

New Features and New Risks of Global Banking Industry and Development of China's Banking Industry

**Dr. Zong Liang, DGM of the Strategic
Development Department of Bank of China**

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- Latest development of global banking industry

- Overall trend
- Pattern evolution
- Emerging risks
- Integration

- Current status of China's banking industry

- Next step to sustain the development trend

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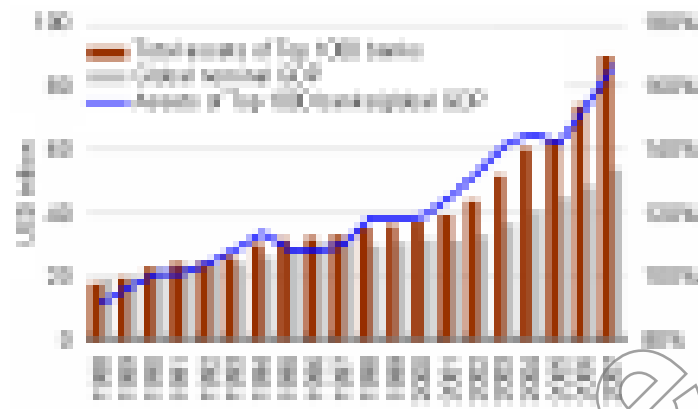
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Latest development of global banking industry

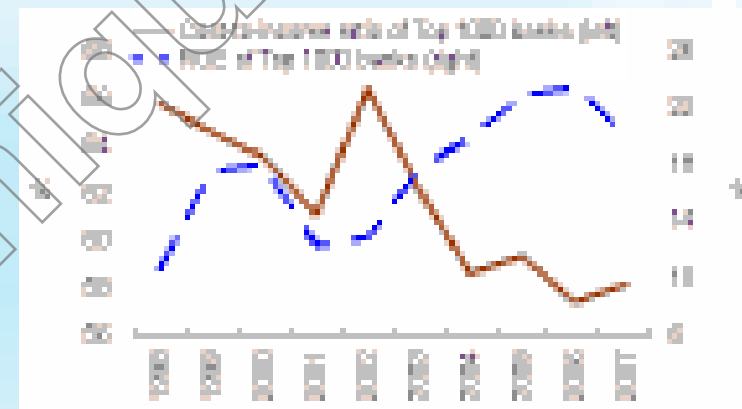


➤ Overall trend

Rapid growth of banking industry's total assets & evident increase of ratio against GDP



Decline of cost-to-income ratio & brilliant business performance



- ✓ Total assets of Top 1000 banks recorded an average growth rate of 13.2% in the new century
- ✓ As of the end of 2007, total assets of Top 1000 banks were USD90.3 trillion, with the ratio against global GDP increasing from 101% in 1990 to 166%.
- ✓ Rapid growth of total assets in the banking industry, worldwide liquidity excess, rapid growth of global economy and changes in financial system are all related to the management and innovation of banking institutions.
- ✓ Continual USD depreciation and accelerated M&A moves also imposed important influence.

- ✓ In 2007, profits before tax of the Top 1000 banks hit USD780.8 billion.
- ✓ ROE of the Top 1000 banks averaged 18.3% from 2000 to 2007, in contrast to ROE of 13.1% in the 1990s.
- ✓ Rapid growth of real economy is the most important reason for the brilliant performance of the banking industry in the new century, while decline of the cost-to-income ratio also played an essential part.
- ✓ The sub-prime crisis in 2007 exerted a negative impact on operations of the global banking industry.

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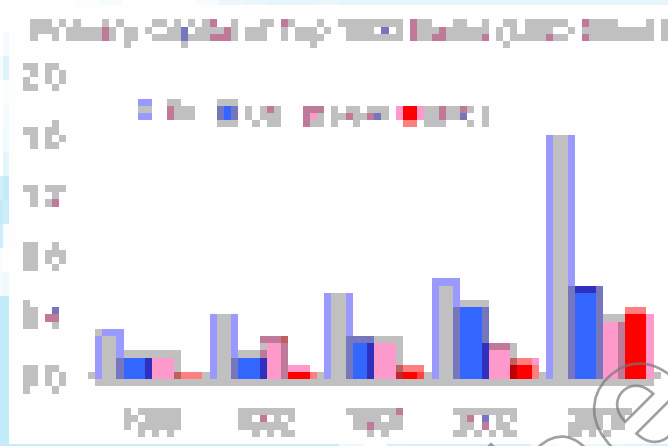


Latest development of global banking industry

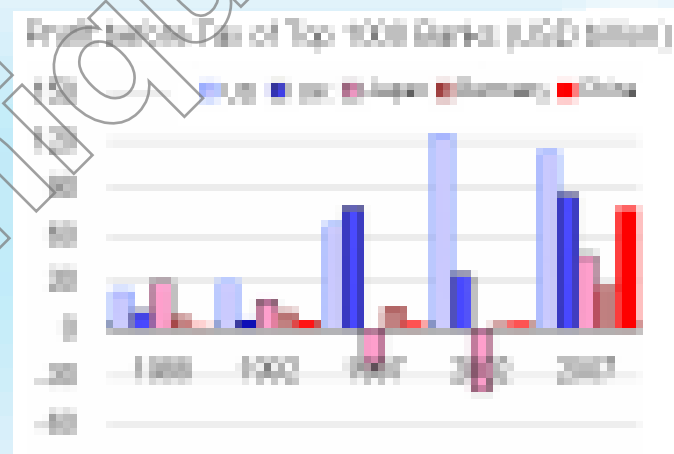


➤ Pattern evolution

Large capital scale of European banking industry & the rise of emerging markets



Profitability of the banking industry kept booming in US and UK, declined in Japan and Germany, and improved in China



- ✓ Banks in Europe, US and Japan used to dominate the global market before the 21st century.
- ✓ The banking industry of Europe has maintained a strong growth momentum since 2000, and EU27 occupied 42% of the primary assets of Top 1000 banks in 2007.
- ✓ Banks of emerging markets rose up quickly after 2000, and banks of BRICs exceeded that of Japan for the first time in terms of ratio of primary capital in total of Top 1000 banks in 2007.
- ✓ Generally speaking, the global banking industry's pattern has become more balanced since the 21st century.

- ✓ Seen from profitability, the global banking industry is becoming increasingly diversified.
- ✓ US and UK maintained good profitability, Japan and Germany delivered average performance, while China witnessed rapid growth in the 21st century.
- ✓ The sub-prime crisis put the most severe impact on the profitability of US banking industry in 2007, reducing its ratio of profits before tax in that of Top 1000 banks.
- ✓ The sub-prime crisis will further boost diversification of the pattern of global banking industry.

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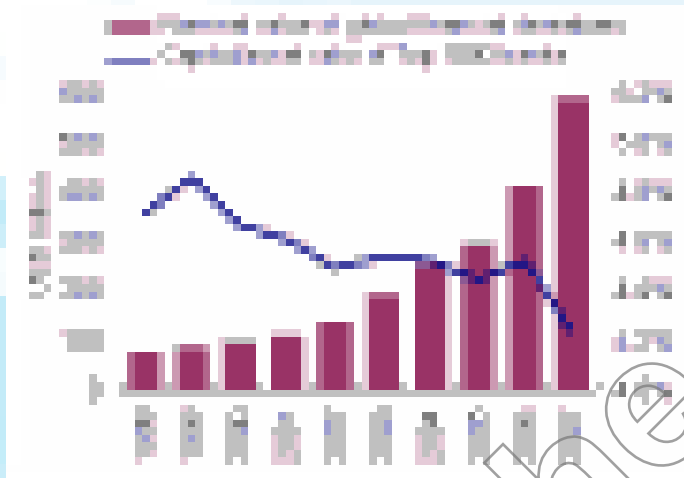


Latest development of global banking industry

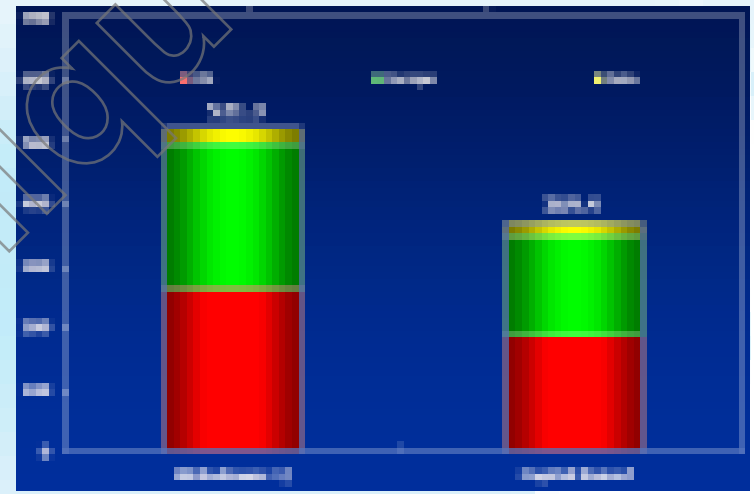


➤ Emerging risks

Financial innovation developed over fast, and capital/asset ratio of banking industry declined



Huge risk exposure of US sub-prime crisis enhanced the market worries about prospect



- ✓ Over rapid development of the global banking industry in the 21st century brought about significant hazards.
- ✓ Financial innovation posted over fast development; e.g. nominal value of OTC financial derivatives on global market was only USD100 trillion in 2000 and grew to nearly USD600 trillion as of 2007.
- ✓ Banking regulation was strengthened with the launch of new standards under Basel Accord, but the capital/asset ratio of global banking industry continued to decline.
- ✓ Financial innovation exposed its feature of a “double-edged sword”.

- ✓ The US sub-prime crisis brought about huge losses to the global banking industry.
- ✓ As of September 2008, the asset written down in the global banking industry was USD521.3 billion, and capitals of USD369.4 billion were injected to cope with the sub-prime crisis.
- ✓ According to IMF, the losses resulted from the sub-prime crisis in the banking industry will further increase and is expected to exceed USD1 trillion.
- ✓ The future development momentum of the global banking industry remains unclear.

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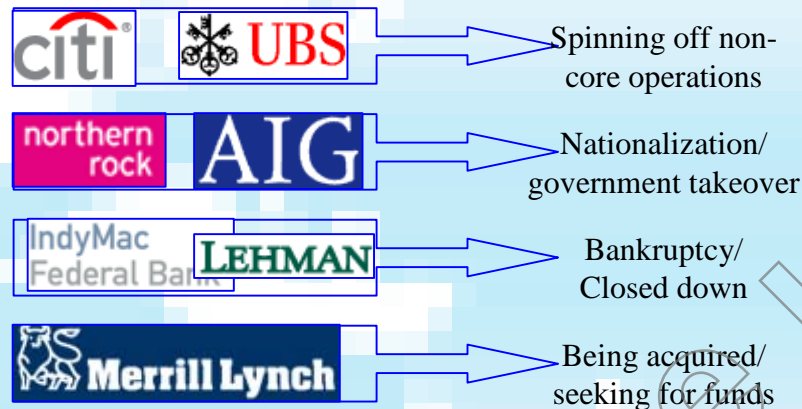


Latest development of global banking industry



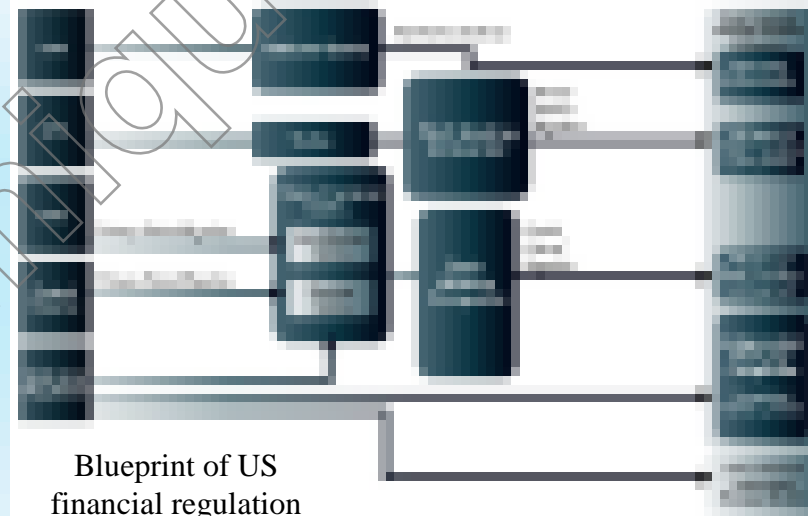
➤ Integration

Industrial structure further integrates amidst bankruptcies and M&As



- ✓ The industrial integration intensified in the context of economic recession and financial crisis.
- ✓ Large banks such as Citigroup and UBS sorted out their balance sheets and spun off the non-core operations.
- ✓ The financial institutions represented by Northern Rock and Lehman were either nationalized or acquired or went bankrupt.
- ✓ Significant changes will continue to take place in the future global banking industry.

Financial regulators cope with the great crisis challenges with reforms



- ✓ The US plans to establish a blueprint of financial regulation to reconstruct the regulatory system.
- ✓ The regulators of main developed economies created various ways to rescue the market, including liquidity injection, playing the role of lender of last resort and direct takeover, etc.
- ✓ The US government established a USD700 billion bill to rescue the market and other countries expressed willingness to support their actions with an aim to cope with the “once-in-a-century” crisis.
- ✓ The future development of the global banking industry is full of uncertainties.

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- Latest development of global banking industry

- Current status of China's banking industry

 - Strength

 - Weakness

 - Opportunity

 - Threats

- Next step to sustain the development trend

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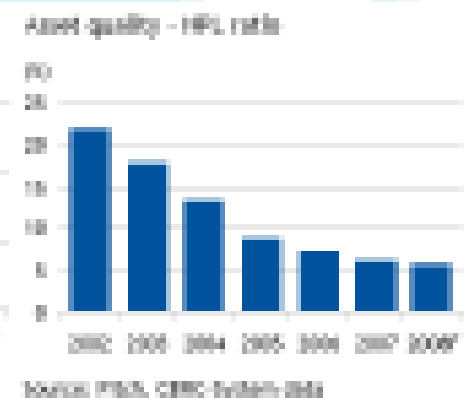
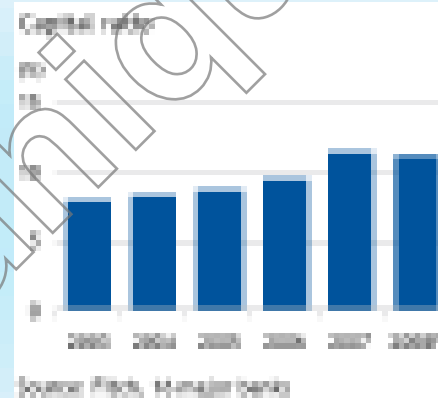
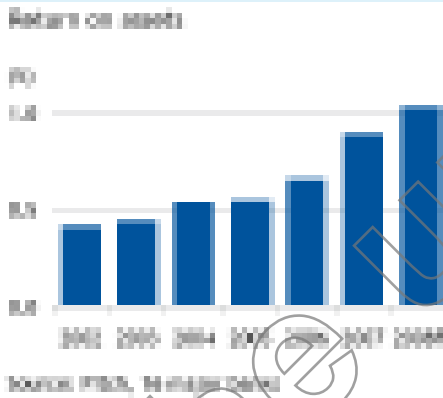
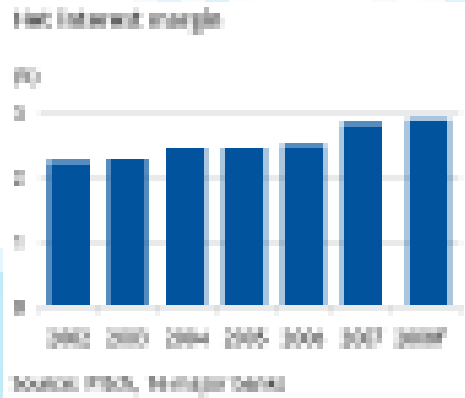
Current status of China's banking industry



➤ Strength

Rich interest margin & steady growth of earnings

Prudent operation & adequate capital



- ✓ China's banking industry posted sharp increase of earnings in the past five years.
- ✓ Wide interest margin provided a sound condition for sustainable growth of the banking industry; and rapid development of the financial market boosted the increase of non-interest income.
- ✓ In H1 2008, China's banking industry achieved rapid development against the widespread depression in the global banking industry.
- ✓ With the rapid growth of macro economy, China's banking industry will continue to deliver sound performance in the future.

- ✓ Development of China's banking industry has become increasingly prudent in the past five years.
- ✓ Capital adequacy ratio continued to rise, the asset quality improved, and the provisioning coverage ratio expanded.
- ✓ In H1 2008, the banking industry's NPL ratio dropped to 6.5%; and 175 banks met the required capital adequacy ratio. The proportion of qualified assets increased to 81.3%.
- ✓ Sound development prevented China's banking industry from being severely affected by external impacts.

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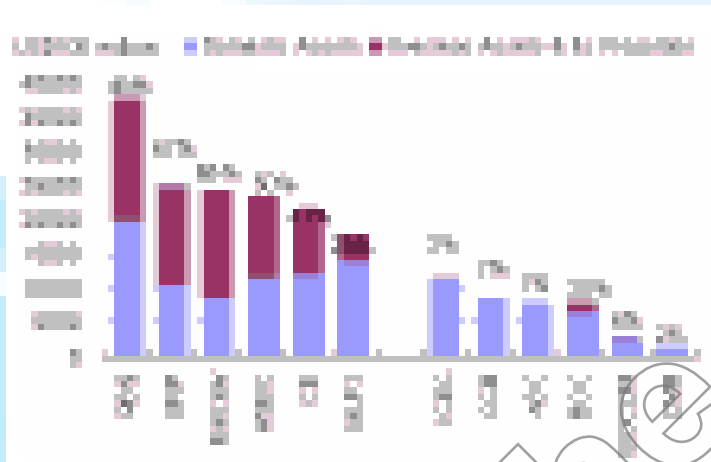


Current status of China's banking industry



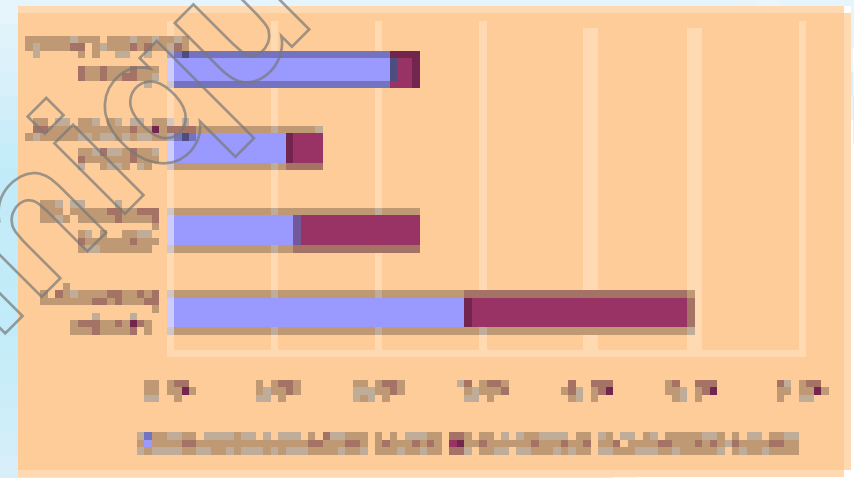
➤ Weakness

Small scale & insufficient overseas expansion



- ✓ The asset scale of China's banking industry remains small.
- ✓ China's largest bank in terms of asset scale ranked only the 19th place among the Top 1000 banks in 2008.
- ✓ As a reflection of the small asset scale, the pace of "Going Global" needs to be accelerated and the overseas assets account for less than 5% of total in China's banking industry.
- ✓ With full globalization of China's economy and trade, the banking industry is expected to make further overseas expansion.

Limited product scope, unbalanced income structure



- ✓ The products of China's banking industry remains scarce.
- ✓ The banking industry highly depends on traditional credit and settlement businesses, and innovation of capital market tools shall be strengthened.
- ✓ Fee-based businesses developed fast since 2007; but the proportion of non-interest income in China's banking industry remains under 20% up to now, indicating a huge gap from the international large banks.
- ✓ China's banking industry calls for in-depth transformation and product innovation.

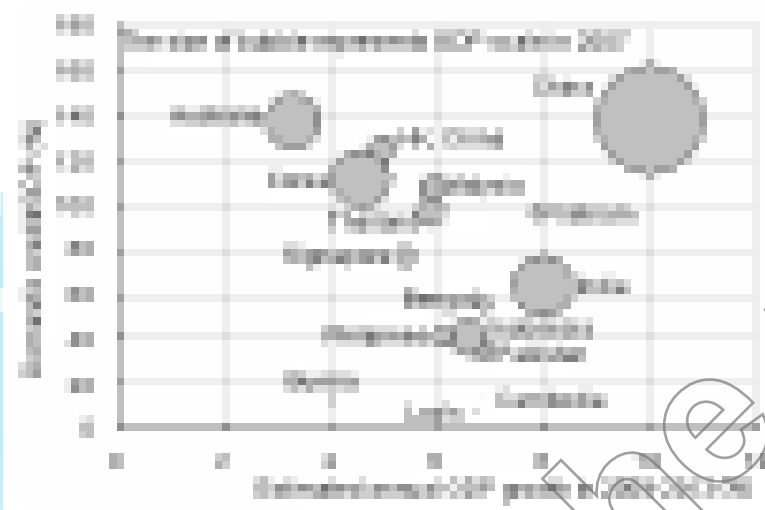
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Current status of China's banking industry



➤ Opportunity

Extensive market & sub-prime crisis



Reform and opening up, & comprehensive operation

Interest rate marketization

- More effective monetary policies
- More yield for depositors
- More reasonable fund costs
- Less distortion of banking system

Open-up of capital account

- More volatile exchange rate
- Linkage of domestic and overseas markets
- Higher regulatory requirements
- Increased demand for banking products

✓ China's banking industry is faced with new opportunities.
 ✓ As the domestic economy may sustain annual growth rate of 8-9% in the next 10 years, China's banking market is likely to top the world.
 ✓ With the increasingly close economic and trade connection between China and the Asia-Pacific, the most booming area in the next 10 years, there is plenty of room for China's banking industry to make global presence.
 ✓ The sub-prime crisis also provided China's banking industry with the opportunity to enter the developed markets.

✓ China will continue to reform its financial system.
 ✓ Product innovation and comprehensive operation of the banking industry has spacious room for further development.
 ✓ The banking industry will continue its expansion through restructuring on the domestic market and public offering.
 ✓ The sub-prime crisis left China's banking industry a precious lesson to avert the same mistake.

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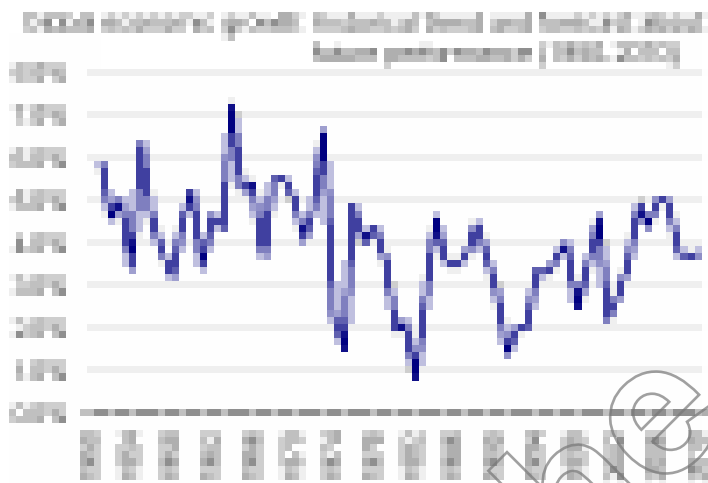


Current status of China's banking industry



➤ Threat

Economic cycles & sub-prime crisis



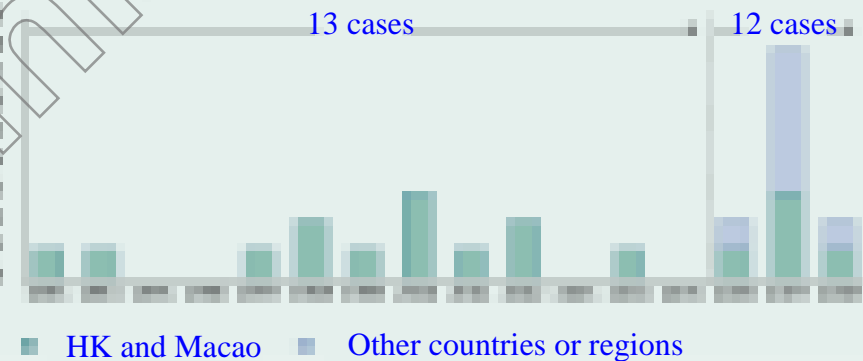
- ✓ China's economic growth slowed down along with the cyclical correction of global economy.
- ✓ The US sub-prime crisis has not yet hit the bottom, China's banking industry will be affected through the demand channels of real economies and the infection channel of financial markets.
- ✓ China's banking institutions have never experienced such a huge economic and financial crisis, and shall keep a prudent and proactive attitude towards it.
- ✓ Particularly, pay attention to the challenges from real estate market and export-oriented sectors.

Transformation of economy and management

Overseas M&A of China's Financial Institutions (1993-2008.9)

The 1st round mainly took place in Hong Kong and Macao

2nd round



- ✓ Economic transformation is onward in China.
- ✓ The transformation from eastern areas to western areas, from low end to high end and from export to domestic demand inevitably comes with pains and throes.
- ✓ China's banking industry is undergoing transformation in the meantime.
- ✓ The transformation from traditional banking businesses to new businesses, from separate operation to integrated operation and from domestic orientation to focus on both domestic and overseas operations involves many risk factors.

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- New development of global banking industry
- Current status of China's banking industry
- Next step to sustain the development trend
 - Open-up
 - Cooperation
 - Innovation
 - Control

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Next step to sustain the development trend



➤ Resolutely keep to the principle of open-up

Introduce: management experience, products and technologies

- ✓ China's banking industry calls for introduction.
- ✓ Management experience: including human resource management, risk management, business line management and other advanced experiences.
- ✓ Products: products for high-end customers, products linked to the financial market and products diversifying risks.
- ✓ Technologies: IT technology, service support, and etc.

Go abroad: support industrial enterprises and diversify risks

- ✓ China's banking industry shall accelerate the pace of "going global"
- ✓ Support more industrial enterprises to go abroad and support financial markets to realize bilateral open-up.
- ✓ Exploit more overseas markets and diversify operation risks with diversified growth pattern.
- ✓ Cooperate with overseas financial institutions to make better use of domestic funds.

➤ Give top priority to cooperation

Cooperation between banks and real economy

- ✓ Banks shall support the growth of real economy.
- ✓ The US sub-prime crisis shows that development of financial industry must be based on real economy and that it involves great risk developing finance on the basis of finance.
- ✓ Banks must adapt to the changes in the structure of real economy and support real economy with more products and services.
- ✓ Banks shall keep aware of their social responsibilities and strive to build "green banks".

Cooperation between banks and securities and insurance companies

- ✓ It is necessary for banks to cooperate with other financial sectors.
- ✓ On the one hand, the demand for financial services is becoming increasingly diversified, ranging from financing to investment and to insurance; on the other hand, the securities and insurance sector is willing to cooperate with banks.
- ✓ It may achieve the economy of scales and synergetic effect combining the demands for various financial services and providing a package of financial services.
- ✓ Comprehensive operation is an inevitable trend in the future.

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Next step to sustain the development trend



➤ Deem innovation the driving force

As the driving force for success, innovation shall not be denied because of the crisis

- ✓ **Financial innovation is a double-edged sword.**
- ✓ Innovation is always the driving force for the past, current and future development of the banking industry. Financial innovation built the continual financial advantages of Europe and US economy.
- ✓ Financial innovation also created technical bubbles and real estate bubbles, gave rise to evident fluctuations in the process of economic and financial development. However, financial innovation shall not be denied because of the aforementioned risks.

Innovation of management, systems, products and services

- ✓ **China's banking industry needs more innovation.**
- ✓ There is plenty of room for innovation in terms of corporate governance and institutional construction so as to further improve operating efficiency.
- ✓ There is substantial room for innovation in terms of financial products and service approaches in order to change the unitary financial market structure and better support economic development.

➤ Guarantee realization of goal by risk control

Banks shall timely update their risk management

- ✓ Risk management of banks must adapt to the development of financial innovation.
- ✓ Ensure that financial innovation is understood by banks.
- ✓ Ensure that financial innovation is made based on the needs for development of real economy and the customer demands.
- ✓ Ensure that risks of financial innovation are under control of banks.

Banking regulation shall be strengthened

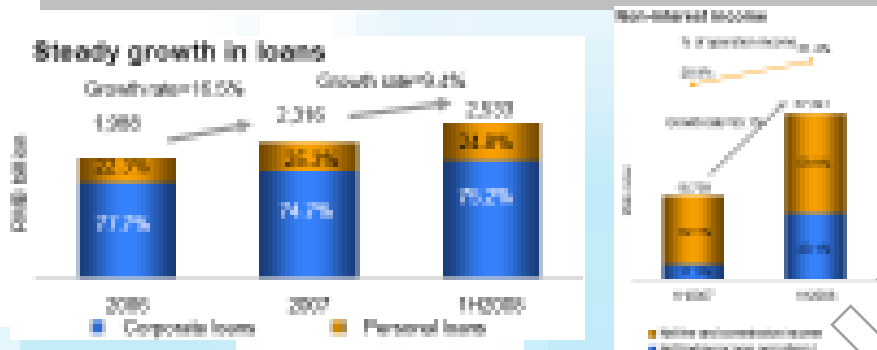
- ✓ Banking regulation must adapt to the development of financial innovation.
- ✓ Ensure that banks have adequate capitals to cover the innovation risks.
- ✓ Ensure that banks disclose adequate information about innovation businesses.
- ✓ Ensure that innovative businesses of banks meet the various regulatory standards.

Bank of China: Delivering Growth and Excellence

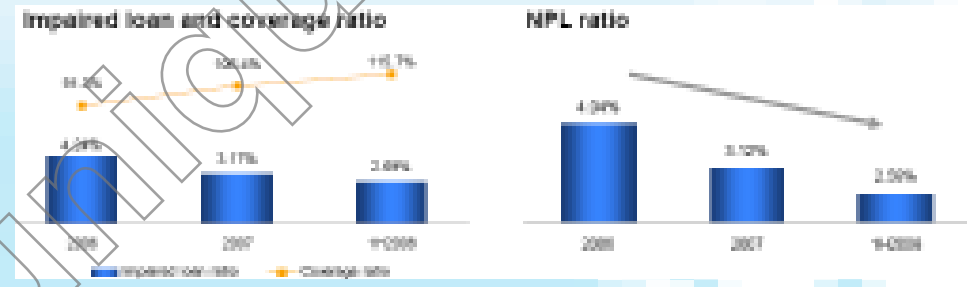


➤ Up to H12008, BOC has made fast and sound growth

Fast Growth



Sound Asset Quality



➤ Delivering Growth and Excellence, Becoming Leading Global Bank

Based on mainland, serving for global customers

- ✓ In the Chinese Mainland, BOC had a total of 37 tier one branches, 283 tier two branches and 9,824 outlets.
- ✓ BOC had built up an extensive international network of 689 institutions in Hong Kong, Macau and 26 overseas countries and regions with 22,000 staff by the end of 2007.

Delivering growth and excellence, Aiming to be leading global bank

- ✓ To be the most internationalised bank in China
- ✓ To be the strongest global bank in Asia-Pacific Region
- ✓ To be the biggest international settlement and trade financing bank of the world

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Thank You!

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