the 16 banks had increased securities investment ratios, while those of the other four banks fell.

In the third quarter of 2014, the banking industry remained supportive of the development of the real economy and pushed forward the optimization of loan structure by regulating total loans and adjusting loan structure.

Moreover, due to the elevation of credit risk, all commercial banks adjusted their asset structures to varying extents. In the third quarter of 2014, the commercial banks oriented more of their capital to securities investment in order to gain higher investment performance and mitigate credit risk.

Condition of assets – Total loans

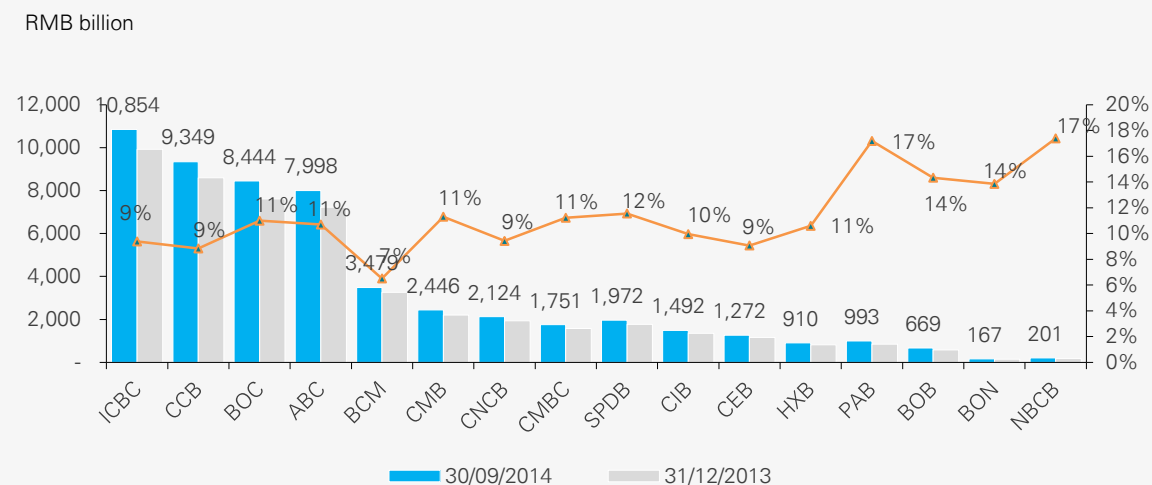
Credit Assets



In the third quarter of 2014, the total scale of the credit assets of the listed banks was RMB 54.12 trillion. The rate of growth slowed significantly to 10%.

Under the pressure of an economic downturn, the need for loans remains at a low level while the bad debt ratio continues to grow. These problems have forced the banks to tighten the amount and structure of their capital lending in order to reinforce risk management.

Credit Assets



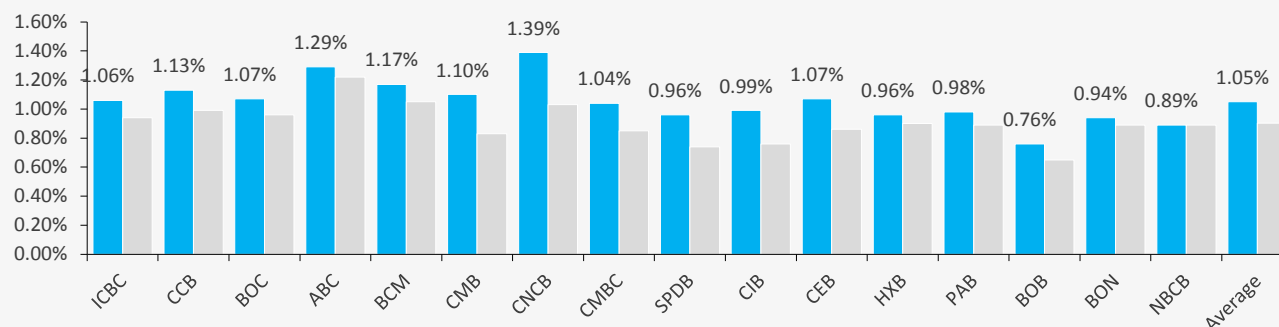
In Q3, the growth rate of the credit assets of the listed banks showed an opposite trend to their total scale.

Some of the banks with a smaller credit asset scale recorded a higher than average growth rate. Their growth was driven by the following factors: increased financing support to small and micro enterprises; expansion of the scale of consumer loans and credit card loans; and financial innovation of loans through cooperation with key industries.

According to the 2014 3Q statistical report of loan investment issued by the People's Bank of China, although small banks increased financing support to small and micro enterprises, the growth rate of overall financing support to small and micro enterprises from major financial institutions, small rural financial institutions, and foreign banks has slowed.

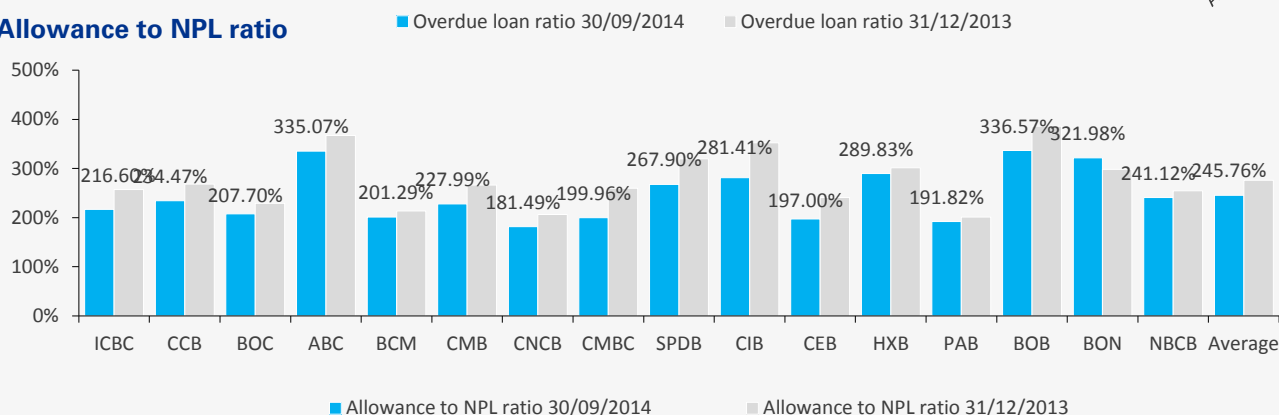
Condition of assets – Loan quality

NPL ratio



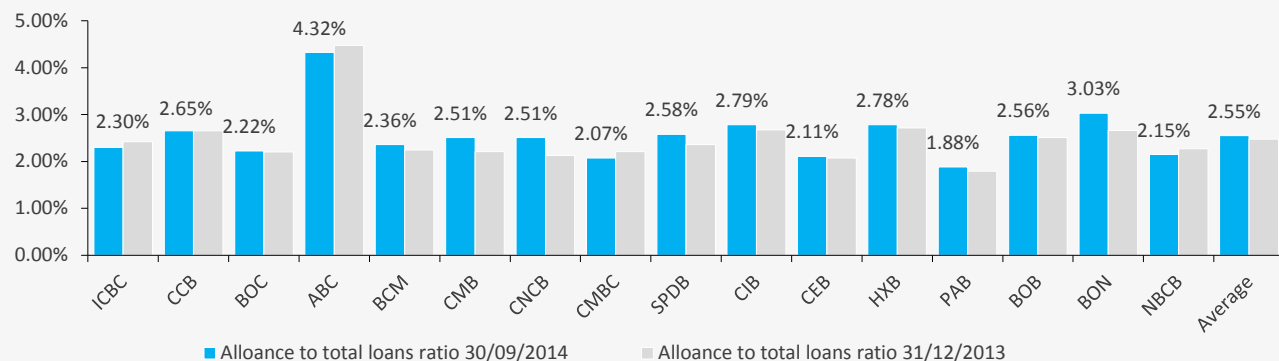
In the third quarter of 2014, the NPL ratios of the listed banks increased compared with those as at the end of 2013, with an average NPL ratio of 1.05% (2013: 0.90%). BOB recorded the lowest NPL ratio of 0.76% while CNCB recorded the highest NPL ratio of 1.39%.

Allowance to NPL ratio



In the third quarter of 2014, although there were sufficient allowances for the listed banks, the allowance to NPL ratio of most listed banks decreased compared with those as at the end of 2013 as a result of an increased NPL ratio. The only exception is BON, which recorded an increased allowance to NPL ratio.

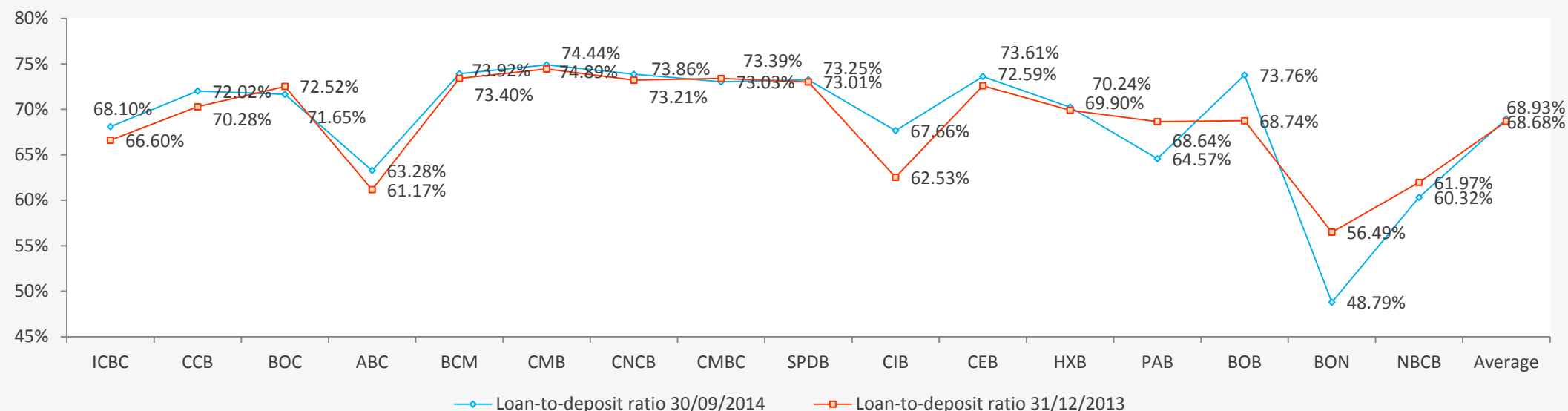
Allowance to total loans ratio



In the third quarter of 2014, the scale of the allowance to total loans ratio of the listed banks centered around 2% to 4.3%, except for PAB, the ratio of which remained at a low level.

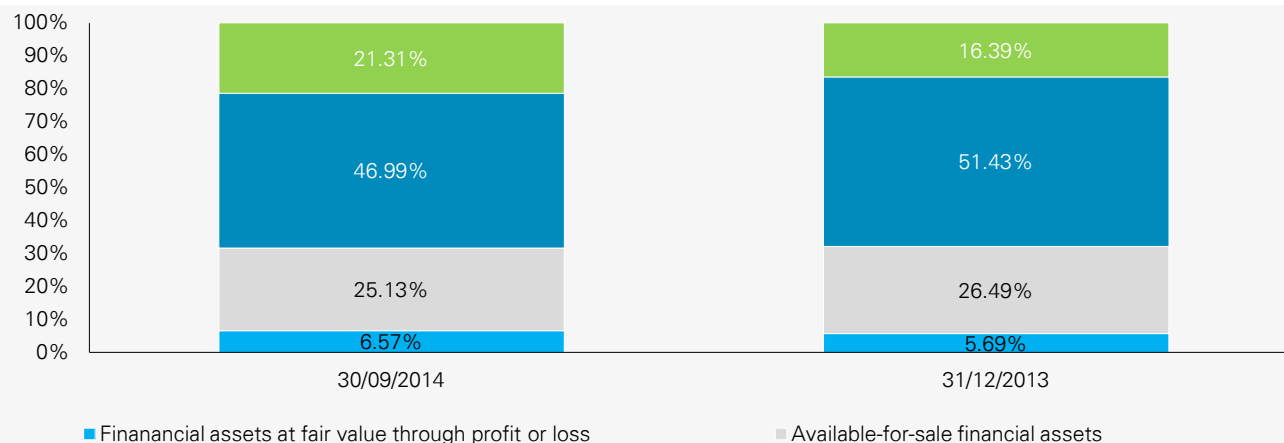
Source: The banks' 2013 annual reports & 2014 Q3 reports, KPMG China research

Condition of assets – Loan-to-deposit ratio



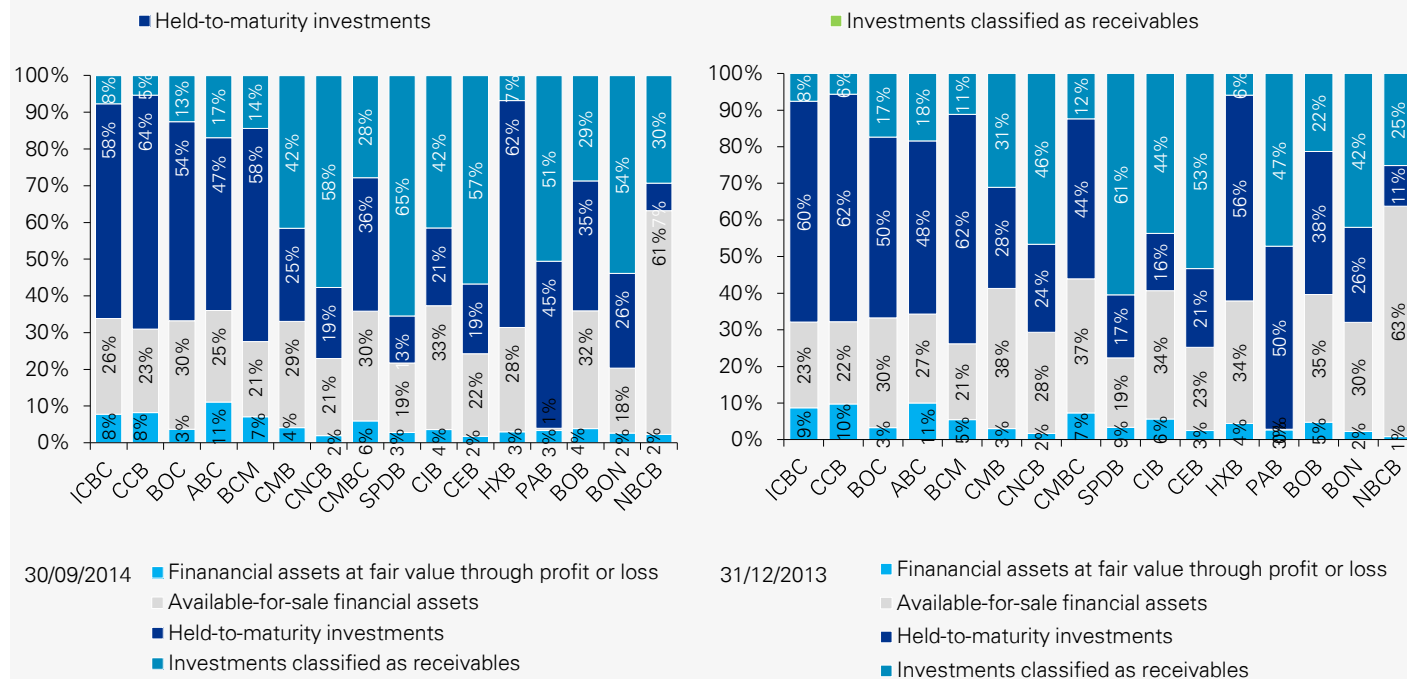
As at the end of the third quarter of 2014, the LDR for most of the listed banks remained fairly the same compared with that as at the end of 2013. However, the ratio as at the end of third quarter increased from the ratio of the second quarter. Although the overall deposits increased from the end of 2013, the growth rate decreased. It is worth mentioning that overall deposits decreased during the third quarter according to the financial statistical reports issued by the People's Bank of China. The disparity between the growth rate of deposits and loans has resulted in the increase in the LDR. The ratios of CIB and BOB increased over 5 percentage points, while the ratios of PAB and BON decreased by 4 and 7 percentage points, respectively. In addition, because the CBRC adjusted the criteria for calculating commercial banks' LDRs, certain commercial banks with a higher ratio of small and micro businesses loans, and of loans related to San Nong (agriculture, farming and rural areas), benefited from the policy that these types of loans were to be removed from calculating the LDR, resulting in a significant drop in their LDRs.

Condition of assets – Securities investment



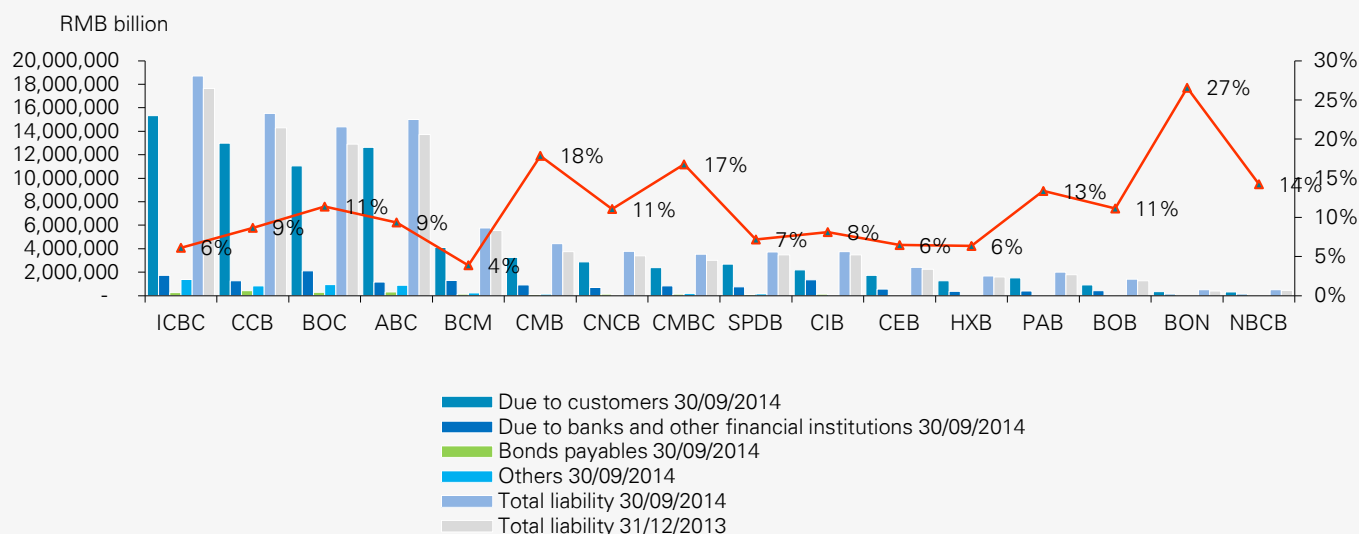
In the third quarter of 2014, the listed banks increased the scale of their securities investment as a proportion of overall asset structure by 16.76% on average compared with that as at the end of the previous year.

As for general securities investment structures, influenced by the tightening of the interbank business, the listed banks moderately increased the ratio of investments classified as receivables according to their demand of assets/liabilities configuration and operational performance improvement in order to gain higher investment portfolios and performance levels than those from ordinary bonds.

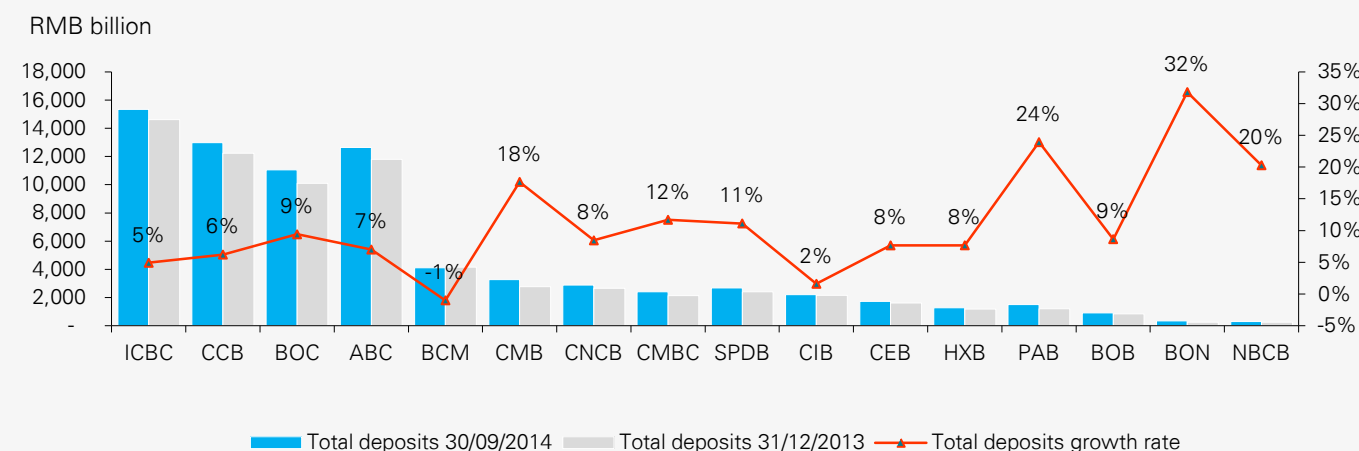


In the third quarter of 2014, the securities investment structures of the listed banks differed. The five state-owned banks still held a high percentage of held-to-maturity investments, while other commercial banks increased the proportion of investment classified as receivables to varying degrees.

Condition of liabilities – Liability structure



In Q3 2014, the growth trend of the total liabilities of the listed banks was the same as that of the total assets, with an average increase of 11% compared to that as at the end of 2013. This was mainly because the banks enhanced their deposit taking scale. Customer deposits and amounts due to banks and other financial institutions experienced a steady rise. BON, CMB and CMBC recorded the highest increases. Customer deposits were still the major component of liabilities.

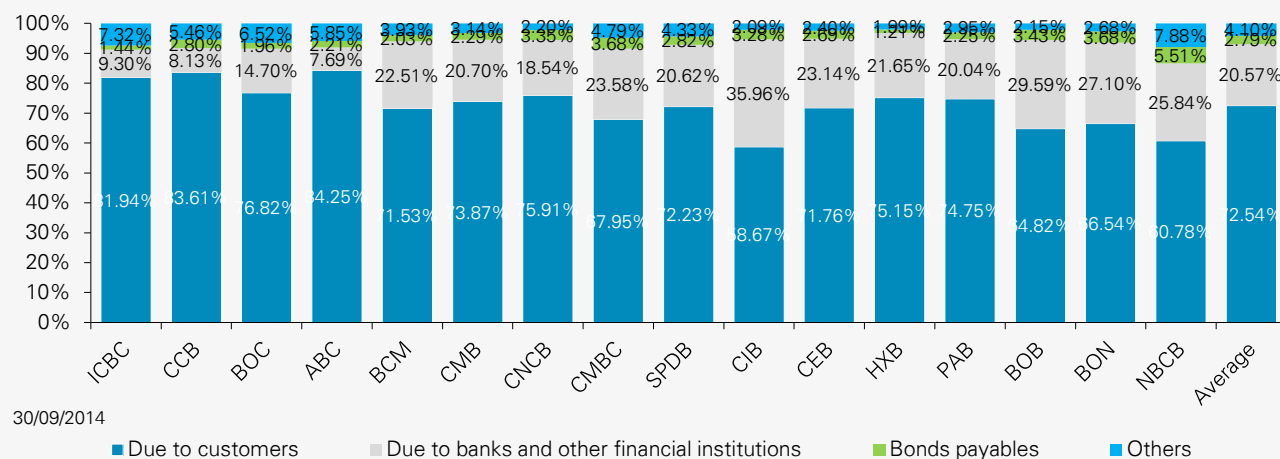


In the third quarter of 2014, the total scale of deposits of the listed banks was RMB 75.62 trillion, 7% more than that at the end of 2013. BON recorded the highest rate of increase at 32%, while CIB experienced the lowest increase of 2%. BCM recorded a decrease of 1%, mainly because internet finance and customer churn led to a loss of deposits.

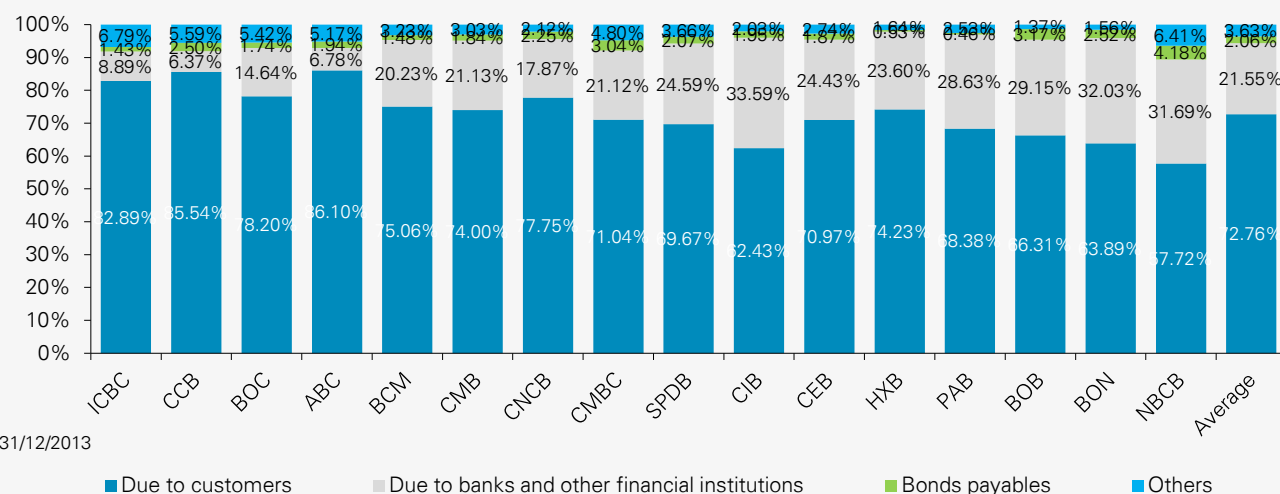
Although the total scale of deposits increased from that as at the end of 2013, the overall deposits decreased by RMB 950 billion during the third quarter according to the financial statistical reports issued by the People's Bank of China.

Condition of liabilities – Liability structure (continued)

Liability structure



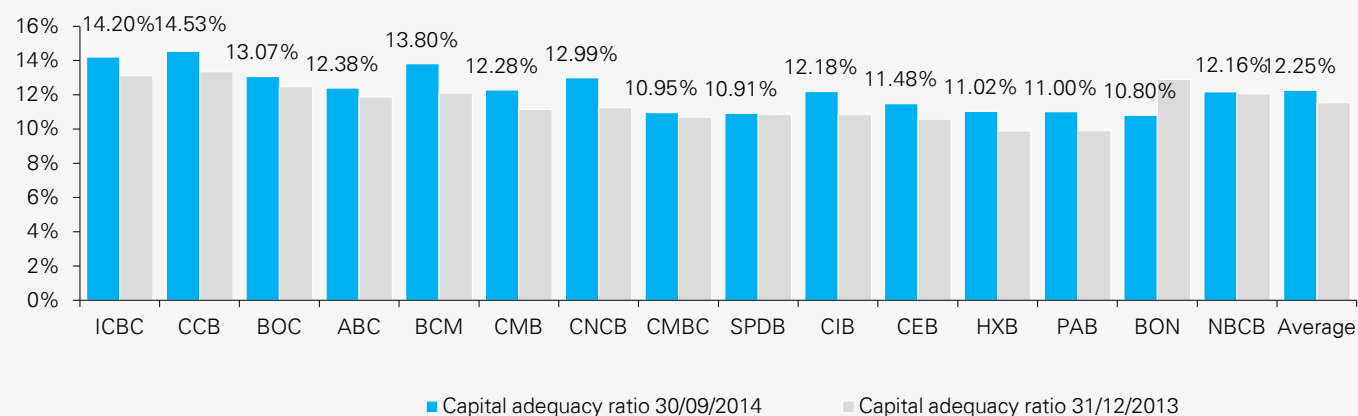
Liability structure



In the third quarter of 2014, customer deposits were the major component of the liabilities of the listed banks. The big five state-owned banks had higher rates, with ICBC, CCB and ABC each recording a rate of over 80%, reflecting their advantages in attracting deposits. Shareholding commercial banks and city commercial banks organized sources of funds based on the needs of resource allocation. Comparatively, they had a higher proportion of amounts due to banks and other institutions than the big five state-owned banks. CIB had a rate of 35.96%, mainly caused by the significant increase in deposits in other banks and financial institutions as well as repurchase agreements during this period.

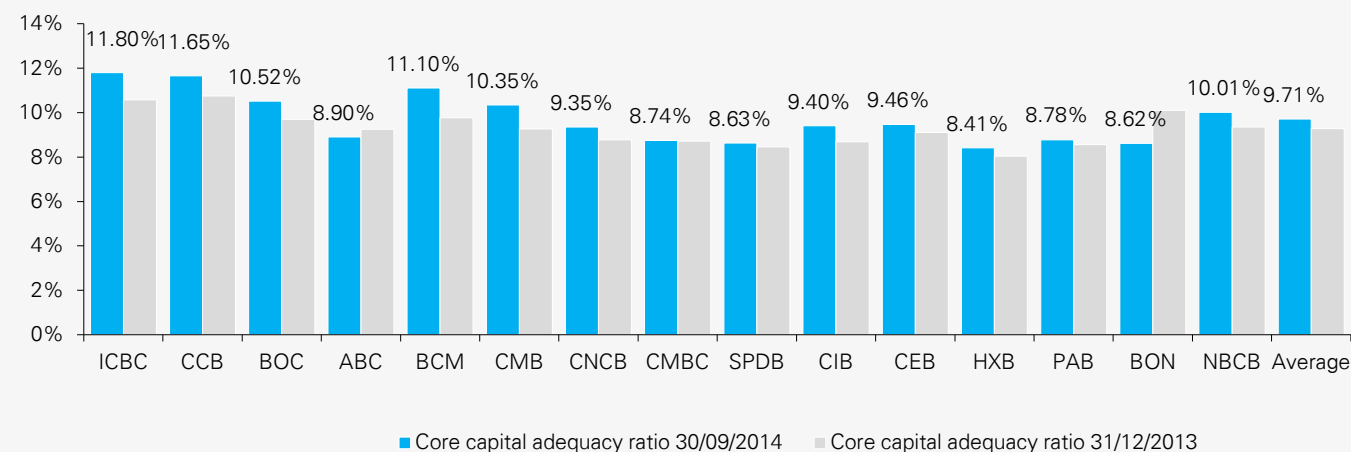
In the third quarter of 2014, the liability structure of the listed banks remained basically unchanged. ICBC, CCB and ABC maintained the highest rates of customer deposits and CIB had the highest ratio of amounts due to banks and other financial institutions. BON and PAB had significant changes to its liability structure, with the condensing of high cost liabilities from banks and other financial institutions as well as the expansion of low cost customer deposits. As a result, the liability structure improved and net interest margin uplifted.

Risk management – Capital adequacy ratio and core capital adequacy ratio



As at 30 September 2014, the capital adequacy ratios of the listed banks was 12.25%, 0.72 percentage points higher than that as at the end of 2013. The banks adjusted the ratio based on their own circumstances to meet regulatory indicators, while taking the optimization of equity holders' interest into account and maintaining a reasonable capital leverage structure.

CNCB experienced the highest increase of 1.75 percentage points. BCM also saw an increase of 1.72 percentage points. BCM adopted the advanced method of capital management in measuring the capital adequacy ratio at the end of June; therefore, the growth rate was affected by the change in the calculating method.



As at 30 September 2014, the average core capital adequacy ratio of listed banks was 9.71%, 0.44 percentage points higher than that of the end of prior year.

BCM saw the highest increase of 1.34 percentage points, which was mainly caused by the change in the calculating method.

Profitability - Profitability analysis

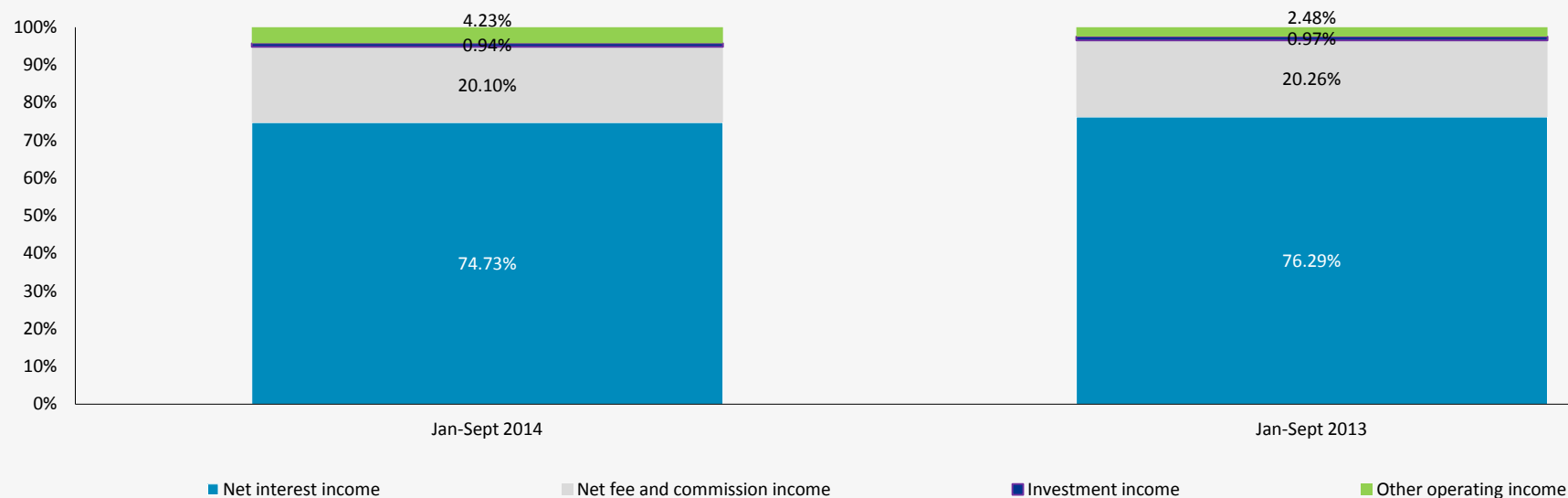
- The People's Bank of China announced a cut of the benchmark rate for one-year deposits by 25 basis points to 2.75% and the one-year lending rate by 40 basis points to 5.6%. It also lifted the upper limit of the floating band of deposit rates to 1.2 times the benchmark from the existing 1.1 times.
- The asymmetric interest rate cuts, especially the lift of the upper limit of the floating band of deposit, can be seen as a signal of interest market stimulation. This measurement is expected to increase the competitiveness of the bank deposit business. As the loan growth slowed, it is possible that the net interest margin will continue to narrow, affecting the profitability of banks.

- The banks' asset quality decreased, overdue and non-performing loans increased significantly, and the provisioning pressure for impairment loss increased as a result of the slowdown in the macro economy and the enlargement of credit risk.

- The regulators have strengthened inspection on service charges from banking financial institutions in order to reduce unreasonable charges for banking services, as well as illegal charging behavior, such as intentionally or objectively increasing the financing burden of enterprises, which has also limited the increase of traditional commission fee. Therefore, the listed banks have had to expand the intermediate business income channel through financial innovation.

- The expansion of business, as well as the establishment of new outlets and marketing channels, led to an increase in financial R&D and operating expenses, which brought bigger profitability pressures to the banks.

Profitability – Operating income and income structure analysis



The total operating income of the listed banks increased by 14.82% year-on-year in the first three quarters of 2014.

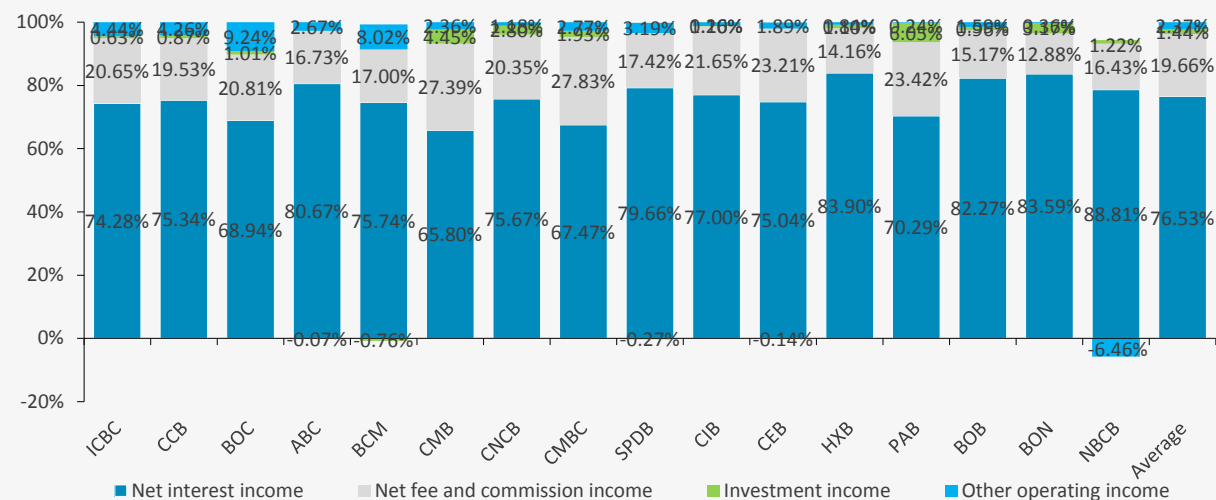
Components of operating income in the first three quarters of 2014:

- Net interest income accounted for 74.73% on average, decreasing by 1.56 percentage points year-on-year
- Net fee and commission income accounted for 20.10% on average, decreasing by 0.16 percentage points compared to the same period in the previous year
- Investment income accounted for 0.94% on average, decreasing by 0.03 percentage points compared to the same period in the previous year
- Other operating income accounted for 4.23% on average, increasing by 1.75 percentage points compared to the same period in the previous year. Other operating income mainly consists of gains from changes in fair value, exchange gains, and other income.

Source: The banks' 2013 annual reports & 2014 Q3 reports, KPMG China research

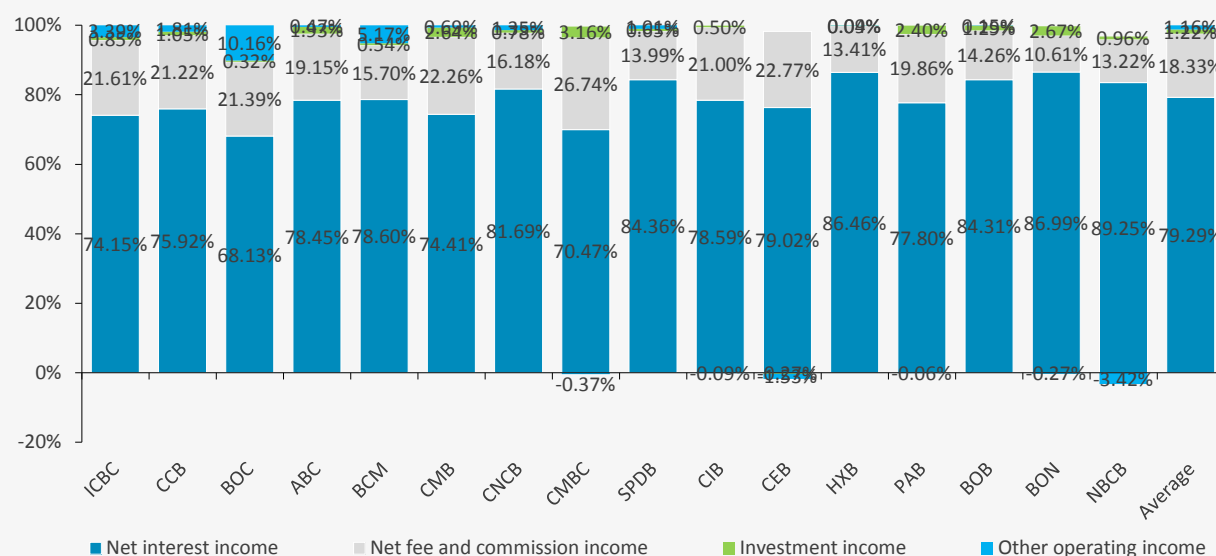
Profitability - Operating income and income structure analysis (continued)

2014 operating income structure of the first three quarters



During the first three quarters of 2014, the net interest income of the listed banks accounted for 76.53% on average, while net fee and commission income and investment income accounted for 19.66% and 1.44% respectively. Net interest income was the main source of operating revenue for the banks.

2013 operating income structure of the first three quarters

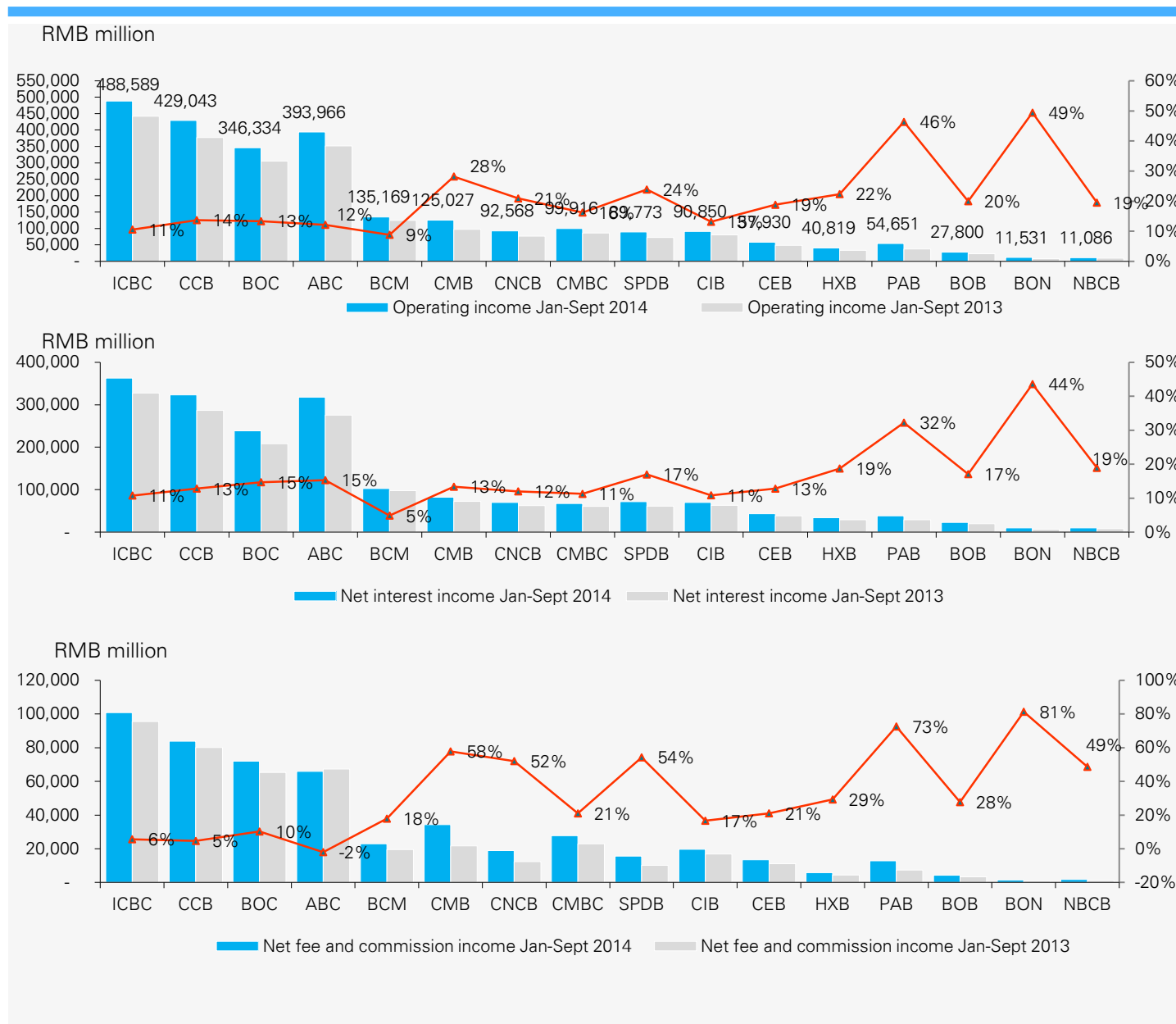


Compared to the first three quarters of 2013, the average ratio of net interest income of the listed banks decreased, mainly due to the narrowing net interest margin under the influence of interest rate liberalization.

During the first three quarters of 2014, the average ratio of net fee and commission income for the listed banks increased, mainly due to the increase in income sourced from intermediate business, which was driven by financial innovation.

BOC and BCM have the highest proportion of other operating income among listed banks. The significant increase of BCM was mainly contributed by the increase in gains from changes in fair value, while the increase in other operating income of BOC was mainly due to the increase in gains from changes in fair value as well as foreign exchange,

Profitability - Operating income and income structure analysis (continued)



During the first three quarters of 2014, all the listed banks experienced an increase in operating income, caused by the rise in the increase of net interest income and net commission income.

PAB and BON enjoyed an increase of over 40% due to the expansion of interest-bearing assets.

In addition, the net commission income of shareholding banks grew significantly faster than that of the four major state-owned banks.

During the first three quarters of 2014, all the listed banks experienced an increase in net interest income compared to the corresponding period in 2013. In the context of accelerating interest rate liberalization and the narrowing of net interest margin, the increase in net interest income was mainly derived from the continual growth of interest-bearing assets.

The net interest income of PAB increased by 32% compared to the corresponding period of 2013. The main reasons behind the increase are the growth of interest-bearing assets as well as the yield of return. The net interest income of BON also increased by 44% as a result of the growth of interest-bearing assets.

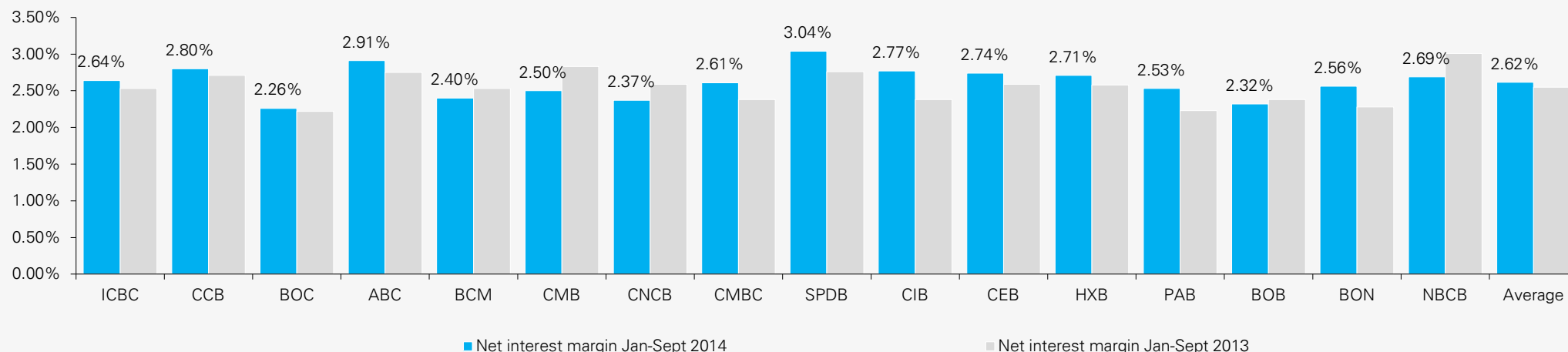
During the first three quarters of 2014, all the listed banks experienced an increase in net commission income compared to that of the corresponding period of the prior year. Though influenced by narrowing market interest margins, the banks proactively adjusted income structure and increased commission income by promoting financial innovation through exerting their comprehensive finance advantages, driving the significant income increase in the investment banking business, bank cards and custody business.

The net commission income of CMB has increased by 58% as a result of the increase in the commission of custody business. The net commission income of CNCB has increased by 52% as a result of the increase in bank card fee and consulting fee. The net commission income of SPDB has increased by 54% as a result of the increase in commission of wealth management and investment bank business. The net commission income of PAB has increased by 73% as a result of the increase in agency fee, bank card fee and consulting fee. The net commission income of BON has increased by 81% as a result of the increase in agency fee and consulting fee.

Source: The banks' 2013 annual reports & 2014 Q3 reports, KPMG China research

Profitability- Net interest margin

Net interest margin



During the first three quarters of 2014, the listed banks experienced an increase of 0.07 percentage points in average in net interest margin compared with that of the corresponding period of 2013. 11 out of 16 listed banks experienced an increase in their net interest margin.

CIB recorded the largest increase of 0.39 percentage points. CIB continued to optimizing the structure of its interest-bearing assets and adjusting its pricing strategy in order to improve the efficiency in utilizing its resources. The scale of CIB's interest-bearing assets was increasing steadily, resulting in a recovery of interest margin from last quarter.

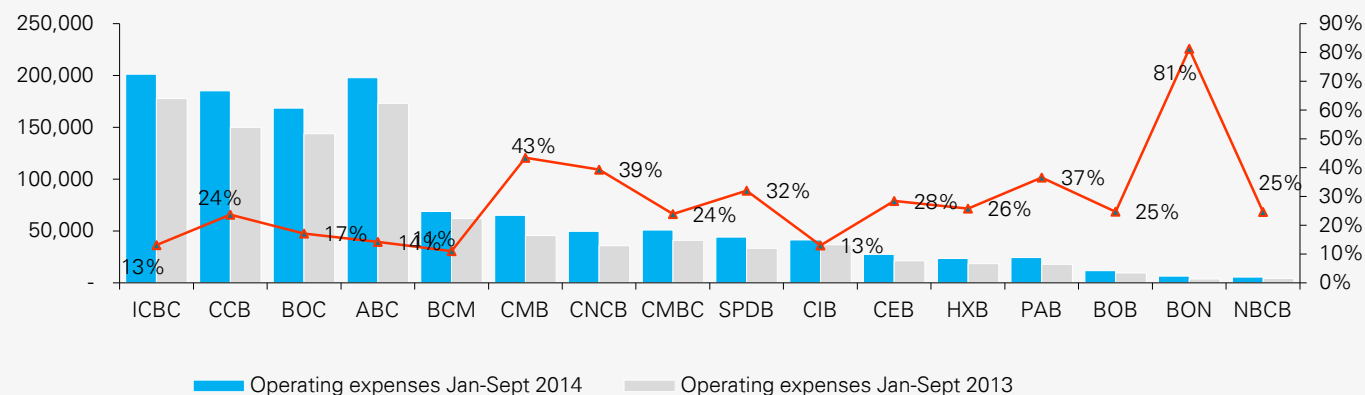
PAB experienced the second largest increase of 0.30 percentage points. This was mainly due to its continued effort in adjusting structure and pricing strategy.

On the other hand, the net interest margin narrowed for 5 banks, including BCM, CMB and CNCB, which were affected by loan repricing due to decreasing interest rate and by interest rate liberalization.

Source: The banks' 2013 annual reports & 2014 Q3 reports, Wind Info, KPMG China research

Profitability – Cost control – Cost-to-income ratio

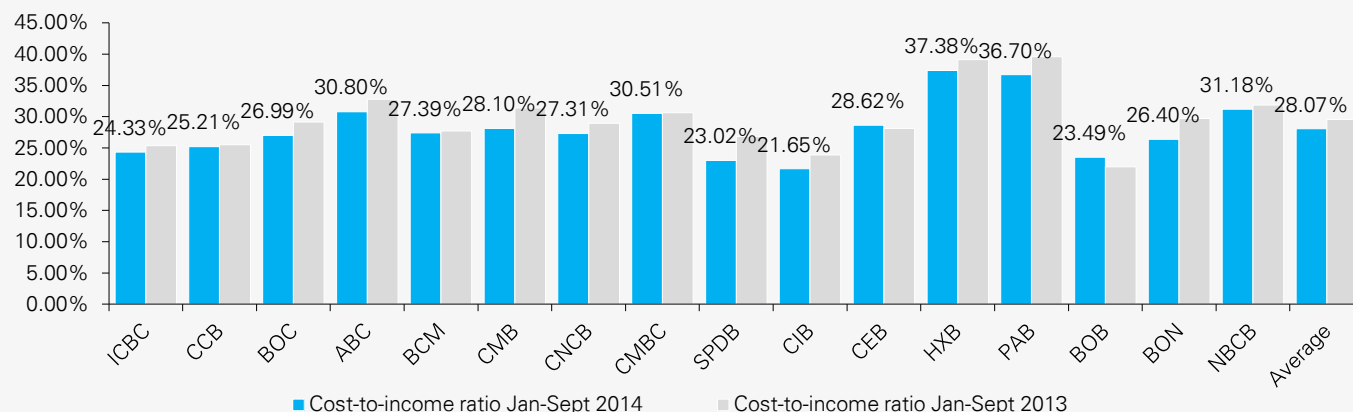
Operating expenses



The operating costs of all the listed banks increased in the first three quarters of 2014. The expansion of business scale and the increase in asset impairment loss drove the steady increase in the banks' operating costs.

BON, CMB and CNCB experienced the highest growth rates of 81%, 43% and 39%, respectively. The main reasons for the increase of BON is the increase in business scale as well as loan provision. The increase in loan provision also caused the growth of operating costs of CMB and CNCB.

Cost-to-income ratio

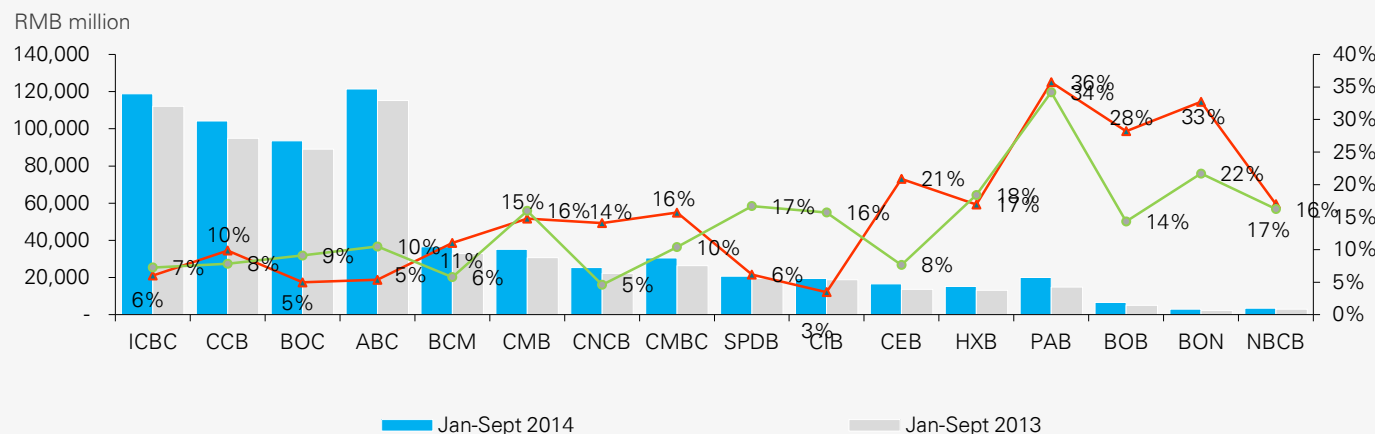


During the first three quarters of 2014, several banks experienced a decrease in their cost-to-income ratios, as a result of efficient cost control, refinement of operating expenses, and the comprehensive effect of asset structure optimization and rapid growth of intermediary business. SPDB experienced the sharpest decrease of 3.84 percentage points.

Nevertheless, considering the increasingly rigorous external regulations, as well as the listed banks' demand to remain competitive through continual innovation with respect to their products and services going forward, whether the low cost-to-income ratio can be sustained or not will be a key challenge facing the listed banks' profitability.

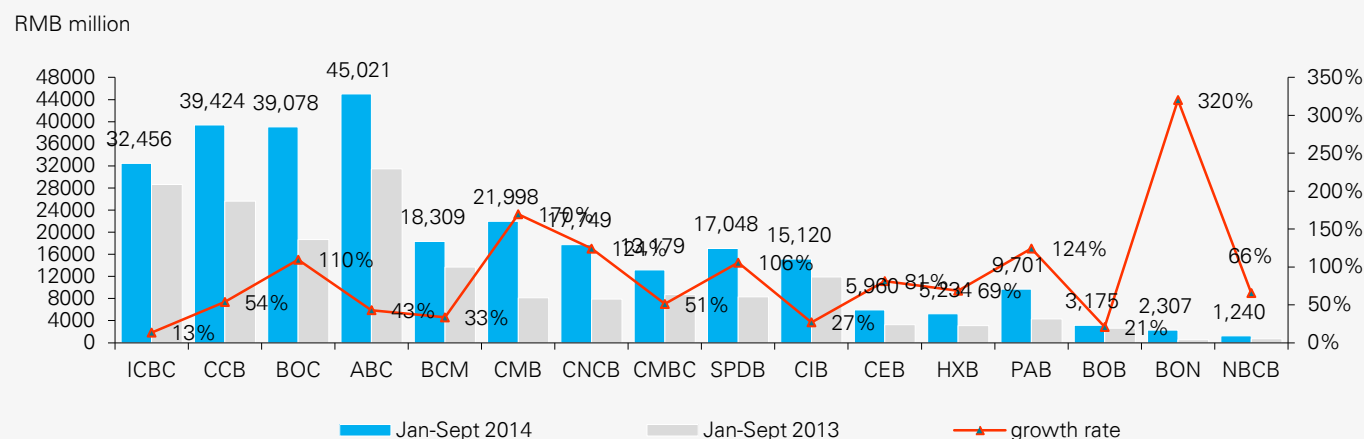
Profitability – Cost control – General and administrative expenses and impairment losses

General and administrative expenses



Overall, the listed banks saw an average increase of 9% in administrative expenses during the first three quarters of 2014. PAB and BON experienced the highest growth rate of 36% and 33% respectively among all the banks. This was mainly due to expansion in business scale and the establishment of new outlets.

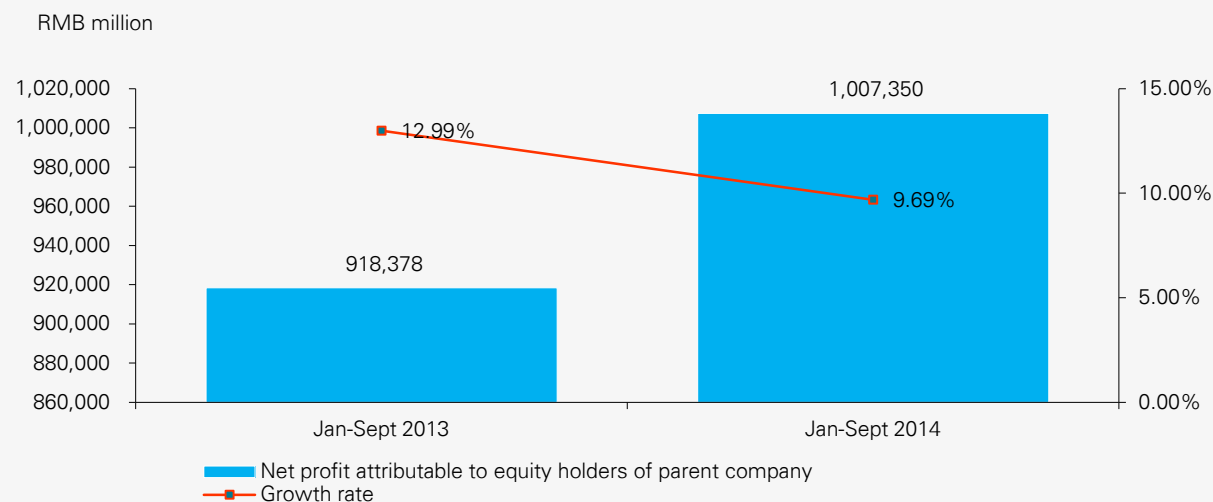
Impairment losses



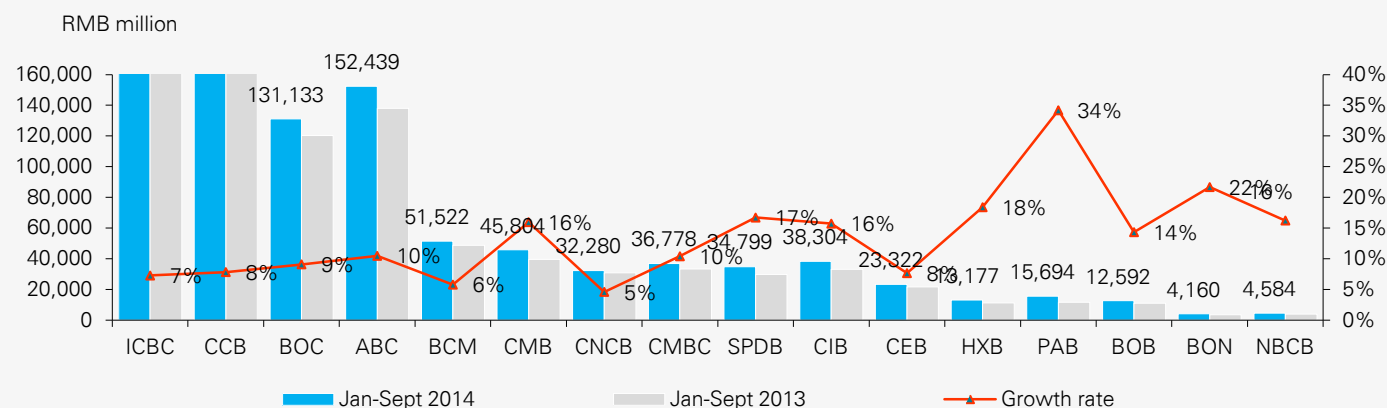
In the first three quarters of 2014, the banking industry increased loan provision for credit assets as a result of increased pressure of economic downturn and a decrease in asset quality. The impairment losses increased significantly to 61% on average, compared to 17% for the same period in the previous year.

BON and CMB experienced the highest increase in impairment losses of 320% and 170%, respectively, as a result of the sharp decrease in asset quality.

Profitability – Net profit attributable to equity holders of parent company



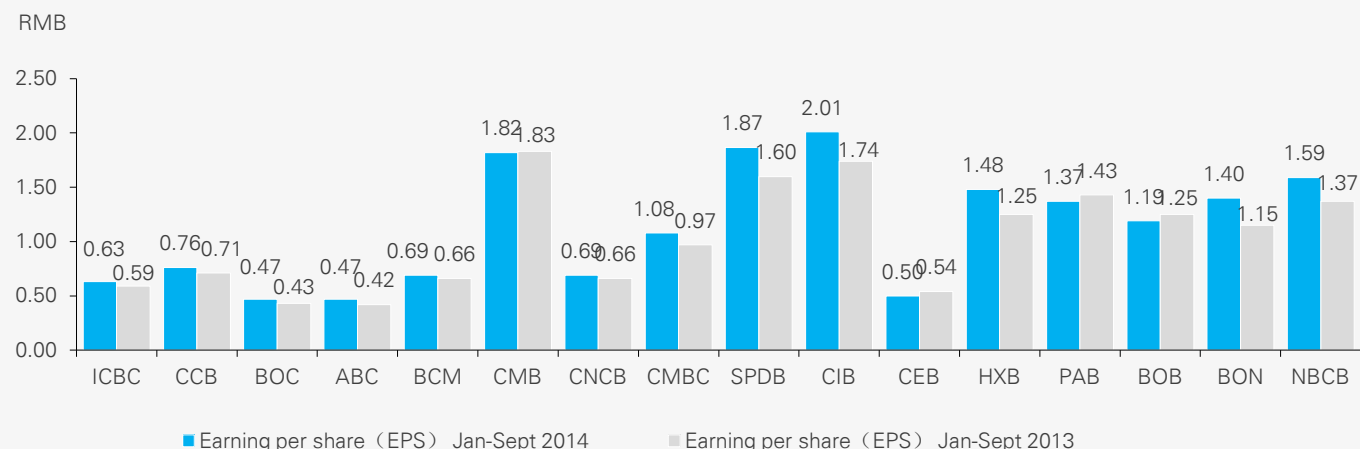
In the first three quarters of 2014, net profit attributable to equity holders of the parent company experienced an increase while the growth rate was obviously slower than that during the same period in 2013, falling from 12.99% to 9.69%.



In the first three quarters of 2014, net profit attributable to equity holders of the parent company of the listed banks decreased from double-digit average increase (since 2010) to 9.69%, which was mainly due to the increase in net interest income (13.26%).

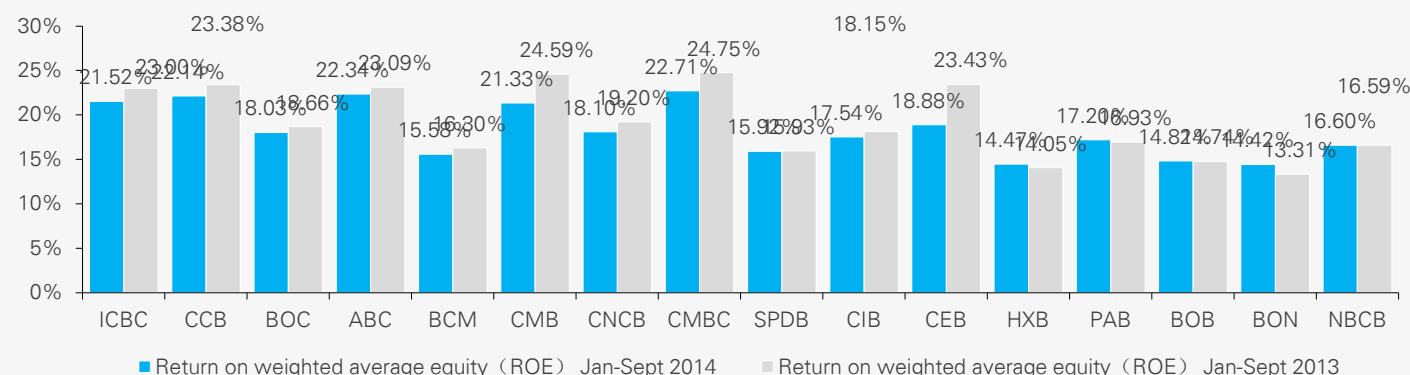
PAB enjoys the fastest grow rate of 34%. Net interest income has increased by 32.22%, or RMB 9.362 billion; net fee and commission income has increased by 72.58%, namely RMB 5.382 billion; other operating income has increased by 293.14%, or RMB 2.562 billion. The net profit growth rate of BON and HXB reached 22% and 18% respectively.

Profitability – Financial performance indicator



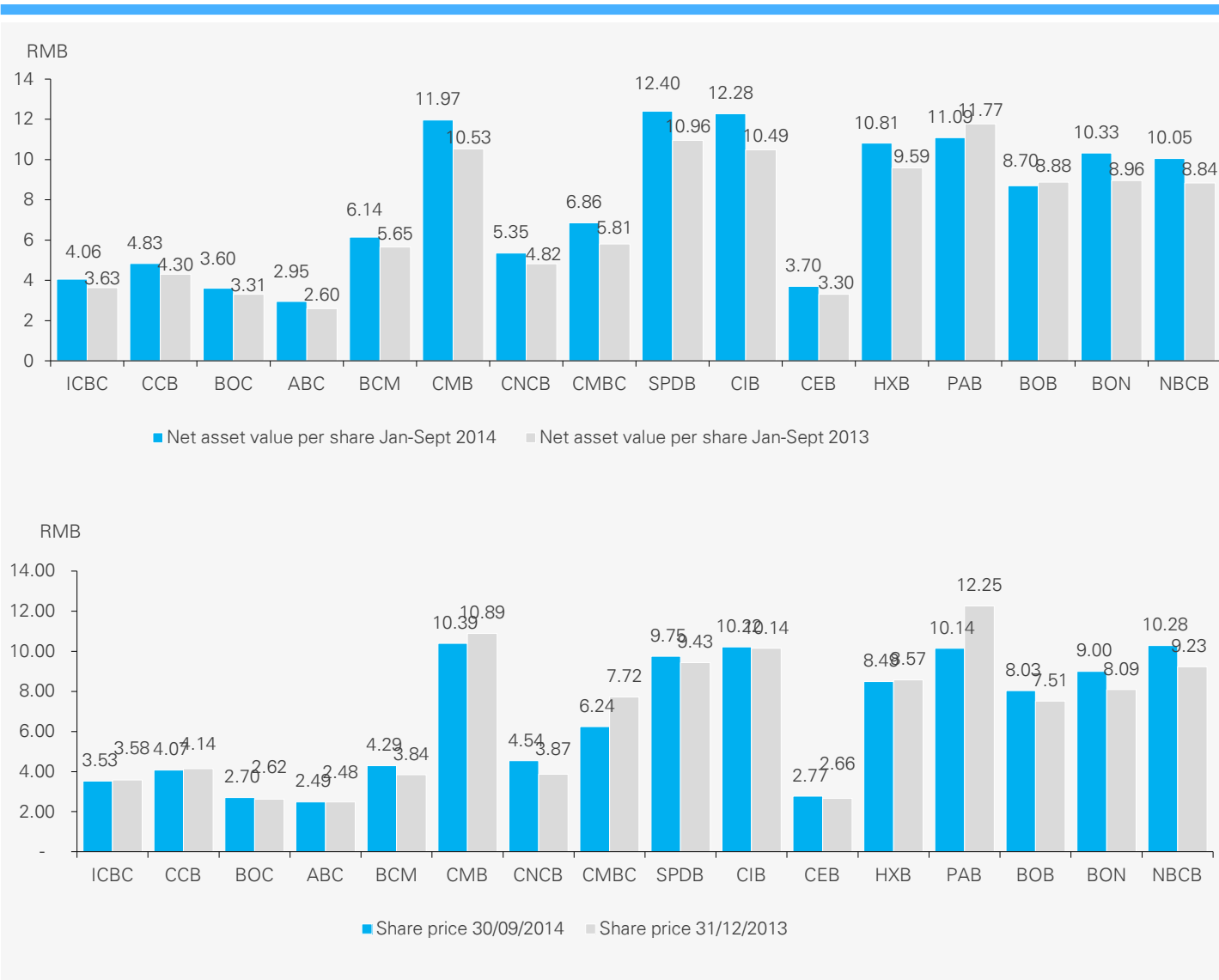
In the first three quarters of 2014, the listed banks experienced increasing earning per share (EPS), which was caused by higher income from banking business expansion. However, the increasing trend was weaker than that during the corresponding period in 2013 as a result of the overall market condition.

The EPS for some banks were even lower than that of the corresponding period in 2013. Among the 16 listed banks, the EPS of CMB, CEB, PAB and BOB decreased by 0.01, 0.04, 0.06 and 0.06 respectively from that of the corresponding period in 2013.



In the first three quarters of 2014, the return on weighted average equity (ROE) of the listed banks decreased by 0.91% compared to that of the corresponding period in the prior year, mainly due to the flattening increase in net profit and the increased net assets in line with the expansion of banking business. CEB and CMB saw a higher rate of decrease at 4.55 percentage points and 3.26 percentage points respectively.

Profitability – Financial performance indicator (continued)



In the first three quarters of 2014, the net asset value per share of all the listed banks maintained the trend of increase. The only exception is BOB, whose net asset value per share decreased from RMB 8.88 as at the end of 2013 to RMB 8.70 as at the end of September 2014.

SPDB had the highest net asset value per share at RMB 12.40, an increase of RMB 1.44 during the three quarters.

In contrast, CIB achieved the highest amount of increase of RMB 1.79 per share.

Investors were cautiously optimistic as the macro economy slowed down and the stock market remained sluggish.

Six out of 16 listed banks experienced a drop in their share price in the first three quarters of 2014.

Influenced by the downward economy and the decrease in asset quality, some of the banks with higher proportion of credit assets from small and micro businesses faced much more pressure. For instance, CMBC suffered a drop in share price of 19%. PAB's share price also dropped by 17%. This was mainly caused by the cash dividend distribution and capital reserve transferred to equity in the first half of 2014.

03



Hot topics

Background information

An interconnection with the mainland market has been a strategy of the HKEx for years. The HKEx has made moves, but there has been no breakthrough due to the delay in liberalizing RMB capital accounts.

- **“Through-train”**

In August 2007, the State Administration of Foreign Exchange released *Pilot Program of Direct Investment in Overseas Securities Markets by Domestic Individuals*, intending to launch a pilot program in Tianjin for individuals in the mainland to directly invest in Hong Kong stocks. Many mainland scholars and officials pointed out that this pilot was meant to relax capital controls, and thus it would be difficult to control cross-border inflows and outflows of a large amounts of hot money. By the end of 2007, Premier Wen Jiabao made it clear that the “through-train” was facing four challenges: whole flows of the mainland capital market would need to be under appropriate regulatory oversight; a large amount of funds flowing into Hong Kong would affect its market stability; investors were in need of risk education; and lastly, various parties including Hong Kong authorities would have to be consulted to avoid decision-making bias. These reasons coupled with the global financial crisis caused by the US subprime mortgage crisis postponed the “through-train” indefinitely.

- **QDII2**

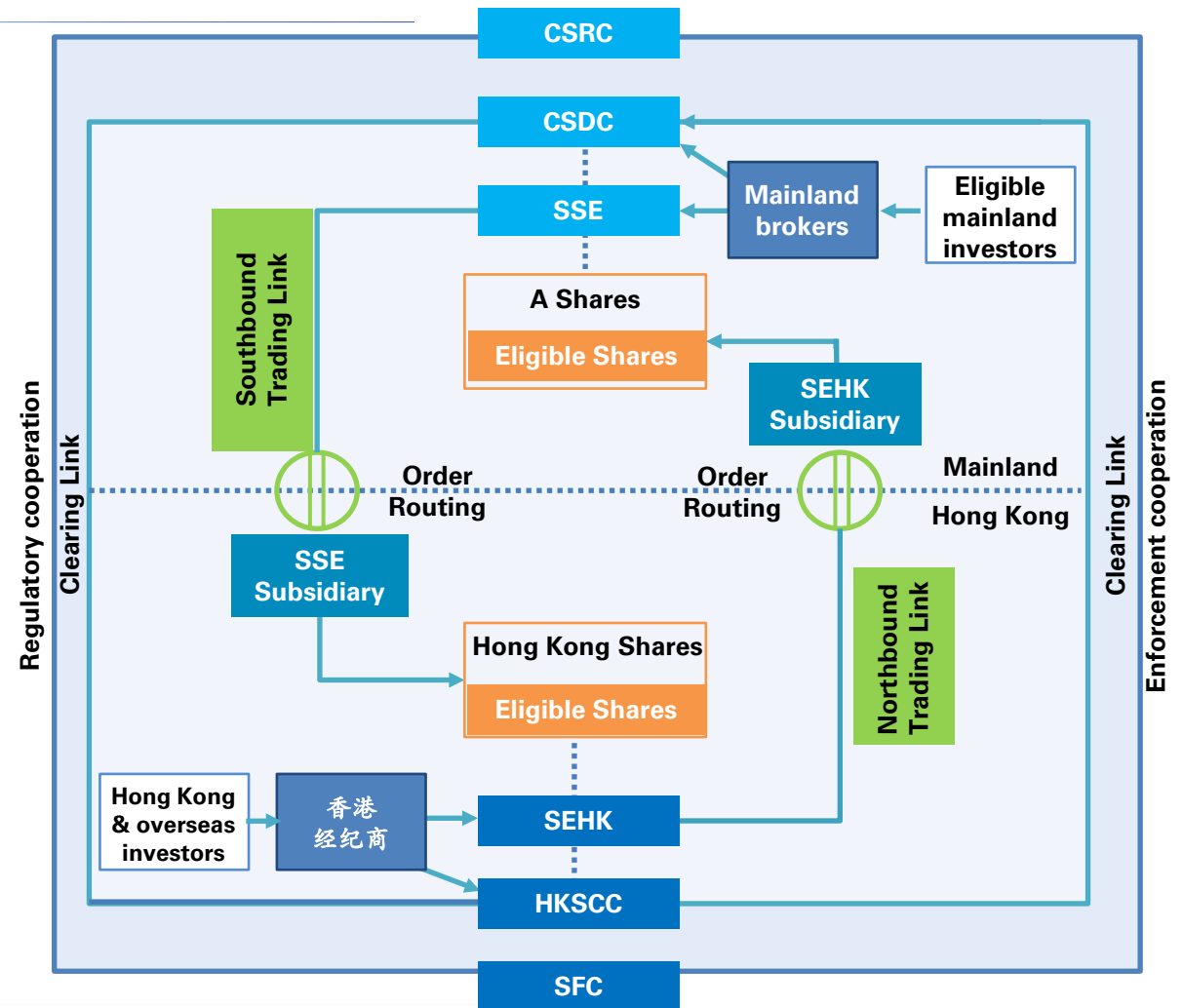
China began to make arrangements for QDII in 2003. On 5 July 2007, *Pilot Rules on the Administration of Overseas Securities Investment by Qualified Domestic Institutional Investors* and *Notice of China Securities Regulatory Commission (CSRC) on the Issues concerning the Implementation of the Pilot Rules on the Administration of Overseas Securities Investment by Qualified Domestic Institutional Investors* promulgated by the CSRC took effect. With investment quotas under control, QDII products provided mainland investors indirect channels to buy Hong Kong stocks. During 2011-2012, the Chinese Securities Association of Hong Kong and several regional securities regulatory bureaus proposed in “QDII2” or “Qualified Domestic Individual Investors” plans to use QDII quotas to attract mainland high net worth individuals to invest into Hong Kong stocks. On 14 January 2013, Guo Shuqing, a former chairman of the CSRC, said on Asian Financial Forum that interaction of funds between the mainland and Hong Kong should be promoted, and introduction of individual investors should be taken into account. Subsequently, at the 2013 working conference of The People’s Bank of China, the central bank proposed to make good arrangements for QDII2 pilot; it was the first time for the central bank to mention the QDII2 pilot publicly. Those in the industry presumed that QDII2 would be launched in 2013 with a quota of approximately USD 50 billion and the investor eligibility requirement of RMB 0.5-1 million in personal liquid assets. However, QDII2 has not been implemented yet.

- **Shanghai-Hong Kong Stock Connect**

In June 2009, Charles Li was appointed as the CEO of HKEx. He has made drastic reforms, the most significant of which has been to shift the focus of HKEx to “interconnection” with the mainland. “Interconnection” refers to networking between trading platforms in the mainland and Hong Kong. In addition to stock spot, derivatives, RMB products and commodities were also intended to be covered. However, RMB capital account liberalization is still the key to the implementation of the “interconnection”. The “Shanghai-Hong Kong Stock Connect” is a pioneering attempt. Without changing local institutional rules and market transaction practices, a two-way, all-dimensional, closed operating, scalable and risk controllable open market structure has been established for the first time, winning precious time and space for the gradual reform of systems and rules.

Trading structure

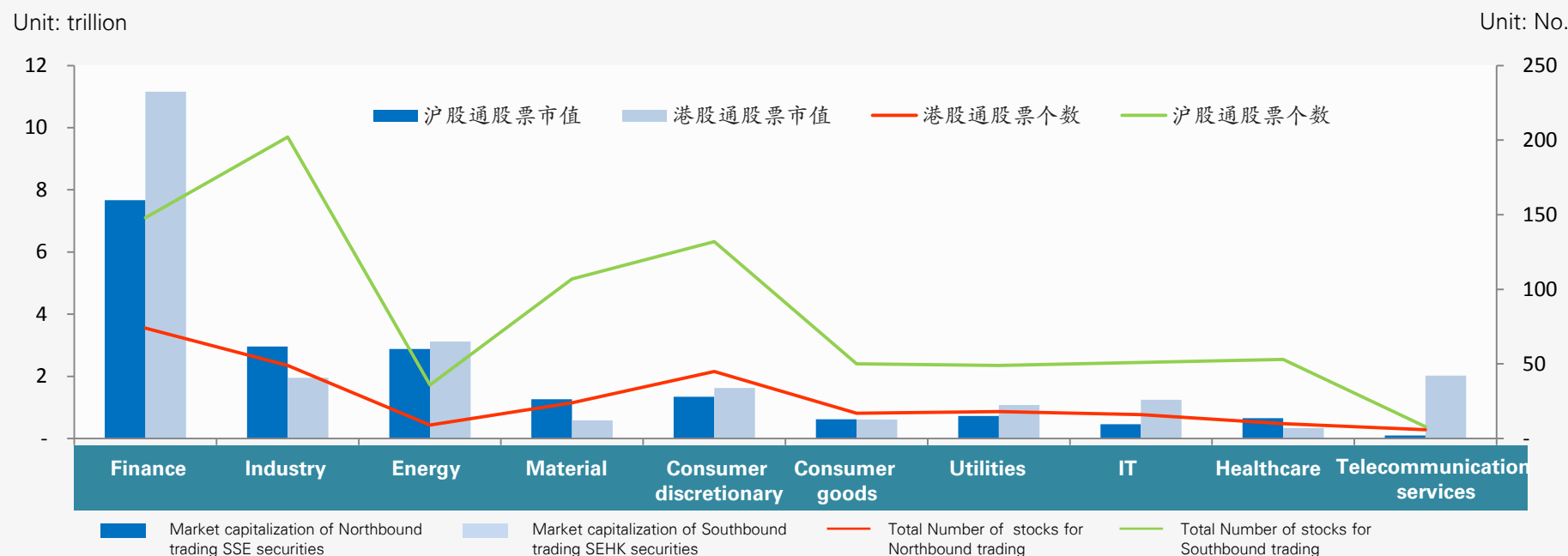
- Shanghai-Hong Kong Stock Connect comprises a Northbound Trading Link and a Southbound Trading Link.
- Under the **Southbound Trading Link**, eligible investors, through mainland securities firms and a securities trading service company to be established by the SSE, will be able to place orders to trade eligible shares listed on the SEHK by routing orders to the SEHK.. Stocks bought and sold by domestic investors in Hong Kong securities market are **quoted in Hong Kong dollars with RMB as the currency of payment**.
- Under the **Northbound Trading Link**, investors, through their Hong Kong brokers and a securities trading service company to be established by the Stock Exchange of Hong Kong (SEHK), will be able to place orders to trade eligible shares listed on the Shanghai Stock Exchange (SSE) by routing orders to the SSE. **Stocks are quoted in RMB with RMB as the currency of payment. Swaps are handled by China Securities Depository and Clearing Corporation Limited (CSDC) in Hong Kong.**



Implementation

Date	Document	Main content
10 April 2014	Joint Announcement of China Securities Regulatory Commission and Securities and Futures Commission	The CSRC and the Securities and Futures Commission (SFC) have approved, in principle, the development of a pilot program (Shanghai-Hong Kong Stock Connect). When launched, the pilot program will operate between the SSE, the SEHK, China Securities Depository and Clearing Corporation Limited (ChinaClear) and Hong Kong Securities Clearing Company Limited (HKSCC). The following principal elements are set out: clearing, eligible shares, quotas and eligible investors. The SSE, SEHK, ChinaClear and HKSCC will, during the development of Shanghai-Hong Kong Stock Connect, and prior to launch, liaise with market participants in relation to all rules, systems and technical requirements relevant to their operations, and trading and settlement cooperation agreements will be reached. It should take approximately six months from the date of this announcement to complete the preparation for formal launch.
13 June 2014	Certain Provisions on Shanghai-Hong Kong Stock Connect Pilot Program	Released by the CSRC, this comprised 19 articles of provisions. Its main content covers responsibilities of the SSE and SEHK; responsibilities of securities trading services companies; responsibilities of the CSDC and HKSCC; responsibilities of mainland securities companies; shareholding quotas for domestic equities by foreign investors; interest entitled to investors who buy shares under Shanghai-Hong Kong Stock Connect.
4 September 2014	Four-party Agreement	The SEHK and HKSCC signed a four-party agreement with the SSE and ChinaClear, the foundation for the cooperation of the four parties. The Four-party Agreement makes arrangements for Trading Links and Clearing Link. The main agreements on Trading Links are as follows: 1. establishment of the order-routing arrangements; 2. shares eligible to be traded through the Trading Links; 3. applicable trading currencies; 4. ban on grey market trading; 5. development and launch of derivatives; 6. applicable laws and rules; 7. rule and procedure amendments; 8. agreements on Trading Links and Clearing Link; 9. revenue sharing; 10. conditions.
26 September 2014	SSE Measures for Pilot Program of SHSECM SSE Guidance of Investor Suitability Management for Buying and Selling Stocks of SEHK-listed Companies	Promulgated by the SSE, SSE Measures for Pilot Program of SHSECM contains the main rules of the SSE in the Shanghai-Hong Kong Stock Connect business, stipulating the basic model and specific requirements to conduct relevant transactions in full detail. There are six chapters and 124 articles in total, whose main content is as follows: 1. Northbound Trading Link. A stock exchange under the SEHK must apply for eligibility to participate in SSE trading; eligible shares and relevant transfer rules; special institutional arrangements for trading, order types, margin trading and naked short selling; quota control formula and the approach to dealing with the situation when a quota limit is reached; measures to handle the situation when shareholding ratio limit is reached. 2. Southbound Trading Link. Suitability requirements for investors to participate in Southbound trading and how to participate in Southbound trading; the means in which a member participates in Southbound trading and relevant requirements; eligible shares and relevant transfer rules; quota control formula and the approach to dealing with the situation when a quota limit is reached; the arrangements for designated trading, third-party custody, and front control over funds and securities same as A shares. 3. Trading exception handling. 4. Self-management.
17 October 2014	Memorandum of Understanding between the CSRC and the SFC on Strengthening of Regulatory and Enforcement Cooperation under Shanghai-Hong Kong Stock Connect	<i>Memorandum of Understanding between the CSRC and the SFC on Strengthening of Regulatory and Enforcement Cooperation under Shanghai-Hong Kong Stock Connect</i> (hereinafter referred to as the "MoU") was co-signed by the CSRC and SFC, thus institutional arrangements for cross-border regulatory cooperation between the mainland and Hong Kong under the Shanghai-Hong Kong Stock Connect were made. It mainly covers: 1. purpose and validity of the MoU; 2. a joint mechanism for notification of alerts and exchange of investigatory information; 3. investigatory assistance and joint investigation procedures and relevant arrangements; 4. use of information, including scope of use and confidentiality of information; 5. service of documents; 6. mutual assistance in execution of orders under Shanghai-Hong Kong Stock Connect; 7. miscellaneous, including investor compensation, publication of information, consultation and regular liaison, internship, training and secondment programmes for enforcement staff.
10 November 2014	Joint Announcement of China Securities Regulatory Commission and Securities and Futures Commission	The announcement stipulates that stock trading under Shanghai-Hong Kong Stock Connect begins on 17 November 2014.
14 November 2014	Notice on Tax Policies on Shanghai-Hong Kong Stock Connect Pilot Program	The notice was jointly issued by the Ministry of Finance, State Administration of Taxation and CSRC. Policies on income tax, business tax and stock trading stamp duty and other tax policies in connection with Shanghai-Hong Kong Stock Connect pilot program are explicitly stipulated.

Eligible securities



Northbound Trading Link

Eligible shares: SSE 180 Index, SSE 380 Index, SSE-SEHK A+H; ST, * ST shares, B shares are excluded

Total No of Stocks*: 568 (including 69 A+H shares)

Proportion accounted for by eligible shares in SSE A shares by number: 59%

Market Capitalization:** RMB 18.69 trillion

Proportion accounted for by eligible shares in SSE A shares by market capitalization:** 90%

Average Daily Turnover*:** RMB79.5 billion

Maximum Aggregate Quota: RMB 300 billion

Daily Quota: RMB 13 billion



Southbound Trading Link

Eligible shares: HS LargeCap, HS MidCap, SSE-SEHK A+H

Total No of Stocks*: 268 (including 69 A+H shares)

Proportion accounted for by eligible shares in H shares by number: 15%

Market Capitalisation:** RMB 23.74 trillion

Proportion accounted for by eligible shares in H shares by market capitalisation:** 68%

Average Daily Turnover*:** Approximately RMB 30 billion

Maximum Aggregate Quota: RMB 250 billion

Daily Quota: RMB 10.5 billion

* The updated list on the HKEx website as of 24 October 2014

** Data from WIND Information as of 30 September 2014

*** Data for Jan-March 2014 from WIND Information

Trading rules and arrangements

	Northbound trading	Southbound trading
Rules	"Home Market" rules and laws apply to the extent possible with respect to trading and settlement, price limit, tax rates etc. No price limit for Southbound trades.	
Trading day	Open when both the SEHK and SSE are open for business and banking services of both markets are open on the corresponding money settlement days.	
Order type	At-auction limit order only; market order not allowed.	At-auction limit order or enhanced limit order
Margin trading and securities lending	<p>Currently, Mainland investors can only conduct margin trading in certain A shares that the SSE has determined are eligible for margin trading, and stock borrowing and lending. Hong Kong and overseas investors conducting margin trading in SSE securities via the Shanghai-Hong Kong Stock Connect will be subject to a similar restriction.</p> <p>Regarding stock borrowing and lending, the input price of a short selling order must not be lower than the last traded price (and in the absence of the last traded price, the previous closing price). The price requirements apply with respect to the input price of sale of the same amount of borrowed stocks for naked short selling prior to return of the borrowed stocks, with any exceeding amount being excluded. In respect of each SSE security, restrictions will be imposed on the total quantity that can be short sold: (i) on each trading day (i.e. 1% of HKSCC's holding of that security in the omnibus account maintained in ChinaClear); and (ii) for a rolling period (i.e. 5% for 10 trading days);</p> <p>Hong Kong and overseas investors cannot participate in the Margin Trading and Securities Lending Programme provided by the SSE in mainland China but short selling of A shares will be permitted for HK investors in early 2015 according to the SEHK.</p>	Margin trading and securities lending is pending to separate arrangement by SSE.
Shareholding restriction	For SSE securities purchased through the Shanghai-Hong Kong Stock Connect, shareholding restriction, information disclosure and forced-sale rules will be considered in totality with those purchased by QFII and RQFII.	No single investor shareholding restriction is provided in existing regulations in HK SAR.
Eligible investors	Single foreign investors' shareholding in an A share must be $\leq 10\%$ of the total issued shares; the aggregate of foreign investors' shareholding in an A share must be $\leq 30\%$ of the total issued shares. Approved strategic investment in an issuer by a foreign investor is not subject to the above restrictions.	Initially, the SFC restricts participants in southbound trading to institutions and single investors with a securities/funds balance of not less than RMB 0.5 million.
Share transfer out	Only selling is permitted after a stock is no longer eligible for northbound and southbound trading.	
Calculation of quota	Daily Quota Balance: Daily Quota – Buy Orders + Sell Trades + Adjustments (e.g. Buy Order cancelled, Buy Order rejected by SSE, Buy Order executed at a better price); Aggregate Quota Balance: Aggregate Quota – Aggregate Buy Trades + Aggregate Sell Trades	

Tax arrangements

Northbound trading of SSE securities

Income tax

Business tax

Stamp duty

Capital gains

From 17 Nov 2014, gains from transfer of A-shares in SSE by Hong Kong investors (corporations/individuals) are provisionally exempt from corporate and individual income tax.

Dividends

From 17 Nov 2014, Hong Kong investors (corporations/individuals) shall pay income tax at a 10% rate on dividend income from investment in A-shares.

From 17 Nov 2014, gains from transfer of A-shares in SSE by Hong Kong investors (corporations/individuals) are provisionally exempt from business tax.

From 17 Nov 2014, the sale, inheritance and donation of A-shares in SSE by Hong Kong investors are subject to stamp duty in accordance with existing mainland tax laws and regulations.

Southbound trading of SEHK securities

Income tax

Business tax

Stamp duty

Capital gains

From 17 Nov 2014 to 16 Nov 2017, gains from transfer of SEHK shares by mainland individual investors are exempt from income tax for a period of three years; corporate investors shall pay income tax for such gains.

Dividends

Dividend income from investment in SEHK shares by mainland corporate investors and individuals is subject to corporate and individual income tax.

Individuals (including individual households and others) are exempt from paying business tax for the sale of securities while corporate investors shall pay business tax at a 5% rate on the buy-sell price difference.

From 17 Nov 2014, the sale, inheritance and donation of SEHK shares by mainland investors are subject to stamp duty in accordance with existing tax laws in Hong Kong SAR.



RMB internationalization

- Daily quota for northbound trading of SSE securities and southbound trading of SEHK securities is RMB 13 billion and RMB 10.5 billion, respectively. The deals are settled in RMB. In other words, the clearing centre under SEHK will have to exchange RMB with HK dollars before going to ChinaClear. This will result in an outflow of RMB 10.5 billion to HK and an inflow of RMB 13 billion to the mainland. The frequent exchange of currencies in Hong Kong reflects the enhanced needs of RMB in an offshore RMB centre.

Drawing international investors to Shanghai market

- A-share investors are dominated by individuals and HK investors by institutional investors. The institutional investors prefer blue chip shares with better dividend-paying prospects and tend to value these shares favorably. Consequently, the Shanghai-Hong Kong Stock Connect will enhance the investment value of blue chip shares in the mainland.

Incoming international funds as additional lifeblood for sustainable development

- The A-share market is relatively closed, with overseas investors accounting for less than 1%, in contrast to 61% of overseas participants in the Hong Kong market. With the launch of the Shanghai-Hong Kong Stock Connect, overseas investors will take an interest in stocks that are relatively under-valued and scarce, i.e. blue chip shares, which will provide rallying momentum to the A-share market.

Implications

Convenience for mainland investors with an aim of diversification

- Among the eligible stocks, 69 of the A+H shares represent 26% of total, and a large quantity of Hong Kong issuers are on the eligible SEHK securities list. Current market expectations are that the probability of USD appreciation relative to RMB is high, and HK stocks could be viewed as USD assets since the HKD is pegged to the USD. Some investors opting for USD denominated assets may turn to stocks on the SEHK.

Price discovery of A+H shares

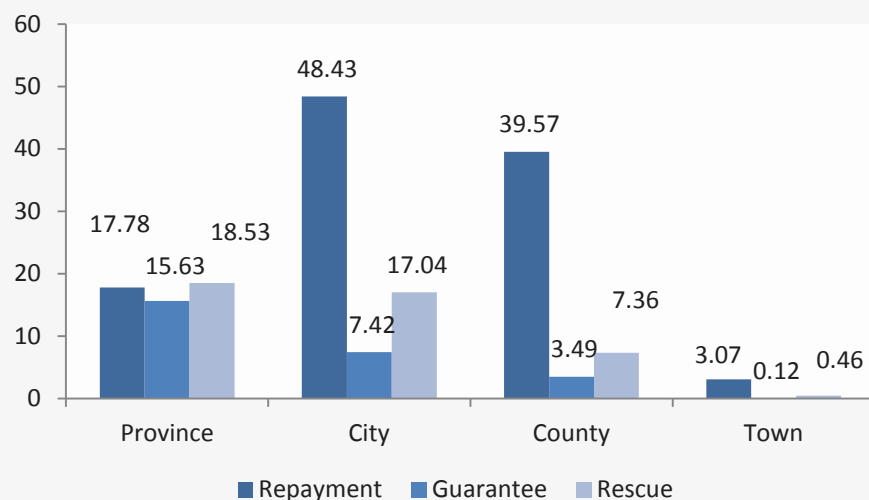
- Among the 67 A+H issuers in China Connect, 43 (mainly industrial companies) carry a premium of A against H shares and 23 (mainly financial entities) show a discount A against H shares. On the other hand, the valuation of certain Hong Kong stocks as lower than A-shares is appealing. As at June 2014, A+H shares were in a low discount/premium valuation range, with a general 10% discounts in valuation of high-capitalization, high-dividend A-shares. This could be explained in terms of risk-free interest rate, investor structure, rationale, and expectations as well as scarcity; nevertheless, arbitrage players could be drawn in by China Connect to narrow the discount range of valuation.



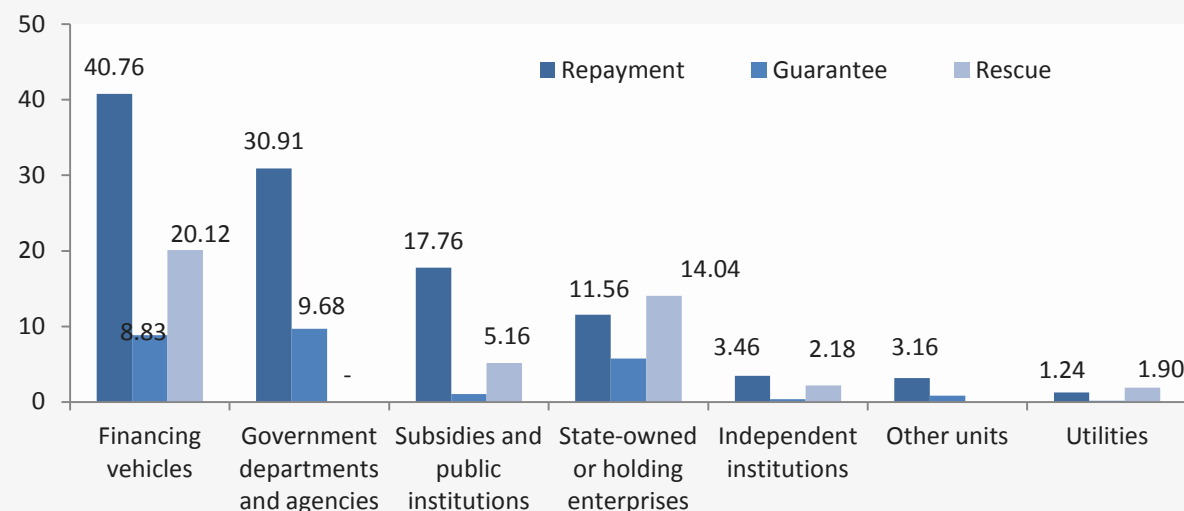
- The audit report of government debt indicates that as at 30 June 2013 the government was directly responsible for repayment of a total debt of RMB 10.89 trillion, and had guaranteed liability debt of RMB 2.67 trillion and potential rescue liability debt of RMB 4.34 trillion. The audit covered government debt arising from 31 areas (provinces, autonomous regions and municipalities), five cities listed independently in the state plan, 391 other municipalities (cities, prefectures, leagues, districts), 2,778 counties (cities, districts, qis), and 33,091 townships (towns, sumus). Following is the analysis, respectively by local government level, borrower, capital source, expenditure direction and maturity.

Unit: RMB, hundred billion

Analysis by government level

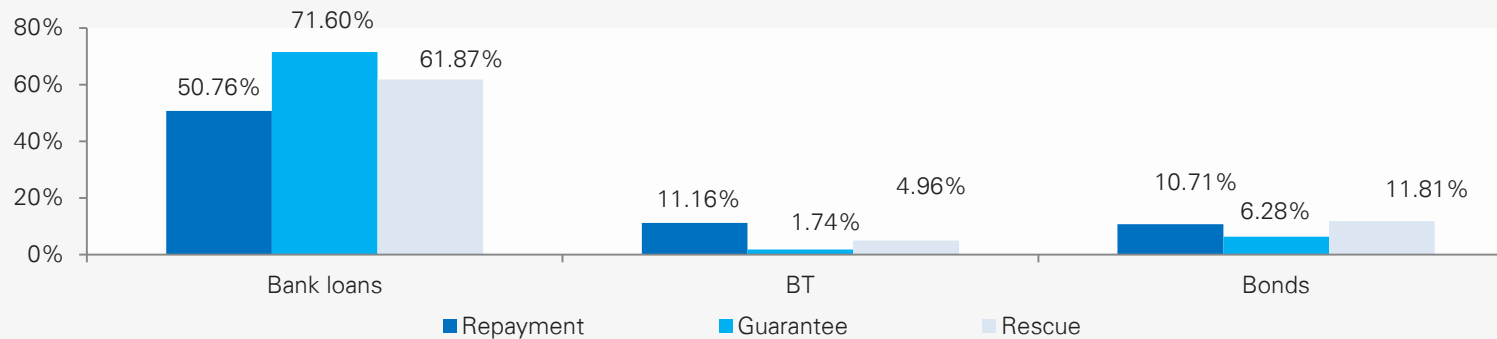


Analysis by borrower



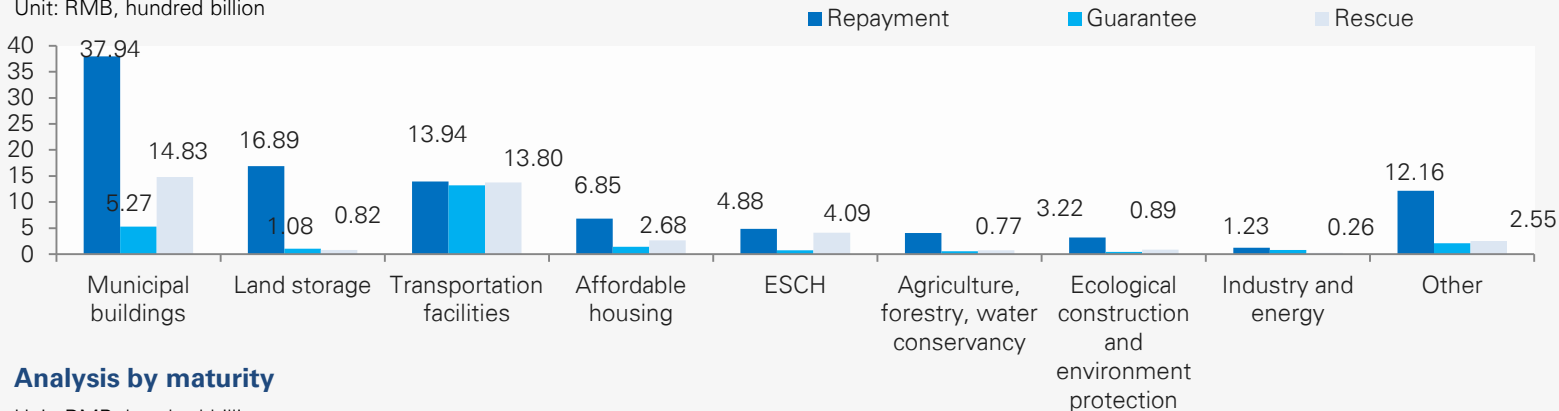
Source: 2013 Audit Report of Government Debt released by China National Audit Office

Analysis by capital source



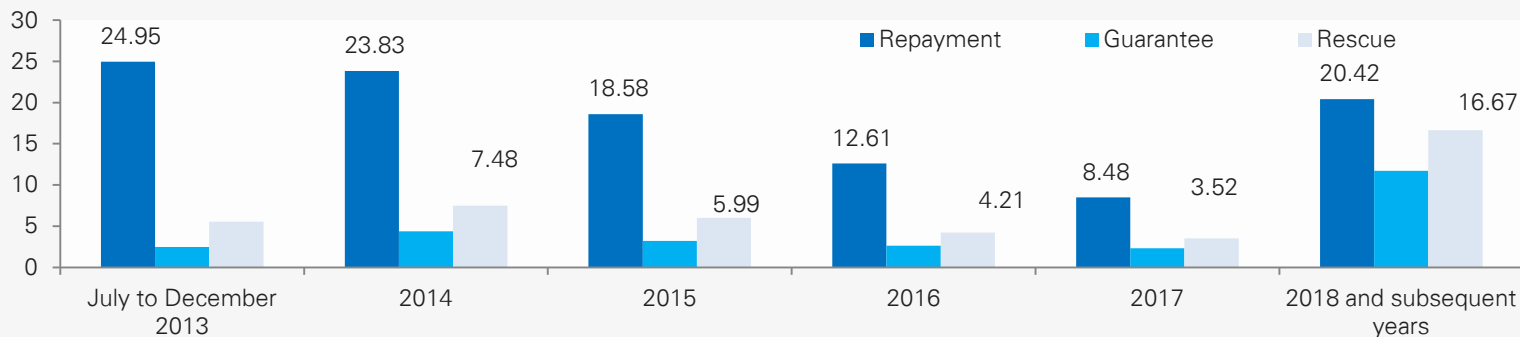
Analysis by expenditure direction

Unit: RMB, hundred billion



Analysis by maturity

Unit: RMB, hundred billion



Source: 2013 Audit Report of Government Debt released by China National Audit Office

- Overall, the debt is from city and county-level governments, especially debt whose repayment the government is directly responsible for. This debt was mainly borrowings by financing vehicles, government departments and agencies, and subsidies and public institutions, respectively accounting for 37.44%, 28.40% and 16.32%, and is mainly financed by bank loans, Build-Transfer (BT) and bonds, respectively totaling RMB 5.53 1.22 and 1.17 trillion. Most of the debt was for infrastructure and public welfare projects, including municipal buildings, transportation facilities, affordable housing, and ESCH (i.e. Education, Science, Culture & Health). Most of the debt would mature during the second half of 2013 and 2014.

The scale of local government debt is difficult to estimate or to control. The solvency of local governments is limited, and borrowing new debt for old debt and land revenue cannot be relied upon as long-term solutions.



Government financing vehicles serving as main financing sources

Since local governments were not able to raise funds through budget deficits or bond issuances prior to the pilot project, financing vehicles served as an important medium to ease financial gaps. According to the audit findings, the debt due for repayment of financing vehicles totaled more than RMB 4 trillion. Blurred responsibilities between financing vehicles and local governments, as well as a lack of transparency of debt information, have led to a huge, inestimable grey area in terms of local government debt.



Fundraising relying mostly on loans from financial institutions

Local government debt arises primarily from loans from financial institutions: the proportion of debt coming from bonds and other direct financing instruments is quite small.

Difficulties arise in controlling risks due to complex structures. When banks strengthen credit control, local governments turn to other fundraising channels, including bank wealth management, trust products, securities, insurances, finance lease, BT, and mortgages, resulting in a complex structure of local debt and increased difficulty in controlling risks.



Borrowing new debt for old debt and relying on land revenue to ease debt pressure

Local governments tend to invest in low income projects, and debt is incurred primarily for infrastructure construction, which means little cash flow will be generated in spite of large-scale investment. The low return cannot meet the interest requirements.

Borrowing new debt for old debt: Delay overdue risks using debt cycle, but repayment risks still exist and banks face increasing pressure.

Revenue generated through land (such as by leasing land use rights) is not a lasting solution since it cannot match the pace of the increase in local government debt, and land acquisition and resettlement lead to social risk. When the real estate market fluctuates wildly, any significant reduction in revenue from land will make it difficult for local government to meet their repayment obligations.

Hot topic: Government debt

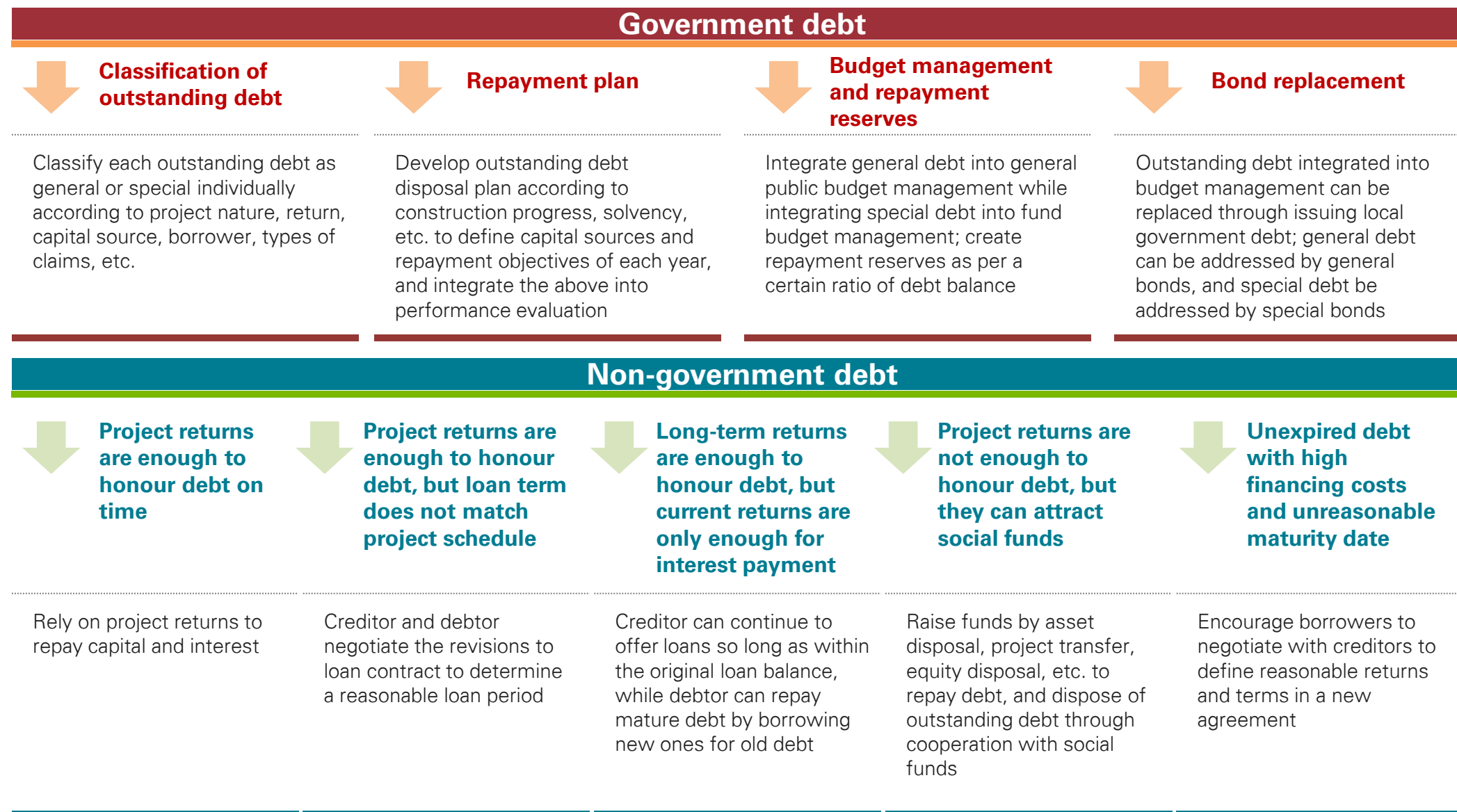
On 2 October 2014, the State Council issued the Opinions on Strengthening the Administration of Local Government Debt (the “Opinions”) to provide general guidelines for local government financing and risk control. The Opinions permits legal, moderate fund-raising while prohibiting illegal financing activities. Subsequently, the Ministry of Finance released the implementing rules, i.e. the Local Government Debt Clearance Regulations (Draft) (the “Regulations”), and the Measures for Screening Outstanding debt of Local Governments and Including Them in Budget Management. The Regulations provide screening criteria for outstanding debt, modes for disposal of government and non-government debt, treatment of follow-up financing and financing vehicles, completion dates, etc., which will have a profound impact on local debt risk.

1. Division of outstanding debt

Classification criteria	The 2013 audit divides local government debt into three categories: government debt of which the government was directly responsible for repayment, that for which the government bears a guarantee liability, and that for which the government bears some responsibilities for potential rescue.
Deadline	Specify the scope of outstanding debt, i.e. the local government debt that has not been cleared as of 31 December 2014.
Classification criteria and basis	For the debt as at 30 June 2013 identified during the 2013 audit, the balance as at 31 December 2014 will be determined according to the audit results and the changes calculated by local government debt management system (the “debt system”). For the debt occurred after 30 June 2013, the balance as at 31 December 2014 will be determined according to the amount calculated by the debt system.
Debt screening	The outstanding debt with repayment liability shall be classified as general or special, based on project nature, return, capital source, borrower, type of claims, etc. Contingent debt (including the outstanding debt with guarantee liability or rescue responsibility) will be classified by local finance departments into valid or invalid guarantees in accordance with relevant laws and regulations. Legally guaranteed debt shall be monitored as contingent debt, and that with overdue or invalid guarantees shall be cleared in time.

Outstanding debt screening involves multiple parties, including local governments, financing vehicles, banks and other bond investors. The debt with repayment liability is easily screened and identified while contingent debt is more difficult to differentiate.

2. Disposal of outstanding debt



Hot topic: Government debt

In May 2014, the State Council approved the Opinions on the Important Tasks of Deepening Economic System Reform, which specifies that local government debt shall be integrated into limit management and strips the financing function of financing vehicles. Facing increasing economic pressure, the Ministry of Finance issued on May 21 the Measures for the 2014 Pilot Project for the Autonomous Issuance and Repayment of Local Government Bonds (the “Measures”) to provide important measures to help address the financing difficulties of local governments.

The Measures

Outline	Autonomous issuance and repayment is a system in which the pilot districts issue bonds, and repay principal and interest, with the total issuance amount not exceeding the limit approved by the State Council
Positive impact	<ul style="list-style-type: none"> • Define payer and control hidden risks: transform from national credit to local credit and introduce rating agencies to prevent risks • Reduce financing costs: autonomously issue and repay local government bonds by local government • Reduce approval procedures and enhance issuance efficiency: flexibly issue, repay and utilize bonds so long as within the approved scale
Limitations	<ul style="list-style-type: none"> • Control total amount: manage annual circulation to ensure that total amount of bonds issued does not exceed the approved limit • Disallow carrying forward: the scale limit is effective only in 2014 and cannot be carried forward to the next year

Extended terms

Debt issuance terms are extended from three years to five years, five years to seven years, and seven years to 10 years ,with the proportion maintained at 4:3:3, respectively

10 pilot provinces and cities

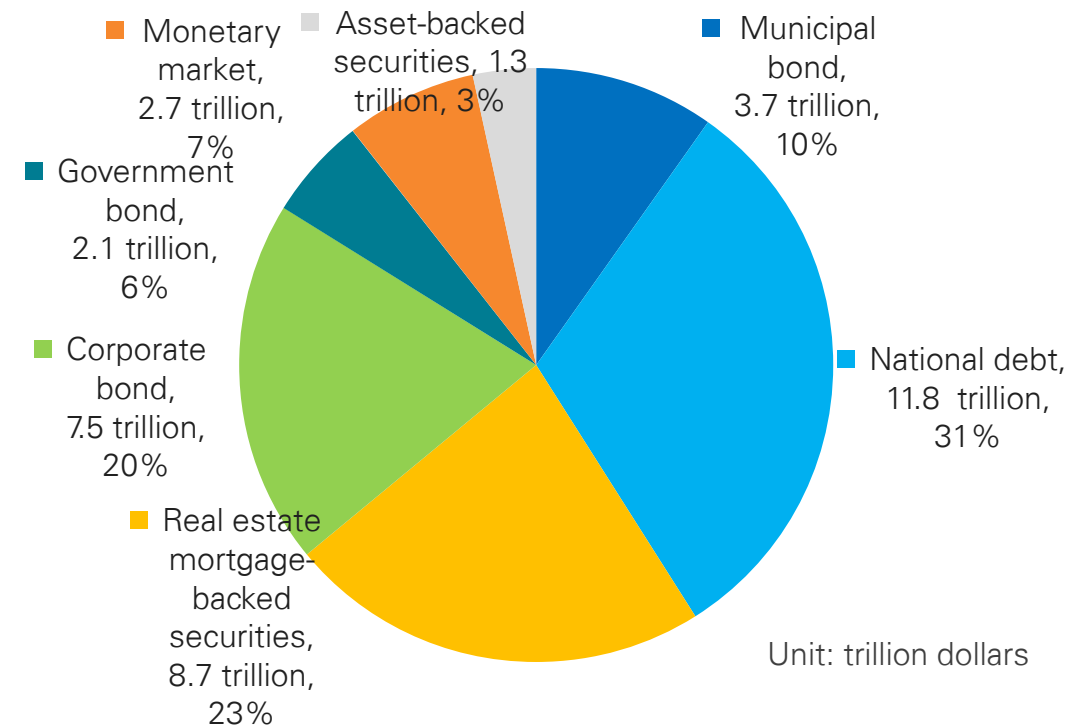
Shanghai, Zhejiang, Guangdong, Shenzhen, Jiangsu, Shandong, Beijing, Jiangxi, Ningxia, Qingdao

Overview

Asset securitization is a structured financial instrument through which an issuer takes an asset or group of assets (underlying assets) with poor liquidity and predictable cash flow, and sells it to special purpose entities in order to issue securities (asset-backed securities) based on the cash flow generated by the underlying assets and obtain financing as well as maximize the asset's liquidity.

According to statistics from the Securities Industry and Financial Markets Association (SIFMA), the asset-backed securities (including real estate mortgage-backed securities) reached 10 trillion dollars, accounting for 26% of the US bond market, second only to US bonds, and exceeding the market size of the corporate bonds in 2013.

US bond market



Source: The Securities Industry and Financial Markets Association (SIFMA)
<http://www.sifma.org/research/statistics.aspx>

The development of asset securitization in China

Early stage

Asset securitization was tested for the first time in China in 1992.

In 2000, China Construction Bank (CCB) and the Industrial and Commercial Bank of China (ICBC) served as pilot institutions permitted by the People's Bank of China to issue mortgage-backed securities, which marked the formal start of asset securitization.

In January 2002, the domestic banks issued a series of offshore securitized products for the first time.

In February 2004, *Some Opinions of the State Council on Promoting the Reform, Opening and Steady Growth of Capital Markets* was issued, which proposed diversifying securities products.

On 15 December 2004, the People's Bank of China released *The Rules of Verification of Bond Trading and Negotiation in Countryside Interbank Bond*, which paved the way for securities products.

Gradual recognition

In 2005, *the Administration of Pilot Projects for Securitization of Credit Assets Procedures* was issued by the People's bank of China and the China Banking Regulatory Commission (CBRC). The CBRC also issued *Measures for the Supervision and Administration of the Pilot Securitization of Credit Assets of Financial Institutions* in 2005.

On 15 December 2005, China Development Bank issued the first security product and CCB issued the first RMB product.

Stagnation

In 2007, the State Council approved and agreed the expansion of the securitization pilot of credit assets. In 2008, as the financial crisis broke out, the development of credit asset securitization entered stagnation.

Re-opening

In 2012, People's Bank of China, the CBRC and Ministry of Finance jointly issued *Notice on Matters Concerning Further Expansion of Credit Assets Securitization Pilot*, restarting the credit assets securitization, with an amount of RMB 50 billion.

At present, China Development bank, Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, CCB, Bank of Communications, and other joint-stock commercial banks all have the qualifications for asset securities.

Accelerating

In November 2014, the CBRC issued *Notice on the credit asset securitization registration work*, which transformed credit asset securitization from an approval system to a filing system. This provides further support for the economy and accelerate the credit asset securitization.

In line with the principle of decentralization, the CBRC will no longer require approval for securities products case by case. Financial institutions in banking sector should apply for business qualifications and register in the filing system before they issue securities products.

The issuance of asset securities in 2014

The development of asset securitization has been accelerating since 2014. The table shows parts of the asset securities recently issued.

Issuer	Name of the trust	Types of asset-backed securities	The amount issued (100 million)	Self-sustaining proportion
China Development Bank	Kai Yuan 2014-5 Credit Asset-backed Securitization Trust	Credit asset	99.76	5% of all tranches
Industrial Bank	Xing Yuan 2014-2 Credit Asset-backed Securitization Trust	Credit asset	34.94	5% of all tranches
Shanghai Pudong Development Bank	SPD 2014-3 Credit Asset-backed Securitization Trust	Credit asset	47.90	5% of all tranches
Bank of Qingdao	Qing Yin 2014-1 Credit Asset-backed Securitization Trust	Credit asset	28.33	5% of all tranches
ICBC	Gong Yuan 2014-1 Credit Asset-backed Securitization Trust	Credit asset	55.72	5.01% of all senior tranches, 5.03% of all subordinated tranches
GMAC	Tong Yuan 2014-1 Personal Automobile Mortgage Securitization Trust	Personal automobile mortgage loans	30.00	The subordinated tranches are not less than 5% of the issuance size
GAC-SOFINCO Automobile Finance Co., Ltd	GAC-SOFINCO 2014-1 Personal Automobile Mortgage Securitization Trust	Personal automobile mortgage loans	8.00	All subordinated tranches, accounting for 5% of the issuance size
Bank of Communications Financial Leasing CO., Ltd	Jiao Rong 2014-1 Leasing Asset-backed Securitization Trust	Leasing projects	10.12	All subordinated tranches, accounting for 11.59% of the issuance size

Source: China bond information network, all issuance paper for asset securitization

The focus areas of specific terms in asset securitization



To ensure the issuance of the asset-backed securities, an issuer generally designs certain trading terms to ensure the interests of issuer, security holders, managers and other parties, which may have impact on accounting treatment. Therefore, focus should be put on whether the related trading terms have impact on the merger of special purpose entities, the pass through test on transfer of financial assets, and the degree to what the risk and reward can be transferred, etc..Following are some focus areas of specific terms in asset securitization :

Recurring purchase

- Recurring purchase refers to the trading arrangement in which the issuer or special purpose entities purchase a new and similar underlying asset based on the cash flow generated by the underlying assets.
- Such structural arrangement solve the mismatch problem that the underlying assets such as petty loans and credit loans have relatively short-term cash flow while the asset-backed securities have a relatively long-term cash flow. If the loan in the loan portfolio is paid before its maturity, the payment can be used to purchase a new loan until its maturity.
- There is uncertainty in the trading structure of a recurring purchase. That is, the quality of the purchased asset may be different from the quality of the mature loans. It requires designing strict trading mechanism to prevent purchasing loans of low quality and deteriorating the credit standards in the asset pool.

The focus areas of specific terms in asset securitization



Liquidity support

- Liquidity support refers to when difficulty occurs in the payment for the expected income of the current senior beneficiary certificates and banks provide short-term liquid loans to issuers according to an agreement. The banks directly transfer the loans to the account of special purpose entities in order to make payment in full for the current senior beneficiary certificates.

The focus areas of specific terms in asset securitization



Prepayment risk

- Prepayment risk refers to the risk that a borrower will repay a loan before its maturity, depriving the lender of future interest payments. Thus, the interest payments generated from the underlying assets are less than the interest estimated at the establishment of the asset-backed securities, which will impact on the income of the asset holders if there is no other arrangements.
- Prepayment risk also contains the risk that the asset holders cannot receive the payments in time. The payments may be retained in the account of the issuer after being prepaid, as long as there is no restriction to distribute it in time.
- Prepayment risk depends on the changes in market interest rates and the conditions in the loan agreement. Declining interest rates and fierce competition could encourage prepayment. If loan contract has a condition (such as prepayment penalty) to limit the prepayment, the borrowers are subject to this penalty.

The focus areas of specific terms in asset securitization



Excess spread

- Excess spread means that the asset pool provides a higher spread as support for the principal and interest payment of the senior beneficiary certificate. For example, suppose that a special purpose entity has a total amount of principle and interest receivable of RMB 500 million, and the total amount of principle and interest is estimated to be about 400 million, the principal and interest covers a multiple of 1.25, which enables the asset pool to provide spreads support for the payment of principle and interest.

History of development

Community banks have played a decisive role in the financial system of the US. According to the statistics of 6,900 banks from the website of Federal Deposit Insurance Corporation (FDIC), as at 30 September 2013, the number of banks with an asset scale below USD 10 billion in the US was 6,791, over 98 percent of the total number of the American banks. The total asset scale of these banks amounted to USD 2.85 trillion, 19.43 percent of the total asset scale of the American banks, with the average asset scale of only USD 420 million. However, these community banks, whose total asset scale made up less than 20 percent of the total asset scale of the American banks, offered over 60% of the small loans made to companies and farms in the US. Community banks have evolved with changing trends of the financial and regulatory policies in the US, an evolution which can be summarized in three stages. By looking into the development of the community banks in the US, we might get valuable perspectives for the development of community banks in China.



Three stages of development

Before 1980

- Under the protective wing of regulatory policies, community banks were allowed to provide traditional financial services, such as bank deposits and loans and account settlement, in specific business areas, thereby gradually dominating the market in certain areas. This was also the period when the American community banks enjoyed the fastest growth.

1980 - 1990

- There were shifts in the financial and regulatory policies in the US. Financial innovation pushed forward deregulation. Under the interest rate liberalization in 1986, community banks faced enormous pressure from the fall of interest rate differential. Moreover, technological innovation facilitated the business expansion of the major banks. Through managing the basic information database based on customer relationships, the major banks could analyse a customer profile at different market levels, and were able to provide loans to small and medium enterprises (SMEs) at lower costs, thereby directly challenging the community banks' market position. The number of community banks in this period fell by more than 2,000 from that at the end of 1980.

1990 to date

- Community banks faced with fierce competition from cross-state banks after the limitations on operating areas of commercial banks were removed. The Gramm-Leach-Bliley Act enabled the major banks to engage in securities underwriting and insurance services and to develop a more comprehensive business platform, which increased SMEs and household customers' dependency upon major banks and further weakened the competitive edge of the community banks. The number of community banks continued to drop from more than 11,000 in the early 1990s to about 6,700 at the end of 2013. Those that survived the regulatory shifts and the ups and downs of the financial environment played an important role in the economic and financial development of the US.

Advantages

Serving SMEs And community members

- Different from the major banks who mainly served mid-to-high end corporate clients, community banks focus on serving SMEs and community members.
- The differentiation of the customer orientation gave the community banks a competitive edge. By focusing on serving SMEs and community members neglected by the major banks, community banks can centralize resources on enhancing their core competitiveness instead of competing with the major banks directly.

Less credit risk and highly sensitive to risks

- As their asset scales were smaller, community banks were highly sensitive to risks, and thus dedicated to improving their risk management process.
- Community banks accepted deposits from SMEs and community members and provided financial services to SMEs and community members. As the bank staff were often in direct contact with the customers, they were quite familiar with the credit position and operating condition of the community members and SMEs, thus lowering the risks of loans to these customers.

Resistant to economic fluctuation and aligning with SMEs' needs

- During an economic crisis, the community banks' ability in adding deposits, developing new customers and maintaining financial soundness is elevated relative to that of the major banks.
- Community banks' operating characteristics are different from those of the major banks, and so are their efficiency characteristics. When the economy was sound, the major banks had the operating efficiency that the community banks could not achieve because of the economies of scale; only when the economy suffered from negative impacts could the differentiated operation of the community banks really show efficiency advantages.
- SMEs' business will fluctuate even in a stable economic environment. Community banks can better suit the financing demands of SMEs because of their operating characteristics; therefore, they tend to maintain a more stable operating efficiency.

Challenges

Since 1980, the business environment for the banking industry has experienced great changes, and challenges to the community banks have emerged, which can be summarized in the following aspects:

Deregulation

- Deregulation led to interest rate liberalization, and the community banks had to face enormous pressure from the fall of interest rate differential.
- The limitations on operating areas of commercial banks were removed. The geographic expansion intensified the competition among banks and posed a great challenge to community banks and their small asset scale.

Advancement of technology

- Conventionally, the community banks provided relational loans to SMEs based on soft information such as the borrowers' integrity and capabilities while the major banks gave out transactional loans to large companies based on hard information such as standardized financial information.
- The advancement of information technology reduced the significance of relational finance and the need for face-to-face communication when conducting business. The low-cost information processing approach and the enhanced credit rating model improved the transparency of the financial position of SMEs and community members.

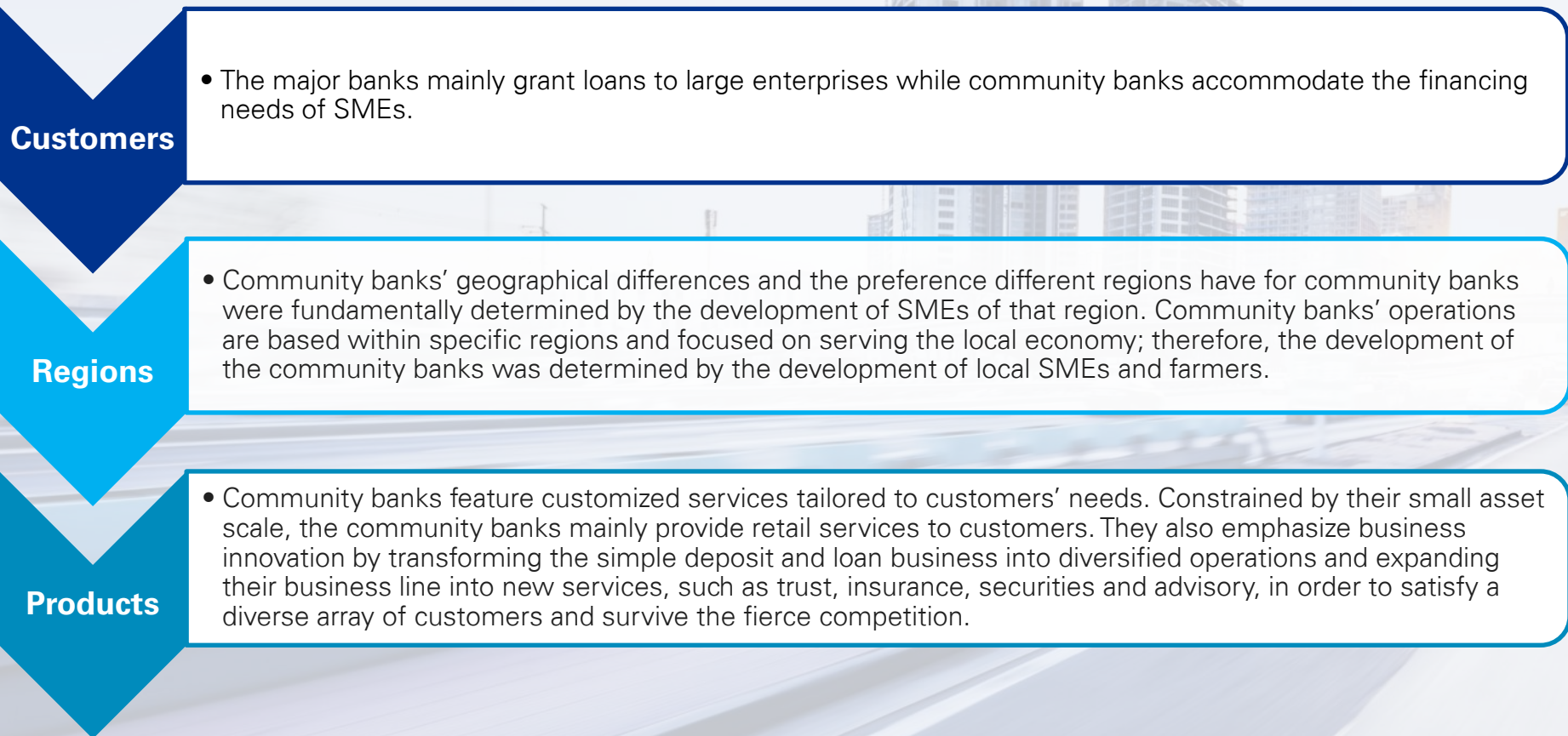
Financial innovation

- Financial innovation enabled non-bank financial institutions to issue consumer finance loans. Mutual funds, online brokerage accounts and money market funds emerged to offer more attractive investment opportunities to depositors. while the popularisation of credit cards and debit cards also weakened the attraction of checking accounts. All in all, financial innovation has affected the financing source of the community banks.

Hot topics: Community banking in the US

Community banks in the US adopted a differentiated development strategy. The differences in targeted customers, operating regions and the provision of products, from those of the major banks avoided strong obstruction from the major banks when entering the market and helped develop their own business characteristics and advantages.

Development strategy



Successful case — Wells Fargo

- Founded in 1852, Wells Fargo originally engaged in postal services and banking services in California, and later expanded its operations across America. In 1998, Wells Fargo merged with Norwest Corporation, which was known for its retail business and cross-selling strategy, a business philosophy similar to that of Wells Fargo's. Through a series of splits and combinations in 2001, Wells Fargo allocated the mortgage operation to the business lines of community banking and wholesale banking, thereby forming three main business segments that are still in effect: community banking, wholesale banking and wealth management. Community banking specializes in providing financial products and services to personal clients, and small businesses with annual sales under USD 10 million.
- In order to cope with the market-oriented reform, since the 1980s, Wells Fargo has chosen a development path different from those of other major commercial bank. JPMorgan Chase and Citigroup have focused on investment banking and the expansion of investment and brokerage services while Wells Fargo has stuck to the traditional commercial banking services and focused on community banking business. Community banking has been the main source of revenue for Wells Fargo. Since 2000, the revenue from community banking has remained above 50 percent of the total revenue of Wells Fargo, even reaching 70 percent in certain years. Even when personal customers and SMEs had to face deleveraging and operating difficulties after the financial crisis in 2008, community banking was still its main source of revenue. Benefitting from its community-oriented business model, Wells Fargo was the only major bank that overcame the subprime crisis and grew stronger. Wells Fargo is the largest bank in the world in terms of market value, and has the most community bank branches and staff members in America while maintaining a relatively low operating expense; the community banking segment has sustained over 70 percent of long-term deposits for Wells Fargo and contributed over 50 percent of revenue for a long time.



What we learn from Wells Fargo

1

Emphasizing channel building and customer engagement

As at the end of 2012, the total assets of Wells Fargo were about USD 1.4 trillion while those of Bank of America reached USD 2.1 trillion. However, Wells Fargo had 9,097 branches and Bank of America only had 5,500, about 60 percent of the branches of Wells Fargo. While emphasizing the building of branches, Wells Fargo made great investment in personnel. Its total staff amounted to 269,200, exceeding the staff of Bank of America of 262,800.

Through the spreading of branches, Wells Fargo can directly deliver its financial services to the community and instantly acquired customer information and service demand by face-to-face communication. Wells Fargo provides financial services to one third of all American families. The community branches of Wells Fargo processed 5.5 billion times of customer enquiries and sales every year, which were 10,000 times of financial services per minute provided to the customers.

2

Product diversification and cross-selling strategy

Wells Fargo's financial services include saving services, financing services and wealth management services. Through its cross-selling strategy, Wells Fargo offers diversified and all-around financial services to community members and SMEs.

Wells Fargo has also established financial service channels combining physical sites, internet and mobile terminals through self-service banks, online banking and telephone banking.

At present, Wells Fargo has the most extensive service network in America, which enables it to attract more retail customers. The versatile product system has improved Wells Fargo's cross-selling ability, which can be seen from the fact that the number of products sold to the retail customers rose from 3.8 in 2001 to 6.3 at the end of 2011.

3

Accurate positioning and focusing in small and micro loan business

Focusing in small and micro loan business was the key to success for Wells Fargo's community banking. From 2001 to 2012, the scale of its small and micro loan business topped those of other American banks.

Wells Fargo has subdivided its small- and micro-enterprise customers as follows: services for small enterprises with annual sales from USD 2 million to USD 20 million and with a staff of 20 to 99 people were provided by a specially-appointed customer manager; small and micro enterprises with annual sales below USD 2 million and with a staff of less than 20 people were provided by the local community banks.

In addition, Wells Fargo specially developed a credit rating card system for small and micro businesses based on its powerful information system, which automated the approval of two-thirds of small- and micro-enterprise applications based on their credit rating, greatly reduced the service costs for the small and micro businesses.

What we learn from Wells Fargo (Cont'd)

4

Dedicated to product & service innovation

The emphasis on product and service innovation enabled Wells Fargo to maintain its competitive edge. Wells Fargo provides a special service called Business Direct to the small and micro enterprises of small scale, which had lower profits and were less standardized. Through Business Direct, the targeted customers can submit their loan applications via email and telephone and they are automatically approved through the advanced credit rating system. This streamlined process greatly simplifies small and micro enterprises' applications for loans and enables more convenient access to financing services.

At the end of 2012, Wells Fargo's loan balance for the small and micro enterprises had achieved a more than 30 percent increase compared to that in 2011. Newly granted small and micro enterprise loans reached USD 16 billion, with a loan balance of over USD 57 billion. Loans under USD 1 million made up over 90 percent of total loans granted, a percentage much greater than that of its American peers.

5

Precision modelling

One of the shortcomings of community banking is that the lack of business models often leads to deviation from the original development strategy and low operating efficiency. Through restructuring, Wells Fargo came up with the density model, cross-selling model, efficiency model and investment model for community banking, keeping the staff and operations in line with the original development strategy while scientifically managing the costs for its scale of development.

What we learn from Wells Fargo (Cont'd)

Precision model

To apply a standardized and quantitative model to continuously align the company's development with its original strategy is still a frontier to be explored. Wells Fargo's community banking business achieved rapid development thanks to the application of precision models and the economies of scale. Wells Fargo's precision models are designed as below:

- ▶ **Density model:** To set up branches at an appropriate density in different markets (cities) and to encourage local residents to open accounts. Based on research and data analysis, they look for the greatest gradient on the curve of population coverage of a branch and the corresponding curve of market share, and develop more customers at the same time to dilute the fixed cost. According to Wells Fargo's calculation, the increase of every 500 household customers will improve the ROA level of each branch by 10 to 20 bp, which indicates that both the quantity and quality of the community bank branches are the keys in the density model. Under this quantitative model, the community branches can conduct more targeted operations and prevent the upsurge of costs resulted from unchecked expansion.
- ▶ **Cross-selling model:** To satisfy customers' needs through multiple sales channels and encourage customers to open deposit accounts. Simply put, if more of the customers' financing needs can be satisfied, the cross-selling volume per customer will increase, resulting in the increase of profits from family customer unit. In order to achieve this goal, multiple sales channels should be fully mobilized. According to the statistics of Wells Fargo, most of the customers are using self-service systems (including online banking, ATM and telephone banking) to complete transactions, though the percentage of processing transactions in bank branches is also on the rise. Statistics show that over 77 percent of customers have dealt with a community bank teller at least once in the past half year. The other reason why Wells Fargo is so into building branches is that customers accessing more sales channels tend to buy more products.

In addition, the deposit products are also the main attraction

for customers. 64 percent of all newly-developed customers in 2011 became Wells Fargo's customers by purchasing deposit products, while 26 percent by purchasing home mortgage products. Of all existing customers, 63 percent have bought its insurance products and 35 percent have applied for personal mortgages. Deposit customers can bring along more product sales and the service of the bank and the customer experience will have a great influence on the choice of banks of community members.

- ▶ **Efficiency model:** This model can be used to improve the operating efficiency of each branch. Wells Fargo has experienced a few major mergers and acquisitions in the course of its development, including the acquisition of First Interstate Bancorp. in 1996, a merger with Norwest Corp. in 1998 and acquisition of Wachovia Corporation in 2008. As banks in America are generally highly efficient, Wells Fargo did not experience an upsurge in capital expenditure during these mergers and acquisitions. In fact, the site area and costs of the community banks have been falling and will probably continue to fall in the future. The measures to improve efficiency include controlling the staff numbers while ensuring satisfaction of customers and cutting down the operating areas while remain in compliance with the density model. The result of these measures is a community branch becoming more compact, with an appropriate layout and nice atmosphere. Multiple sales channels such as online banking, ATM and telephone banking also play a big role in achieving this result.
- ▶ **Investment model:** To study how branch building can be optimized to enhance customer experience and to increase cross-selling and customer number of each branch.

Introduction

Academic column invites economics scholars to give their views, comments and analyses on the current hot topics and latest development of the banking sector.

Internet finance development, e-money as an alternative and liquidity management of commercial banks

Zhou Guangyou

Against the backdrop of rapid internet finance development, e-money as an alternative to traditional currency has brought challenges to traditional financial theories. In particular, it has a huge impact on the operations and management of commercial banks whose business is to manage money. This article attempts to introduce Keynesian theory on the demand for money in the context of internet finance development to analyse the motives of liquidity demand of commercial banks for the reference of commercial banks with respect to liquidity management.

I. Introduction

The rapid development of internet finance in recent years has imposed unprecedented challenges to our economic lives. Electronic payment (including electronic money or e-money), a crucial development mode in internet finance, is not simply a non-monetary alternative to traditional currency. It not only alters our payment behaviours and lifestyle, and also subtly changes a country's economic structure (Zhou Guangyou, 2006). Meanwhile, it challenges traditional money and financial theories, having a huge impact on the operations and management of commercial banks whose business is to manage the special commodity of money.

For a long time, liquidity management has been the core of the operational management of commercial banks which usually manages liquidity in light of the operating environment, objectives and principles. In general, liquidity is traditionally managed through asset management, liability management or a combination of both, with on- and off-balance sheet items managed uniformly to minimise management cost where possible. The cost of liquidity management depends on low funding costs and convenient funding sources. If commercial banks can obtain funds easily at low costs when needed, then the cost will be low. It means that commercial banks can reduce the level of surplus reserves and allocating more funds for investment in profitable assets.

Nevertheless, the most distinctive features of e-money in the e-money era are fast, convenient and low-cost transactions. This is bound to present challenges to the liquidity management of commercial banks, and affect the structure and quantity of their liquidity demand. Unfortunately, the impact of e-money on the liquidity demand of commercial banks has yet to be fully appreciated. This will inevitably affect the effectiveness, operational efficiency and risk control of the liquidity management of commercial banks.

Existing studies on the impact of e-money mainly focus on the aspects of money multiplier, liquidity and money supply (Zhou Guangyou 2007, 2009 and 2010), paying little attention to the liquidity management of commercial banks. In fact, such impact is obvious and likely to deepen further. Hence, commercial banks should attach greater importance to the function of e-money while managing liquidity and fully utilise it to improve their liquidity management. To this end, this article attempts to introduce Keynesian theory on the demand for money from the perspective of e-money in the context of internet finance development to analyse the motives of liquidity demand of commercial banks with a view to provide valuable ideas for commercial banks with respect to liquidity management.

II. Impact of e-money on liquidity demand of commercial banks

Commercial banks can adjust their liquidity levels to ensure financial security or achieve profitability goals, thus coordinating security, liquidity and profitability dynamically. This is a core aspect of their operational management. The liquidity demand of commercial banks is managed through liability management, asset management or a combination of both, and it is commercial banks' objective to conduct transactions rapidly at low cost. The liquidity demand of commercial banks is in indeed the demand for money. Liquidity demand at different levels is materialised through the demand for money, sometimes for daily transaction needs (such as cash withdrawals by customers), sometimes for precautionary needs (such as during the financial crisis) and sometimes for speculative demand. These motivations show that the liquidity demand of commercial banks is tantamount to the public's demand for money. Therefore, this article attempts to introduce Keynesian theory on the demand for money to analyse the liquidity demand of commercial banks.

(1) Impact of e-money on commercial banks' liquidity demand for transactions

Keynes' transaction motive for the demand for money refers to people's desire to hold money for daily transactions, which can be further classified into the income motive and the business motive from the perspective of individuals and corporations (Hu Qingkang, 2001). Applying this theory to commercial banks, transactions demand for money refers to the liquidity demand of commercial banks to meet daily transaction needs. Banks have to maintain a certain amount of cash in daily operations to meet the withdrawal needs of customers and pay operating expenses. Excess cash at bank lowers banks' income and increases security risk. On the other hand, an insufficient cash level can damage banks' reputation when the withdrawal demand of customers cannot be met. Maintaining an appropriate level of cash liquidity in operations is a worthy objective for commercial banks to pursue. In this article, liquidity demand for transactions primarily refers to deposits that commercial banks place with their counterparts to meet withdrawal demand and interbank settlement requirements. In the following, we will discuss the issue from two aspects.

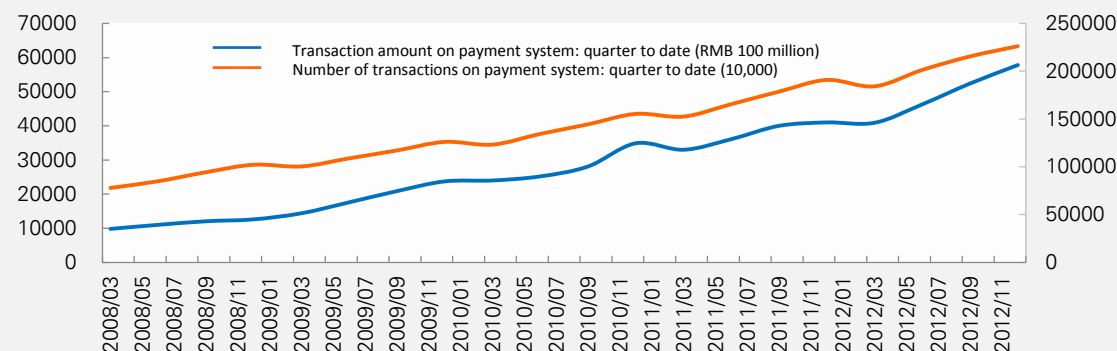
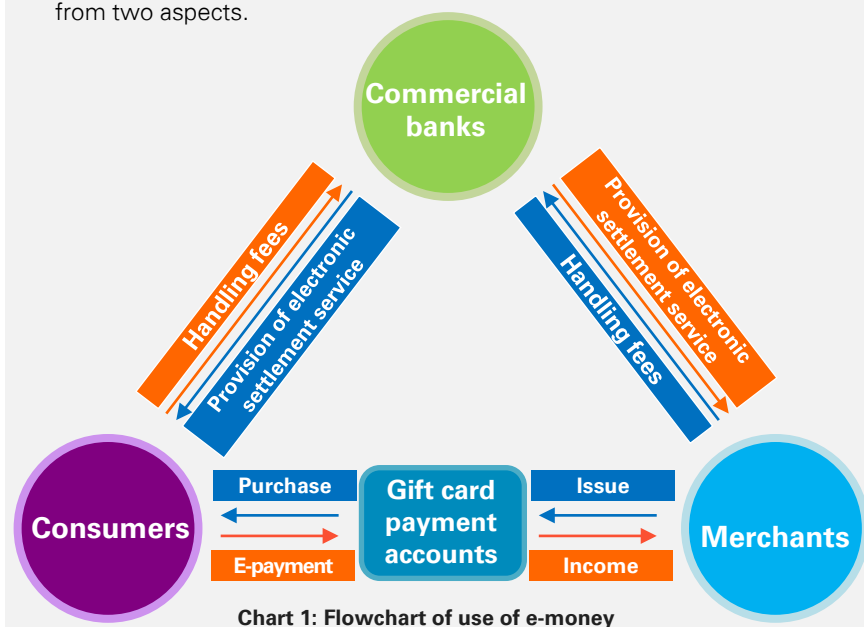


Chart 2: Cross-bank settlement of bank cards on payment system

First, we will analyse changes in the liquidity demand of commercial banks for interbank settlement. The emergence of e-money has changed people's habits. People tend to use cash in the small retail payments. However, when electronic terminal equipment (such as UnionPay POS machines in large supermarkets) or online payment accounts are available, people tend to choose e-payment methods (John Simon and Kylie Smith, 2010). It is especially so when people shop online, they tend to pay with electronic accounts or internet banking. The use of e-cards such as gift cards issued by large supermarkets and mobile top-up cards has directed significant cash flows to suppliers, which are then translated into suppliers' deposits with commercial banks. The process is illustrated in Chart 4.1. Given that e-money is safe to use and not restricted by time or place, it offers great convenience in making payment. The emergence of e-money, electronic transfer settlement and transfer systems has greatly promoted the development of e-commerce while imposing higher requirements on commercial banks' services.

Nevertheless, due to banks' limited resources or geographical restriction, procuring services from other banks or establishing agency relationships with other banks is a more cost-effective option. Interbank settlement business has been greatly boosted with the use of e-money. E-money and electronic payment methods have set higher requirements on the convenience of cross-bank transfer services. In order to retain customers and cut costs, commercial banks' liquidity demand for interbank settlement will increase. In other words, banks will place more deposits with other banks and financial institutions for the purpose of interbank settlement. Commercial banks charge a percentage of fees when providing transfer or clearing services to customers. With the growing use of e-money, such fees will become a major source of income for banks. Under the trend of homogenised banking service channels, increasing efficiency and growing size of intermediary services such as transfer settlement and clearing services will generate considerable income to commercial banks. Chart 2 illustrates the status of cross-bank card payment in China.

Second, another drive for liquidity demand of commercial banks is to meet customers' withdrawal demand. Amid advances in bank transfer and clearing system technology, the efficiency of bank transfer and clearing services continues to improve, satisfying the needs of e-money circulation in this respect. Residents' demand for cash will gradually decline (as shown in Chart 3), and e-money will gradually replace cash in circulation.

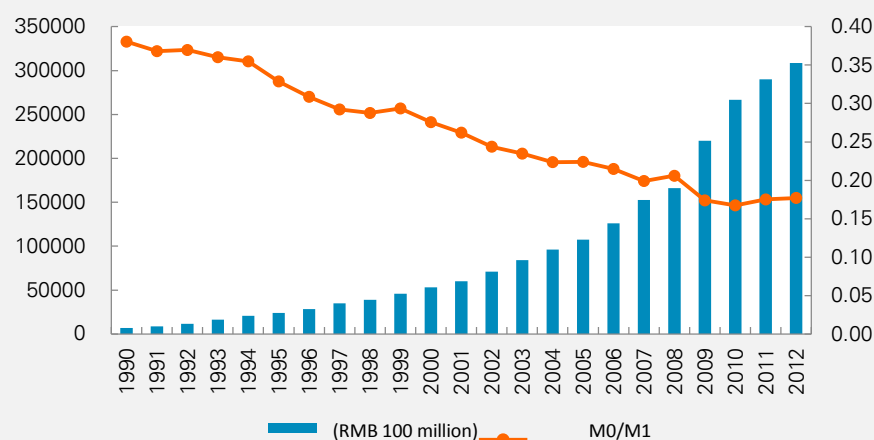


Chart 3 Trends of M1 and M0/M1 in previous years

As shown in Chart 3, cash takes an increasingly small proportion in M1. Therefore, it can be said that thanks to the impact of e-money, customers will have a decreased demand for cash. As China currently has not set the deposit reserve requirement for e-money, consumers' spending with the use of e-money will ultimately lead to increased deposits of enterprises and businesses in commercial banks, which will in turn diversify sources for those banks to gather deposits for lending or investment to increase banks' profitability. Because of e-money, as commercial banks' transactions demand to meet customers' need for cash withdrawal decreased, their deposits for lending or investment increased. This change can be summarised in the following Table (Table 1):

Table 1 Changes in excess deposit reserves of commercial banks

Deposit-taking (D) (RMB 100)		Traditional economy	Circulation of e-money
Category	Use	Amount	Amount
Statutory deposit reserves (R)	Required by the central bank	20	20
Excess reserves (ER)	Customers' cash withdrawal, settlement, financial institution transfer and use of funds	10	8
General reserves (GR)	Lending or investment	70	72

Commercial banks accept three kinds of deposits: statutory deposit reserves, excess reserves and general reserves. Their transactions demand for liquidity mainly involves excess reserves. Here, commercial banks' excess reserves are defined as the sum of those banks' reserves in the central bank that exceed the statutory amount and their vault cash. As excess reserves are commercial banks' most liquid assets, they are the most important liquidity reserves for those banks. If a commercial bank takes RMB 100 as deposits, and the statutory reserve ratio is 20%, the bank has to give RMB 20 to the central bank as statutory deposit reserves and retains RMB 10 as excess reserves while the rest of it (RMB 70) will be saved in the central bank as general reserves. If a consumer withdraws RMB 2, then cash loss is RMB 2 and excess reserves and general reserves will also be reduced by RMB 2. Commercial banks' funds for lending may come from general reserves and excess reserves, as shown in the above table. But when people use e-money for payment, though the total amount of deposits within the whole commercial banking system ultimately will not change, the deposit structure will be more stable, which would mean a decreased demand for commercial banks to set excess reserves and more deposits for them to use on lending or investment to increase their asset profitability.

It can be seen from the above theoretical discussion that under the influence of e-money, commercial banks can, on the one hand, retain less amount of excess reserves for daily transactions, while on the other hand, enjoying a stable inflow of large amounts of deposits from enterprises and businesses. Since presently, commercial banks are not required to pay deposit reserves for e-money, they enjoy a decreased transactions demand for liquidity to meet customers' need for cash withdrawal and increased deposits to be used for lending or investment to improve their profitability. Apart from this benefit, as people are using e-money for payment more frequently and on a larger scale, in order to maintain customer loyalty, commercial banks are forced to make their account transfer, settlement and other clearing services more efficient while at the same time, ensuring adequate liquidity. Besides, they can charge a certain amount of service fees based on the transaction volume for e-transfer and settlement services that they provide, which brings them profits which in turn can compensate for part of their transactions demand for liquidity. Therefore, under the influence of e-money, a decrease in commercial banks' excess reserves to meet customers' need for cash withdrawal and an increase in funds saved in other banks are exerting a great impact on commercial banks' transactions demand for liquidity. As to which one of these two changes will generate more impact than the other, a reliable conclusion will have to come from more empirical research and analysis. Meanwhile, it is also worth noticing that the size of commercial banks' excess reserves and interest rates are closely related with their lending cost: When interest rates are high, opportunity cost for holding excess reserves will increase, while when lending cost increased, commercial banks are more inclined to hold more excess reserves. Finally, the size of transactions demand for liquidity is intertwined with a commercial bank's total assets or the size of deposits accepted: More accepted deposits means larger transactions demand to meet the need of daily cash withdrawal.

(2) Impact of e-money on commercial banks' precautionary demand for liquidity

The precautionary motive, also known as discretionary motive, in Keynes's theory on "liquidity preference" refers to micro-bodies' wish to hold money for emergency situations. For individuals, those situations

may be sickness, unemployment and other events that will result in unexpected demand for money. The author, however, mainly sees the precautionary motive as central banks' mandatory requirement for commercial banks to draw statutory reserves for accepted deposits and loan reserves for lending to prevent the occurrence of extreme liquidity events. Among the two kinds of reserves, the former is the main part while the latter is so set only out of those banks' discretion.

Central banks require commercial banks to pay deposit reserves so that those banks can have enough money to meet depositors' need for withdrawal and to avoid liquidity crisis resulted from inadequate liquidity. In other words, compared with transactions demand for liquidity, commercial banks' liquidity demand for precautionary motive is less likely to be used in practice, for this part of liquidity is not to be used in their daily operation and will only be used when extreme events occur.

Nevertheless, adequate amounts of statutory reserves must be maintained. In commercial banks' actual operations, due to low predictability of changes in deposits and of remittance and other businesses, short-term inadequacy or surplus may occur in reserve accounts in central banks at the end of a day's operation. In order to meet the requirement for reserves, commercial banks may adjust short-term inadequacy through the interbank lending market: banks with a surplus of funds (lender) will lend funds to banks with inadequate funds (borrower) to make up for such inadequacy from daily operation. As deposit reserves paid by commercial banks are determined by the size and structure of all the deposits accepted by them, this precautionary liquidity demand has a close relationship with the total amount of deposits accepted. In addition, commercial banks are also required to make a certain amount of loan loss provisions for lending. In China, the central bank issued the requirement for loan loss provisions for policy banks, state-owned banks, shareholding banks and other banks in April 2002. According to the requirement, all banks should follow the requirement of the Guidelines to provide for losses of different loans in a timely manner. The loan loss provisions made by commercial banks include general, specific and special provisions. For specific provisions, the Guidelines on Loans Classification should be followed to rationally categorise each loan into one of the five

categories as laid out by the Guidelines and loan loss provisions are to be made based on such categorisation. The requirement for loan loss provisions reflects prudence in commercial banks' operations. As a preventative measure, it not only provides a cushion for commercial banks to respond to risky events, but also boosts public confidence, strengthening the ability to obtain more deposits or more stable deposits, which to some extent can be seen as one of commercial banks' long-term precautionary demands for liquidity.



First, in the analysis of commercial banks' transactions demand for liquidity, it has been made clear that as people use e-money more frequently and on a larger scale, the e-money that they use will flow to enterprises or businesses, which ultimately will transfer most of it into their bank accounts as deposits, leaving only a small amount for liquidity. As a result, commercial banks receive more stable "e-deposits". As China has not yet required reserves to be made on e-money, after commercial banks accept those deposits, their reserves for precautionary motive decrease. In addition, an improved efficiency in financing in the financial market and a decrease in financing cost empower commercial banks' ability to rapidly obtain funds from the market even when short-term fund shortage occurs. This will also result in a decreased demand for liquidity as required by precautionary motive. Second, the emergence of e-money initially leads to decreased loss of cash in circulation. And then, with people's changing habit of payment, commercial banks are beginning to obtain more and more stable deposits than traditional payment would bring to be used for their lending or investment. With regard to the precautionary liquidity demand that requires commercial banks to make general and specific loan loss provisions according to the categorisation, if commercial banks, as permitted by their financial strength, choose to use more deposits on lending, their corresponding demand for loan loss reserves increases; if commercial banks choose to use the fund on investment, such as purchasing trading financial assets and derivative financial assets, and making equity investment, liquidity demand as required by precautionary motive will decrease.

(3) Impact of e-money on commercial banks' speculative demand for liquidity

The speculative motive is the third motive in Keynes's monetary demand theory. He assumed that wealth is held in the form of money and securities. In his opinion, the speculative motive arises from people's need to adjust the structure of wealth as a result of uncertainty of interest rates in the future or in order to avoid losses of wealth that might result from fluctuations in the market. When interest rates are high, they are expected to fall. People will hold less money and more securities in order to avoid losses in the value of deposits. Thus the speculative demand for money declines. When interest rates fall as expected, there will be capital gains for those holding securities whose prices have risen. On the contrary, when market interest rates are low, people who expect interest rates to increase will hold more money and less securities in order to avoid the losses that might result from falling prices of securities due to the increase in interest rates. Thus the speculative demand for money rises. It can be seen that according to Keynes's monetary demand theory, the speculative motive for monetary demand and market interest rates are closely related and negatively correlated. To introduce this factor of speculative demand for money into the analysis of commercial banks' demand for liquidity, it refers to the negative

correlation between commercial banks' speculative demand for money and market interest margins.

Commercial banks' speculative demand for liquidity refers to the negative correlation between capital gains and such demand for liquidity as cash on hand. If commercial banks' assets are held in the form of cash and loans, their demand for cash or excess reserves can be considered as speculative demand for liquidity while loans and other investments are thought to be another form of holding wealth. When interest rate margins are high, commercial banks will reduce the holding of cash and excess reserves and lend and invest more money in order to increase the value of their wealth and avoid losses.



When interest rate margins become low, commercial banks will hold more cash and excess reserves and lend and invest less money in order to avoid losses that might result from lower interest margins. Thus lower interest margins will increase commercial banks' speculative demand for liquidity. Under the influence of e-money, consumers move from cash payment to electronic payment when making purchases. With electronic currency becoming popular, more and more cash will flow to commercial banks in the form of deposits which are more stable. On the one hand, commercial banks' speculative demand for liquidity will become less as the demand for reserves decreases; on the other hand, as electronic currency circulates rapidly, it reduces the financing costs for commercial banks significantly while improving financing efficiency. It allows commercial banks to lend money sufficiently even when the interest margins are low and to liquidate financial assets at low costs when liquidity becomes scarce. From this perspective, the emergence of electronic currency facilitates financing for commercial banks and enables them to have less speculative demand and use most of their assets on lending and investments. Commercial banks' Speculative demand and their size of deposits and loans are negatively correlated.

III. Conclusions and implications

- (1) The development of electronic currency has changed the form of currency and what is also changed is the way people pay for their purchases and live their life. It has obvious impact on traditional monetary theory and is also changing the economic structure of a country in a subtle way. Its impact on commercial banks whose business is managing money is the foremost. Traditional conceptions in liquidity management, the most important part for banks, will also be challenged under the impact of internet finance and electronic currency.
- (2) In the age of internet economy, the fast development of electronic currency will affect commercial banks' transaction motive for liquidity, precautionary demand for liquidity and speculative demand for liquidity. This will change not only commercial banks' total demand for liquidity but also the structure of their demand, which will further impact commercial banks' liquidity demand behaviour.





(3) There are two sides to the impact that the development of electronic currency have on commercial banks' management. On the one hand, it encourages commercial banks to innovate their business and offers them the opportunity to meet customers' diversified need. This is also one of the key reasons why commercial banks are expanding their business from balance sheet business to off-balance-sheet business. Therefore, under the conditions of electronic currency, commercial banks should make sufficient use of electronic currency which is convenient and cost-effective and reduce their costs in liquidity management and improve their operating efficiency. On the other hand, the fast development of electronic currency will also impose challenges to commercial banks in the aspect of operations and management. First, with traditional business going electronic and new business becoming innovated, commercial banks will face risks not only from their traditional banking operations but also from emerging business, which means that the risks commercial banks face will be multiplied. Second commercial banks might be reshuffled as a result of the fast development of electronic currency. Commercial banks can no longer rely on their advantages in capital and outlets because then it will be internet technology, capabilities for innovation and the quality of services that count. Small and medium-sized

banks will enjoy unprecedented opportunities. Therefore, commercial banks should take full advantage of the opportunities brought by internet finance, improve their internet technology, innovate their business while enhancing risk control in their operations and management in order to provide customers with diversified financial products and improve the quality of services.

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About the author:

Zhou Guangyou, Doctor of Economics and a postdoctoral fellow of Finance, is an associate professor and a graduate tutor from the School of Economics , Fudan University.

04



Appendix: 2014 Q3 financial data of listed banks

Net profit attributable to equity holders of the parent company

RMB million	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate
ICBC	220,464	205,533	7%
CCB	190,298	176,482	8%
BOC	131,133	120,210	9%
ABC	152,439	137,988	10%
BCM	51,522	48,706	6%
CMB	45,804	39,498	16%
CNCB	32,280	30,860	5%
CMBC	36,778	33,314	10%
SPDB	34,799	29,818	17%
CIB	38,304	33,102	16%
CEB	23,322	21,664	8%
HXB	13,177	11,130	18%
PAB	15,694	11,696	34%
BOB	12,592	11,014	14%
BON	4,160	3,419	22%
NBCB	4,584	3,944	16%
Total	1,007,350	918,378	10%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Financial performance indicator

	Return on weighted average equity		Basic earnings per share (in RMB)		Net asset value per share (in RMB)	
	2014/01/01- 2014/09/30	2013/01/01- 2013/09/30	2014/01/01- 2014/09/30	2013/01/01- 2013/09/30	30/09/2014	31/12/2013
ICBC	21.52%	23.00%	0.63	0.59	4.06	3.63
CCB	22.14%	23.38%	0.76	0.71	4.83	4.30
BOC	18.03%	18.66%	0.47	0.43	3.60	3.31
ABC	22.34%	23.09%	0.47	0.42	2.95	2.60
BCM	15.58%	16.30%	0.69	0.66	6.14	5.65
CMB	21.33%	24.59%	1.82	1.83	11.97	10.53
CNCB	18.10%	19.20%	0.69	0.66	5.35	4.82
CMBC	22.71%	24.75%	1.08	0.97	6.86	5.81
SPDB	15.92%	15.93%	1.87	1.60	12.40	10.96
CIB	17.54%	18.15%	2.01	1.74	12.28	10.49
CEB	18.88%	23.43%	0.50	0.54	3.70	3.30
HXB	14.47%	14.05%	1.48	1.25	10.81	9.59
PAB	17.20%	16.93%	1.37	1.43	11.09	9.81
BOB	14.82%	14.74%	1.19	1.25	8.70	8.88
BON	14.42%	13.31%	1.40	1.15	10.33	8.96
NBCB	16.60%	16.59%	1.59	1.37	10.05	8.84

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Net interest margin

	2014/01/01-2014/09/30	2013/01/01-2013/09/30
ICBC	2.64%	2.53%
CCB	2.80%	2.71%
BOC	2.26%	2.22%
ABC	2.91%	2.75%
BCM	2.40%	2.53%
CMB	2.50%	2.83%
CNCB	2.37%	2.59%
CMBC	2.61%	2.38%
SPDB	3.04%	2.76%
CIB	2.77%	2.38%
CEB	2.74%	2.59%
HXB	2.71%	2.58%
PAB	2.53%	2.23%
BOB	2.32%	2.38%
BON	2.56%	2.28%
NBCB	2.69%	3.01%
Average	2.62%	2.55%

Source: The banks' 2013 Q3 & 2014 Q3 report, Wind Info, KPMG China research

Operating income

RMB(million)	Net interest income	Net fee and commission income	Investment income	Other operating income	Operating income
2014/01/01-2014/09/30	1,864,791	501,407	23,383	105,471	2,495,052
2013/01/01-2013/09/30	1,646,541	440,173	24,299	61,970	2,172,983

	Net interest income			Net fee and commission income			Investment income			Other operating income			Operating income		
RMB million	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate
ICBC	362,934	327,636	11%	100,885	95,503	6%	3,067	3,775	-19%	21,703	15,003	45%	488,589	441,917	11%
CCB	323,237	286,510	13%	83,801	80,088	5%	3,736	3,949	-5%	18,269	6,843	167%	429,043	377,390	14%
BOC	238,775	208,205	15%	72,078	65,385	10%	3,492	981	256%	31,989	31,038	3%	346,334	305,609	13%
ABC	317,793	275,624	15%	65,920	67,270	-2%	(260)	6,779	-104%	10,513	1,668	530%	393,966	351,341	12%
BCM	102,380	97,635	5%	22,984	19,501	18%	(1,033)	668	-255%	10,838	6,418	69%	135,169	124,222	9%
CMB	82,267	72,572	13%	34,246	21,706	58%	5,564	2,577	116%	2,950	676	336%	125,027	97,531	28%
CNCB	70,048	62,548	12%	18,835	12,390	52%	2,596	601	332%	1,089	1,033	5%	92,568	76,572	21%
CMBC	67,405	60,589	11%	27,810	22,987	21%	1,932	2,721	-29%	2,769	(322)	-960%	99,916	85,975	16%
SPDB	71,508	61,138	17%	15,637	10,138	54%	(240)	470	-151%	2,868	731	292%	89,773	72,477	24%
CIB	69,954	63,111	11%	19,665	16,862	17%	87	405	-79%	1,144	(74)	-1646%	90,850	80,304	13%
CEB	43,469	38,538	13%	13,443	11,106	21%	(79)	(131)	-40%	1,097	(745)	-247%	57,930	48,768	19%
HXB	34,248	28,849	19%	5,781	4,473	29%	447	12	3625%	343	31	1006%	40,819	33,365	22%
PAB	38,418	29,056	32%	12,797	7,415	73%	3,305	898	268%	131	(24)	-646%	54,651	37,345	46%
BOB	22,871	19,536	17%	4,218	3,304	28%	268	299	-10%	443	33	1242%	27,800	23,172	20%
BON	9,639	6,714	44%	1,485	819	81%	366	206	78%	41	(21)	-295%	11,531	7,718	49%
NBCB	9,845	8,280	19%	1,822	1,226	49%	135	89	52%	(716)	(318)	125%	11,086	9,277	19%
Total	1,864,791	1,646,541	13%	501,407	440,173	14%	23,383	24,299	-4%	105,471	61,970	70%	2,495,052	2,172,983	15%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Operating income structure

	Net interest income %		Net fee and commission income %		Investment income %		Other operating income %	
	2014/01/01-2014/09/30	2013/01/01-2013/09/30	2014/01/01-2014/09/30	2013/01/01-2013/09/30	2014/01/01-2014/09/30	2013/01/01-2013/09/30	2014/01/01-2014/09/30	2013/01/01-2013/09/30
ICBC	74.28%	74.15%	20.65%	21.61%	0.63%	0.85%	4.44%	3.39%
CCB	75.34%	75.92%	19.53%	21.22%	0.87%	1.05%	4.26%	1.81%
BOC	68.94%	68.13%	20.81%	21.39%	1.01%	0.32%	9.24%	10.16%
ABC	80.67%	78.45%	16.73%	19.15%	-0.07%	1.93%	2.67%	0.47%
BCM	75.74%	78.60%	17.00%	15.70%	-0.76%	0.54%	8.02%	5.17%
CMB	65.80%	74.41%	27.39%	22.26%	4.45%	2.64%	2.36%	0.69%
CNCB	75.67%	81.69%	20.35%	16.18%	2.80%	0.78%	1.18%	1.35%
CMBC	67.47%	70.47%	27.83%	26.74%	1.93%	3.16%	2.77%	-0.37%
SPDB	79.66%	84.36%	17.42%	13.99%	-0.27%	0.65%	3.19%	1.01%
CIB	77.00%	78.59%	21.65%	21.00%	0.10%	0.50%	1.26%	-0.09%
CEB	75.04%	79.02%	23.21%	22.77%	-0.14%	-0.27%	1.89%	-1.53%
HXB	83.90%	86.46%	14.16%	13.41%	1.10%	0.04%	0.84%	0.09%
PAB	70.29%	77.80%	23.42%	19.86%	6.05%	2.40%	0.24%	-0.06%
BOB	82.27%	84.31%	15.17%	14.26%	0.96%	1.29%	1.59%	0.15%
BON	83.59%	86.99%	12.88%	10.61%	3.17%	2.67%	0.36%	-0.27%
NBCB	88.81%	89.25%	16.43%	13.22%	1.22%	0.96%	-6.46%	-3.42%
Average	76.53%	79.29%	19.66%	18.33%	1.44%	1.22%	2.37%	1.16%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Intermediate business income ratio

	2014/01/01-2014/09/30	2013/01/01-2013/09/30
ICBC	20.65%	21.61%
CCB	19.53%	21.22%
BOC	20.81%	21.39%
ABC	16.73%	19.15%
BCM	17.00%	15.70%
CMB	15.57%	22.26%
CNCB	20.35%	16.18%
CMBC	27.83%	26.74%
SPDB	17.42%	13.99%
CIB	21.65%	21.00%
CEB	23.21%	22.77%
HXB	14.16%	13.41%
PAB	23.42%	19.86%
BOB	15.17%	14.26%
BON	12.88%	10.61%
NBCB	16.43%	13.22%
Average	18.93%	18.33%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Operating expenses

RMB million	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate
ICBC	201,084	177,880	13%
CCB	185,235	149,835	24%
BOC	168,369	143,822	17%
ABC	197,728	173,186	14%
BCM	68,650	61,863	11%
CMB	65,153	45,441	43%
CNCB	49,552	35,584	39%
CMBC	50,754	40,984	24%
SPDB	44,039	33,372	32%
CIB	41,384	36,642	13%
CEB	27,315	21,277	28%
HXB	23,319	18,545	26%
PAB	24,179	17,712	37%
BOB	11,698	9,383	25%
BON	6,351	3,504	81%
NBCB	5,352	4,296	25%
Total	1,170,162	973,326	20%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

General and administrative expenses

RMB million	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate
ICBC	118,873	112,117	6%
CCB	104,254	94,893	10%
BOC	93,462	89,050	5%
ABC	121,332	115,162	5%
BCM	36,549	32,919	11%
CMB	35,127	30,607	15%
CNCB	25,282	22,162	14%
CMBC	30,486	26,354	16%
SPDB	20,665	19,466	6%
CIB	19,475	18,821	3%
CEB	16,578	13,715	21%
HXB	15,260	13,050	17%
PAB	20,056	14,776	36%
BOB	6,529	5,092	28%
BON	3,044	2,294	33%
NBCB	3,457	2,955	17%
Total	670,429	613,433	9%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Cost-to-income ratio

	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate
ICBC	24.33%	25.37%	-4.10%
CCB	25.21%	25.53%	-1.25%
BOC	26.99%	29.14%	-7.38%
ABC	30.80%	32.78%	-6.04%
BCM	27.39%	27.72%	-1.19%
CMB	28.10%	31.38%	-10.45%
CNCB	27.31%	28.94%	-5.63%
CMBC	30.51%	30.65%	-0.46%
SPDB	23.02%	26.86%	-14.30%
CIB	21.65%	23.85%	-9.22%
CEB	28.62%	28.12%	1.78%
HXB	37.38%	39.11%	-4.42%
PAB	36.70%	39.57%	-7.25%
BOB	23.49%	21.98%	6.87%
BON	26.40%	29.72%	-11.17%
NBCB	31.18%	31.85%	-2.10%
Average	28.07%	29.54%	-4.97%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Impairment losses

RMB million	2014/01/01-2014/09/30	2013/01/01-2013/09/30	Growth rate
ICBC	32,456	28,620	13%
CCB	39,424	25,633	54%
BOC	39,078	18,652	110%
ABC	45,021	31,483	43%
BCM	18,309	13,721	33%
CMB	21,998	8,162	170%
CNCB	17,749	7,919	124%
CMBC	13,179	8,722	51%
SPDB	17,048	8,292	106%
CIB	15,120	11,910	27%
CEB	5,960	3,287	81%
HXB	5,234	3,103	69%
PAB	9,701	4,326	124%
BOB	3,175	2,628	21%
BON	2,307	549	320%
NBCB	1,240	749	66%
Total	286,999	177,756	61%

Source: The banks' 2013 Q3 & 2014 Q3 report, KPMG China research

Total assets

	Cash and balances with central bank		Loans and advances to customers		Securities investment		Due from banks and other financial institutions		Other assets		Total assets	
RMB million	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013
ICBC	3,472,425	3,294,007	10,603,544	9,681,415	4,441,560	4,322,244	1,015,345	1,049,887	618,082	570,199	20,150,956	18,917,752
CCB	2,737,700	2,475,001	9,102,547	8,361,361	3,567,684	3,414,617	918,041	754,798	409,891	357,433	16,735,863	15,363,210
BOC	2,560,566	2,114,340	8,256,032	7,439,742	2,533,324	2,403,631	1,380,333	1,233,133	697,702	683,453	15,427,957	13,874,299
ABC	2,810,852	2,603,802	7,650,922	6,902,522	3,557,179	3,220,098	1,516,759	1,443,385	423,537	392,295	15,959,249	14,562,102
BCM	932,196	896,556	3,396,875	3,193,063	1,102,653	1,069,821	495,909	566,429	285,085	235,068	6,212,718	5,960,937
CMB	590,593	517,239	2,384,121	2,148,330	994,893	756,830	647,077	505,802	105,964	88,198	4,722,648	4,016,399
CNCB	536,648	496,476	2,070,721	1,899,921	885,337	643,985	462,279	540,792	90,902	60,019	4,045,887	3,641,193
CMBC	438,533	433,802	1,714,728	1,539,447	461,698	304,736	928,694	767,335	225,688	180,890	3,769,341	3,226,210
SPDB	489,574	476,342	1,920,895	1,725,745	1,063,259	850,707	396,779	556,083	86,135	71,248	3,956,642	3,680,125
CIB	433,425	422,871	1,450,544	1,320,682	875,259	752,259	1,100,487	1,071,026	135,862	110,597	3,995,577	3,677,435
CEB	350,266	312,643	1,245,370	1,142,138	575,968	493,057	341,502	360,626	68,312	106,622	2,581,418	2,415,086
HXB	286,689	262,227	884,979	800,726	216,403	194,671	367,776	389,257	28,245	25,566	1,784,092	1,672,447
PAB	277,325	229,924	974,160	832,127	440,010	391,211	352,577	370,847	100,286	67,632	2,144,358	1,891,741
BOB	172,743	170,687	649,872	568,852	315,483	276,904	328,015	297,976	24,540	22,344	1,490,653	1,336,763
BON	61,479	49,594	162,230	143,058	250,383	151,364	58,650	79,870	13,546	10,172	546,288	434,058
NBCB	62,677	62,195	196,638	167,302	206,967	143,568	53,039	79,050	18,600	15,657	537,921	467,772
Total	16,213,691	14,817,706	52,664,178	47,866,431	21,488,060	19,389,703	10,363,262	10,066,296	3,332,377	2,997,393	104,061,568	95,137,529

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Total asset structure

	Cash and balances with central bank %		Loans and advances to customers %		Securities investment %		Due from banks and other financial institutions %		Other assets %	
	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013
ICBC	17.23%	17.41%	52.62%	51.18%	22.04%	22.85%	5.04%	5.55%	3.07%	3.01%
CCB	16.36%	16.11%	54.39%	54.42%	21.32%	22.23%	5.49%	4.91%	2.45%	2.33%
BOC	16.60%	15.24%	53.51%	53.62%	16.42%	16.26%	8.95%	8.89%	4.52%	5.99%
ABC	17.61%	17.88%	47.94%	47.40%	22.29%	22.11%	9.50%	9.91%	2.65%	2.69%
BCM	15.00%	15.04%	54.68%	53.57%	17.75%	17.95%	7.98%	9.50%	4.59%	3.94%
CMB	12.51%	12.88%	50.48%	53.49%	21.07%	18.84%	13.70%	12.59%	2.24%	2.20%
CNCB	13.26%	13.63%	51.18%	52.18%	21.88%	17.69%	11.43%	14.85%	2.25%	1.65%
CMBC	11.63%	13.45%	45.49%	47.72%	12.25%	9.45%	24.64%	23.78%	5.99%	5.61%
SPDB	12.37%	12.94%	48.55%	46.89%	26.87%	23.12%	10.03%	15.11%	2.18%	1.94%
CIB	10.85%	11.50%	36.30%	35.91%	21.91%	20.46%	27.54%	29.12%	3.40%	3.01%
CEB	13.57%	12.95%	48.24%	47.29%	22.31%	20.42%	13.23%	14.93%	2.65%	4.41%
HXB	16.07%	15.68%	49.60%	47.88%	12.13%	11.64%	20.61%	23.27%	1.58%	1.53%
PAB	12.93%	12.15%	45.43%	43.99%	20.52%	20.68%	16.44%	19.60%	4.68%	3.58%
BOB	11.59%	12.77%	43.60%	42.55%	21.16%	20.71%	22.00%	22.29%	1.65%	1.67%
BON	11.25%	11.43%	29.70%	32.96%	45.83%	34.87%	10.74%	18.40%	2.48%	2.34%
NBCB	11.65%	13.30%	36.56%	35.77%	38.48%	30.69%	9.86%	16.90%	3.46%	3.35%
Average	13.78%	14.02%	46.77%	46.68%	22.76%	20.38%	13.57%	15.60%	3.11%	3.08%

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Scale of loan

RMB million	30/09/2014	31/12/2013	Growth rate
ICBC	10,853,652	9,922,374	9%
CCB	9,349,489	8,590,057	9%
BOC	8,444,403	7,607,791	11%
ABC	7,997,605	7,224,713	11%
BCM	3,479,148	3,266,368	7%
CMB	2,445,504	2,197,094	11%
CNCB	2,124,128	1,941,175	9%
CMBC	1,750,969	1,574,263	11%
SPDB	1,971,735	1,767,494	12%
CIB	1,492,121	1,357,057	10%
CEB	1,272,144	1,166,310	9%
HXB	910,394	823,169	11%
PAB	992,892	847,289	17%
BOB	668,700	584,862	14%
BON	167,319	146,961	14%
NBCB	200,951	171,190	17%
Total	54,121,154	49,188,167	10%

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Loan quality

	NPL ratio		Allowance to NPL		Allowance to total loans ratio	
	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013
ICBC	1.06%	0.94%	216.60%	257.19%	2.30%	2.42%
CCB	1.13%	0.99%	234.47%	268.22%	2.65%	2.66%
BOC	1.07%	0.96%	207.70%	229.35%	2.22%	2.20%
ABC	1.29%	1.22%	335.07%	367.04%	4.32%	4.48%
BCM	1.17%	1.05%	201.29%	213.65%	2.36%	2.24%
CMB	1.10%	0.83%	227.99%	266.00%	2.51%	2.21%
CNCB	1.39%	1.03%	181.49%	206.62%	2.51%	2.13%
CMBC	1.04%	0.85%	199.96%	259.74%	2.07%	2.21%
SPDB	0.96%	0.74%	267.90%	319.65%	2.58%	2.37%
CIB	0.99%	0.76%	281.41%	352.10%	2.79%	2.68%
CEB	1.07%	0.86%	197.00%	241.02%	2.11%	2.07%
HXB	0.96%	0.90%	289.83%	301.53%	2.78%	2.71%
PAB	0.98%	0.89%	191.82%	201.06%	1.88%	1.79%
BOB	0.76%	0.65%	336.57%	385.91%	2.56%	2.51%
BON	0.94%	0.89%	321.98%	298.51%	3.03%	2.66%
NBCB	0.89%	0.89%	241.12%	254.88%	2.15%	2.27%
Average	1.05%	0.98%	245.76%	274.58%	2.55%	2.68%

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Securities investment structure

	Financial assets at fair value through profit or loss		Available-for-sale financial assets		Held-to-maturity investments		Investment classified as receivables		Total	
RMB million	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013
ICBC	346,948	372,556	1,157,309	1,000,800	2,593,886	2,624,400	343,417	324,488	4,441,560	4,322,244
CCB	294,545	364,050	809,711	760,292	2,271,926	2,100,538	191,502	189,737	3,567,684	3,414,617
BOC	92,924	75,200	749,358	701,196	1,371,457	1,210,531	319,585	416,704	2,533,324	2,403,631
ABC	396,213	322,882	884,259	781,311	1,674,298	1,523,815	602,409	592,090	3,557,179	3,220,098
BCM	77,940	59,083	226,217	220,397	639,463	670,615	159,033	119,726	1,102,653	1,069,821
CMB	40,880	23,223	288,167	289,265	252,213	208,927	413,633	235,415	994,893	756,830
CNCB	17,561	11,018	185,770	177,960	171,222	154,849	510,784	300,158	885,337	643,985
CMBC	27,479	22,262	137,843	111,532	167,927	133,124	128,449	37,818	461,698	304,736
SPDB	30,435	28,627	201,063	160,593	135,389	146,253	696,372	515,234	1,063,259	850,707
CIB	31,848	42,295	294,549	263,681	185,483	117,655	363,379	328,628	875,259	752,259
CEB	10,381	12,490	129,101	111,948	109,602	105,920	326,884	262,699	575,968	493,057
HXB	6,425	8,699	61,606	65,134	133,563	109,265	14,809	11,573	216,403	194,671
PAB	14,808	10,421	2,476	467	200,189	195,667	222,537	184,656	440,010	391,211
BOB	12,235	13,221	101,225	96,431	111,472	107,381	90,551	59,871	315,483	276,904
BON	6,679	3,455	44,221	45,063	64,644	39,319	134,837	63,527	250,381	151,364
NBCB	4,727	1,179	126,139	90,355	15,462	15,950	60,638	36,084	206,966	143,568
Total	1,412,028	1,370,661	5,399,014	4,876,425	10,098,196	9,464,209	4,578,819	3,678,408	21,488,057	19,389,703

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Liabilities

	Deposits from customers		Liabilities from banks and other financial institutions		Debt certificates issued		Other liabilities		Total	
RMB million	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013
ICBC	15,339,964	14,620,825	1,740,005	1,568,559	268,726	253,018	1,369,886	1,196,887	18,718,581	17,639,289
CCB	12,982,406	12,223,037	1,262,028	909,885	434,863	357,540	848,387	798,419	15,527,684	14,288,881
BOC	11,047,285	10,097,786	2,114,057	1,890,889	282,002	224,704	938,356	699,443	14,381,700	12,912,822
ABC	12,638,575	11,811,411	1,153,712	930,504	331,208	266,261	877,061	709,389	15,000,556	13,717,565
BCM	4,116,546	4,157,833	1,295,422	1,120,692	116,757	82,238	226,113	178,690	5,754,838	5,539,453
CMB	3,265,520	2,775,276	914,821	792,478	101,047	68,936	138,862	113,753	4,420,250	3,750,443
CNCB	2,875,725	2,651,678	702,167	609,568	126,959	76,869	83,351	72,353	3,788,202	3,410,468
CMBC	2,397,690	2,146,689	832,149	638,244	129,829	91,968	168,870	145,022	3,528,538	3,021,923
SPDB	2,688,621	2,419,696	767,321	854,055	105,110	71,970	161,091	127,177	3,722,143	3,472,898
CIB	2,205,228	2,170,345	1,351,479	1,167,597	123,378	67,901	78,576	70,421	3,758,661	3,476,264
CEB	1,728,279	1,605,278	557,360	552,585	64,884	42,247	57,759	61,924	2,408,282	2,262,034
HXB	1,267,922	1,177,592	365,238	374,408	20,396	8,400	33,634	26,028	1,687,190	1,586,428
PAB	1,508,179	1,217,002	404,425	509,471	45,481	8,102	59,537	45,085	2,017,622	1,779,660
BOB	906,585	834,480	413,849	366,848	48,034	39,898	30,103	17,232	1,398,571	1,258,458
BON	342,908	260,149	139,636	130,412	18,975	10,278	13,791	6,362	515,310	407,201
NBCB	307,060	255,278	130,516	140,142	27,823	18,466	39,791	28,364	505,190	442,250

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Liability structure

	Deposits from customers %		Liabilities from banks and other financial institutions %		Debt certificates issued %		Other liabilities %	
	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013	30/09/2014	31/12/2013
ICBC	81.94%	82.89%	9.30%	8.89%	1.44%	1.43%	7.32%	6.79%
CCB	83.61%	85.54%	8.13%	6.37%	2.80%	2.50%	5.46%	5.59%
BOC	76.82%	78.20%	14.70%	14.64%	1.96%	1.74%	6.52%	5.42%
ABC	84.25%	86.10%	7.69%	6.78%	2.21%	1.94%	5.85%	5.17%
BCM	71.53%	75.06%	22.51%	20.23%	2.03%	1.48%	3.93%	3.23%
CMB	73.87%	74.00%	20.70%	21.13%	2.29%	1.84%	3.14%	3.03%
CNCB	75.91%	77.75%	18.54%	17.87%	3.35%	2.25%	2.20%	2.12%
CMBC	67.95%	71.04%	23.58%	21.12%	3.68%	3.04%	4.79%	4.80%
SPDB	72.23%	69.67%	20.62%	24.59%	2.82%	2.07%	4.33%	3.66%
CIB	58.67%	62.43%	35.96%	33.59%	3.28%	1.95%	2.09%	2.03%
CEB	71.76%	70.97%	23.14%	24.43%	2.69%	1.87%	2.40%	2.74%
HXB	75.15%	74.23%	21.65%	23.60%	1.21%	0.53%	1.99%	1.64%
PAB	74.75%	68.38%	20.04%	28.63%	2.25%	0.46%	2.95%	2.53%
BOB	64.82%	66.31%	29.59%	29.15%	3.43%	3.17%	2.15%	1.37%
BON	66.54%	63.89%	27.10%	32.03%	3.68%	2.52%	2.68%	1.56%
NBCB	60.78%	57.72%	25.84%	31.69%	5.51%	4.18%	7.88%	6.41%
Average	72.54%	72.76%	20.57%	21.55%	2.79%	2.06%	4.10%	3.63%

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Loan-to-deposit ratio

	30/09/2014	31/12/2013
ICBC	68.10%	66.60%
CCB	72.02%	70.28%
BOC	71.65%	72.52%
ABC	63.28%	61.17%
BCM	73.92%	73.40%
CMB	74.89%	74.44%
CNCB	73.86%	73.21%
CMBC	73.03%	73.39%
SPDB	73.25%	73.01%
CIB	67.66%	62.53%
CEB	73.61%	72.59%
HXB	70.24%	69.90%
PAB	64.57%	68.64%
BOB	73.76%	68.74%
BON	48.79%	56.49%
NBCB	60.32%	61.97%
Average	68.93%	68.68%

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Capital adequacy ratio and core capital adequacy ratio

	Capital adequacy ratio		Core capital adequacy ratio	
	30/09/2014	31/12/2013	30/09/2014	31/12/2013
ICBC	14.20%	13.12%	11.80%	10.57%
CCB	14.53%	13.34%	11.65%	10.75%
BOC	13.07%	12.46%	10.52%	9.69%
ABC	12.38%	11.86%	8.90%	9.25%
BCM	13.80%	12.08%	11.10%	9.76%
CMB	12.28%	11.14%	10.35%	9.27%
CNCB	12.99%	11.24%	9.35%	8.78%
CMBC	10.95%	10.69%	8.74%	8.72%
SPDB	10.91%	10.97%	8.63%	8.58%
CIB	12.18%	10.83%	9.40%	8.68%
CEB	11.48%	10.57%	9.46%	9.11%
HXB	11.02%	9.88%	8.41%	8.03%
PAB	11.00%	9.90%	8.78%	8.56%
BON	10.80%	12.90%	8.62%	10.10%
NBCB	12.16%	12.06%	10.01%	9.35%
Average	12.25%	11.53%	9.71%	9.27%

Source: The banks' 2013 annual reports & 2014 Q3 report, KPMG China research

Glossary of abbreviated terms

Bank names

- ❑ PBOC – People's Bank of China
- ❑ ICBC – Industrial and Commercial Bank of China
- ❑ CCB – China Construction Bank
- ❑ BOC – Bank of China
- ❑ ABC – Agricultural Bank of China
- ❑ BCM – Bank of Communications
- ❑ CMB – China Merchants Bank
- ❑ CNCB – China CITIC Bank
- ❑ CMBC – China Minsheng Bank
- ❑ SPDB – Shanghai Pudong Development Bank
- ❑ CIB – Industrial Bank
- ❑ CEB – China Everbright Bank
- ❑ HXB – Hua Xia Bank Co.,Ltd
- ❑ PAB – PingAn Bank Co., Ltd
- ❑ BOB – Bank of Beijing Co., Ltd
- ❑ BON – Bank of Nanjing Co., Ltd
- ❑ NBCB – Bank of Ningbo Co., Ltd

General terms

- ❑ MOF – Ministry of Finance
- ❑ CBRC – China Banking Regulatory Commission
- ❑ CSRC – China Securities Regulatory Commission
- ❑ SAFE – State Administration of Foreign Exchange
- ❑ SSE – Shanghai Stock Exchange
- ❑ SEHK-The Stock Exchange of Hong Kong
- ❑ SHIBOR – Shanghai Interbank Offered Rate
- ❑ NIM – Net interest margin

Contact us

KPMG China has around 9,000 staff, working in 16 offices: Beijing, Chengdu, Chongqing, Foshan, Fuzhou, Guangzhou, Hangzhou, Nanjing, Qingdao, Shanghai, Shenyang, Shenzhen, Tianjin, Xiamen, Hong Kong SAR and Macau SAR.

Our dedicated financial services team brings together partners from audit, tax and advisory practices and is linked closely to other member firms in the KPMG network.

For more information, contact one of the financial services partners listed below.

Simon Gleave

Asia Pacific Partner-in-charge,
Financial Services
Tel: +86(10)8508 7007
simon.gleave@kpmg.com

Thomas Chan

Tel: +86(10)8508 7014
thomas.chan@kpmg.com

Christine Song

Tel: +86(10)8508 7015
christine.song@kpmg.com

Walkman Lee

Tel: +86(10)8508 7043
walkman.lee@kpmg.com

Raymond Li

Tel: +86(10)8508 7114
raymond.li@kpmg.com

Larry Choi

Tel: +86(20)3813 8883
larry.choi@kpmg.com

Edwina Li

China Partner-in-charge,
Financial Services Assurance
Tel: +86(21)2212 3806
edwina.li@kpmg.com

Paul McSheaffrey

Tel: +852 2978 8236
paul.mcsheaffrey@kpmg.com

Kenny Shi

Tel: +86(21)2212 2261
kenny.shi@kpmg.com

James Chen

Tel: +86(21)2212 2424
james.chen@kpmg.com

Arthur Wang

Tel: +86(10)8508 7104
arthur.wang@kpmg.com

Ivan Li

Tel: +86(755)2547 1218
ivan.li@kpmg.com

Lewis Lu

Partner-in-charge, Tax
Tel: +86(21)2212 3421
lewis.lu@kpmg.com

Kevin Liu

IT Advisory
Tel: +86(10)8508 7094
kevin.liu@kpmg.com

Louis Ng

Transaction Services
Tel: +86(10)8508 7090
louis.ng@kpmg.com

Derrick Day

DPP Accounting
Tel: +86(10)8508 5008
derrick.day@kpmg.com

Tony Cheung

Partner-in-charge, Advisory
Tel: +86(21)2212 2705
tony.cheung@kpmg.com

Egidio Zarrella

Management Consulting
Tel: +852 2847 5197
egidio.zarrella@kpmg.com

Joan Ho

Management Consulting
Tel: +852 2826 7104
joan.ho@kpmg.com

Contact us

Beijing

8th Floor, Tower E2, Oriental Plaza
1 East Chang An Avenue
Beijing 100738, China
Tel : +86 (10) 8508 5000
Fax : +86 (10) 8518 5111

Chengdu

18th Floor, Tower 1, Plaza Central
8 Shuncheng Avenue
Chengdu 610016, China
Tel : +86 (28) 8673 3888
Fax : +86 (28) 8673 3838

Chongqing

Unit 1507, 15th Floor,
Metropolitan Tower
68 Zourong Road
Chongqing 400010, China
Tel : +86 (23) 6383 6318
Fax : +86 (23) 6383 6313

Foshan

8th Floor, One AIA Financial Center
1 East Denghu Road
Foshan 528200, China
Tel : +86 (757) 8163 0163
Fax : +86 (757) 8163 0168

Fuzhou

25th Floor, Fujian BOC Building
136 Wu Si Road
Fuzhou 350003, China
Tel : +86 (591) 8833 1000
Fax : +86 (591) 8833 1188

Guangzhou

38th Floor, Teem Tower
208 Tianhe Road
Guangzhou 510620, China
Tel : +86 (20) 3813 8000
Fax : +86 (20) 3813 7000

Hangzhou

8th Floor, West Tower, Julong
Building
9 Hangda Road
Hangzhou 310007, China
Tel : +86 (571) 2803 8000
Fax : +86 (571) 2803 8111

Nanjing

46th Floor, Zhujiang No.1 Plaza
1 Zhujiang Road
Nanjing 210008, China
Tel : +86 (25) 8691 2888
Fax : +86 (25) 8691 2828

Qingdao

4th Floor, Inter Royal Building
15 Donghai West Road
Qingdao 266071, China
Tel : +86 (532) 8907 1688
Fax : +86 (532) 8907 1689

Shanghai

50th Floor, Plaza 66
1266 Nanjing West Road
Shanghai 200040, China
Tel : +86 (21) 2212 2888
Fax : +86 (21) 6288 1889

Shenyang

27th Floor, Tower E, Fortune Plaza
59 Beizhan Road
Shenyang 110013, China
Tel : +86 (24) 3128 3888
Fax : +86 (24) 3128 3899

Shenzhen

9th Floor, China Resources Building
5001 Shennan East Road
Shenzhen 518001, China
Tel : +86 (755) 2547 1000
Fax : +86 (755) 8266 8930

Tianjin

Unit 15, 47th Floor, Office Tower
Tianjin World Financial Center
2 Dagou North Road
Tianjin 300020, China
Tel : +86 (22) 2329 6238
Fax : +86 (22) 2329 6233

Xiamen

12th Floor, International Plaza
8 Lujiang Road
Xiamen 361001, China
Tel : +86 (592) 2150 888
Fax : +86 (592) 2150 999

Hong Kong

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong
23rd Floor, Hysan Place
500 Hennessy Road
Causeway Bay, Hong Kong
Tel : +852 2522 6022
Fax : +852 2845 2588

Macau

24th Floor, B&C, Bank of
China Building
Avenida Doutor Mario Soares
Macau
Tel : +853 2878 1092
Fax : +853 2878 1096



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